

Quantification of tax relief in the Czech Republic for 2021

1 Description of the methodology

The American Tax Foundation defines tax expenditures as a deviation from the "normal tax code" that reduces the tax burden on individuals or businesses through an exemption, deduction, credit, or preferential rate¹. Expenditures can lead to significant losses of public revenue and make subsidy or transfer schemes opaque, i.e., the actual amount of the redistributive and allocative function.

Although the methodology for calculating tax relief is not harmonised, the European Commission makes certain recommendations which are reflected in the following text. For the calculation of tax relief in the Czech Republic, the **foregone revenue method** has been chosen. Its principle is to quantify the reduction in revenue achieved by the application of a given relief if the taxpayer makes use of the tax relief. It is a static calculation of the loss of public sector revenue, which does not take into account changes in the behaviour of entities. If a tax credit is abolished, entities may change their behaviour, which may lead to a different impact on public budgets.

At the same time, if any of the tax breaks were removed, this would not automatically mean that public revenue

would increase by the estimated amount. Indeed, the calculation of the amount of tax relief does not take into account, given the lack of knowledge of individualised data, the possible interdependence between tax reliefs. Taxpayers may take advantage of other tax reliefs, may shift their activity to a different area or may be completely deterred from any activity by the omission of the relief. Furthermore, particularly in the case of exemptions, the actual amount of tax would also be affected by the construction of the claimable expenditure. Thus, the overall impact of the removal of the exemption may actually be lower.

In general, a lot of data is needed to determine the amount of each tax credit. This poses a problem in procuring the data base, as in many cases it would lead to a disproportionate increase in the administrative burden on the entities concerned. Although the revenue foregone method used is not data-intensive either, it is relatively simple compared to other methods and is therefore also the most widely used method.

2 Amount of tax relief

It is not possible to quantify all the tax breaks included in the Czech tax system. The main reason for this is the absence, unavailability or incompleteness of the necessary data and the potentially disproportionately high administrative burden, especially compared to the impact of the amount of reliefs identified. In view of this, only those tax concessions for which available data were known were quantified. At the same time, only those whose potential impact on public budgets exceeds the amount of CZK 100 million remain to be analysed.

The Automated Tax Information System, to whose aggregated version the Ministry of Finance has access, was used to calculate the amount of tax relief in most cases. Other sources were publicly published and internal reports of the relevant institutions.

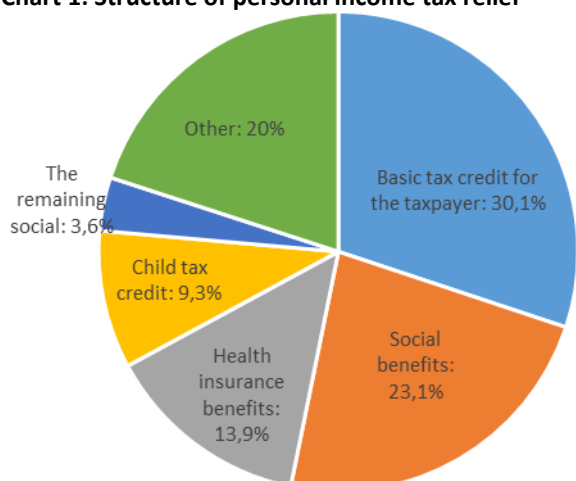
The following is a quantification of the amount of tax relief for 2021 on an annual basis on income tax and value added tax.

2.1 Personal income tax

The analysis of tax relief on personal income tax for 2021 shows that out of the total CZK 443.2 billion, CZK 252.5 billion were tax exemptions, CZK 9.6 billion were items reducing the tax base and CZK 181.1 billion were items reducing the tax (Table 1). As high as the total amount of tax relief may seem, it is important to note that 80% of the relief consisted of social items (see Chart 1). The most significant was the basic tax rebate for the taxpayer itself (over 30%), followed by exemptions for social benefits from public insurance schemes, state social assistance and material need (in aggregate 23%), with tax benefits for children accounting for a further more than 9%. The Czech Republic also exempts benefits from public health insurance (almost 14%).

¹ <https://taxfoundation.org/taxedu/glossary/tax-expenditure/>

Chart 1: Structure of personal income tax relief



Source. Calculations of the Ministry of Finance of the Czech Republic.

Table 1: Personal income tax relief in 2021 (CZK billion)

Category	Name of tax credit	§ ZDP	Above
Tax exemption	Exemption from pension benefits and services	§ 4	79,6
	Exemption from public health insurance	§ 4	61,5
	Exemption for raffle and gambling winnings	§ 10	72,7
	Exemption from state social support benefits	§ 4	7,5
	Exemption of the value of meals provided by the employer (for consumption at the workplace or through other entities)	§ 6	7,1
	Exemption from sickness insurance benefits	§ 4	7,8
	Exemption from social care benefits and income from caring for a close person	§ 4	4,9
	Exemption of benefits from personal insurance except for one-off benefits	§ 4	2,1
	Exemption from the application of state employment policy instruments	§ 4	1,5
	Exemption from material hardship benefits	§ 4	0,8
	Exemption of employer's contribution to an employee's supplementary pension scheme or supplementary pension savings	§ 6	2,0
	Retirement benefits and service housing allowance for professional soldiers and retirement entitlements for members of the security forces	§ 4	1,4
	Exemption of social services	§ 4	1,5
	Exemption of benefits from FKSP, social fund and profit	§ 6	1,9
	Exemption from scholarships	§ 4	0,4
	Items reducing the tax base	Interest on housing finance loans	§ 15
Contributions to private life insurance		§ 15	1,1
Contributions to supplementary pensions, insurance and supplementary pension savings		§ 15	1,3
Donations for public benefit activities		§ 15	1,2
Exemption from blood or organ donation		§ 15	0,3
Tax-reducing items	Basic tax credit for the taxpayer	§ 35ba	133,3
	Child tax credit (tax credit and tax bonus)	§ 35c	41,1
	Spouse tax credit	§ 35ba	4,6
	Child Placement Tax Credit	§ 35ba	1,5
	Student tax credit	§ 35ba	0,4
	Disability tax credit	§ 35ba	0,2
Total			443,2

Source. Calculations of the Ministry of Finance of the Czech Republic.

Note: Sum differences are due to rounding.

2.2 Corporate income tax

Tax relief on corporate income tax amounted to around CZK 15 billion in 2021 (Table 2). Exemptions amounted to CZK 1.1 billion, items reducing the tax base amounted to CZK 4.5 billion, items reducing tax amounted to CZK 4.1 billion, and we estimate the impact of reduced tax rates at CZK 5.3 billion.

However, the calculation of the tax relief does not include the exemption of income from profit sharing between the

subsidiary and the parent company due to the unavailability of the data needed for the calculation. However, the inclusion of this item in the tax relief is questionable. It is a distribution of profits that have already been taxed once. The amount of this item can be estimated at tens of billions of crowns, which is higher than the list of other corporate tax reliefs presented here.

Table 2: Corporate income tax relief in 2021 (CZK billion)

Category	Name of tax credit	§ ZDP	Above
Tax exemption	Exemption from the revenue of the State Institute for Drug Control and the Institute for State Control of Veterinary Biopreparations and Medicines	§ 19	0,2
	Exemption from contributions to the Czech Insurers' Bureau fund	§ 19	0,2
	Exemption from the income of the Deposit Insurance Fund, the Guarantee Fund and the Reinsurance Fund	§ 19	0,2
	Exemption of income from financial market operations with treasury funds	§ 19	0,5
Items reducing the tax base	Deduction of expenditure on science and research	§ 34	2,4
	Deduction to support vocational training	§§ 34(4); 34f-h	0,2
	Deduction for public benefit taxpayers	§ 20	0,6
	Donations for public benefit activities	§ 20	1,2
Tax-reducing items	Investment incentives	§§ 35a, 35b	2,3
	Tax credit for employing people with disabilities	§ 35	1,3
	Tax credit for employing people with severe disabilities	§ 35	0,5
Reduced tax rate	Reduced tax rate for investment funds	§ 21	2,9
	Reduced tax rate for pension funds	§ 21	1,3
	Reduced tax rate for mutual funds	§ 21	1,1
Total			15,0

Source. Calculations of the Ministry of Finance of the Czech Republic.

Note: Sum differences are due to rounding.

2.3 Value added tax

In order to accurately calculate the amount of value added tax relief, it is necessary to know whether the supply provided by the taxpayer is intended for a VAT payer or a non-taxpayer. However, such detailed information is not available and we can only rely on the data on the amount of supplies received by non-taxpayers contained

in the tables of supplies and uses published by the Czech Statistical Office.

Non-taxpayers include households, the public sector and exempt sectors under the Value Added Tax Act. This leads to inaccuracies in the calculation of the amount of tax relief.

Table 3: Value added tax relief in 2021 (CZK billion)

Category	Name of tax credit	§ ZDPH	Above
Tax exemption	Exemption from renting immovable property	§§ 51, 56a	147,6
	Exemption for financial activities	§§ 51, 54	
	Exemption of insurance activities	§§ 51, 55	
	Exemption from lotteries and other similar games	§§ 51, 60	
	Exemption from the basic postal service and delivery of postage stamps	§§ 51, 52	
Reduced tax rate	Reduced tax rate	§§ 47 - 49	72,8
Total			220,4

Source. Calculations of the Ministry of Finance of the Czech Republic.

3 Conclusion

The aggregate amount of tax relief in the Czech Republic is difficult to quantify. Individual tax reliefs influence each other and it is not methodologically correct to simply add up the amount of tax reliefs quantified. On the other hand, this analysis can serve to outline the overall distortions caused by the current tax system.

Given the foregone revenue method and the static approach used, the **individual amounts of tax relief quantified do not simultaneously represent an estimate of the increase in tax revenue that could be achieved if they**

were abolished. In fact, it is likely that in the case of several changes in tax reliefs at the same time, the behaviour of the actors will change, which, combined with the interdependence of some reliefs, will lead to a different impact on public budgets. Thus, the overall impact of the abolition of exemptions is likely to be smaller than the isolated static impact.

In the following table, a simple summation of the quantified tax relief amounts is made to obtain a rough estimate of the total distortions caused by the current tax system setup.

Table 4: Aggregate amount of estimated tax relief for 2021 (CZK billion)

Category	DPFO	DPPO	VAT
Tax exemption	252,5	1,1	147,6
Items reducing the tax base	9,6	4,5	-
Tax-reducing items	181,1	4,1	-
Reduced tax rate	-	5,3	72,8
Total	443,2	15,0	220,4
Total for the year	678,6		

Source. Calculations of the Ministry of Finance of the Czech Republic.