

THE ELECTRONIC RECORD OF SALES AS AN EFFECTIVE TOOL FOR FAIR COMPENSATION PAYMENTS TO ENTREPRENEURS

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Abstract: The electronic record of sales is a tool used by 17 Member States in the European Union. Yet the Czech Republic has decided to cancel the measure introduced in 2016 without providing any replacement. Since its introduction, electronic record of sales has been a political issue and its promoters have failed to convince the professional and lay public of its usefulness. Our article therefore aimed at evaluating the use of electronic record of sales in the Czech Republic while suggesting further possibilities of its use. We particularly focused on the period of the COVID-19 pandemic which was specific in that many entrepreneurs became financially dependent on state aid overnight. While the state had designed compensation schemes to help entrepreneurs, there were many challenges during the application and drawdown process that complicated and delayed the targeted assistance. For a more objective assessment, we used a comparison with other EU countries. We found that the level of aid offered was comparable to the Czech Republic, but that the process of usage may have operated in a non-targeted manner and was complex in terms of bureaucracy. Subsequently, we proposed that the state should have used the data it had available from entrepreneurs since 2016. It involved electronically recorded sales. The totals for a particular entrepreneur was making it possible to determine what impact the restrictions had on his/her business and to provide him/her with an adequate amount within a quite automated compensation process.

Keywords: COVID-19, EET, electronic record of sales, ERS, compensation payments

JEL Classification: H20, O16, O21

INTRODUCTION

The electronic record of sales (the 'ERS') was splitting up the professional and lay public even before it was introduced in 2016 for what was termed 'wave 1 of entrepreneurs', more specifically, those active in accommodation and dining segments. The reason why the then government coalition pushed for the introduction of this measure was to straighten out the business environment in sectors where payments were made purposely in cash¹, without properly issued receipts, and thus presumably without proper income taxation (Radvan, 2013).

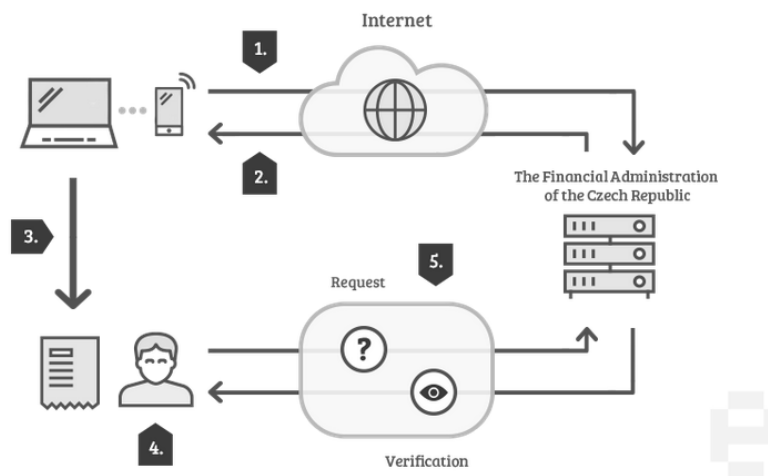
It was estimated that the state was losing up to 160 billion CZK per year (Financial Administration of the Czech Republic, @2016-2022b). Income concealment is not a new phenomenon; indeed, the behaviour can be found in countries other than the Czech Republic (e.g. Artavanis et al., 2016; Kasipillai et al., 2000; Medina

¹ There was no digital footprint for cash payments.

& Schneider, 2019). This is why multiple countries are looking for ways to prevent this fraudulent activity since straightening out the business environment is a very important state measure which, if it fails, or even if the state waives the application of it, can cause irreversible changes in the behaviour of all market actors (Semerád et al., 2022). As dishonest entrepreneurs gain a competitive advantage over honest entrepreneurs², the latter group is left with only two options: Either close the business or adapt to the unfair practices (Le Bon, 1896; Torgler & Schaltegger, 2005).

That is why the Czech Republic was looking for a way to push dishonest entrepreneurs to declare and tax their income properly. Inspiration was drawn from best practices in some EU Member States (particularly Croatia). It was about the electronic record of sales. The system is based on the principle (Figure 1) that a business receiving a cash payment³ is required to register the sale with the tax authorities within 48 hours; the communication between the payee and the payment recipient takes place online using remote communication (1.). Information about the receipt of payment can be sent from any device connected to the internet (e.g. computer/smartphone).

Fig. 1 The electronic record of sales



Source: Financial Administration of the Czech Republic (@2016-2022a)

The sale is now registered by the tax administrator, receiving unique codes (BKP – Taxpayer's Security Code and FIK – Fiscal Identification Code) that uniquely identify the transaction. These codes are now sent to the payee's device (2.) and the payee prints them on the tax receipt/cash receipt (3). The entire exchange of information is automatic and takes no more than a few seconds.

To motivate customers (clients/guests) to accept the document (4.), the tax administrator ran an awareness campaign (TV and radio spots) before and during the introduction of the electronic record of sale. During the campaign, the Ministry of Finance of the Czech Republic explained the reasons for the introduction of the sales recording system and presented estimates of increased tax revenues. In addition to checking whether or not the tax document was registered (5.), customers could participate in a lottery (called *Účtenkovka*, i.e. 'Receipt Lottery') in which they could win financial and material prizes.

In our opinion, it is a pity that the state was not able to convince the professional and lay public of the usefulness of this measure in the long term even in this way. Instead, the electronic record of sales became a political issue that led to clashes of opinion between 2016 and 2022 resulting in political statements in which

² For example, they can afford to offer their products and services at lower prices.

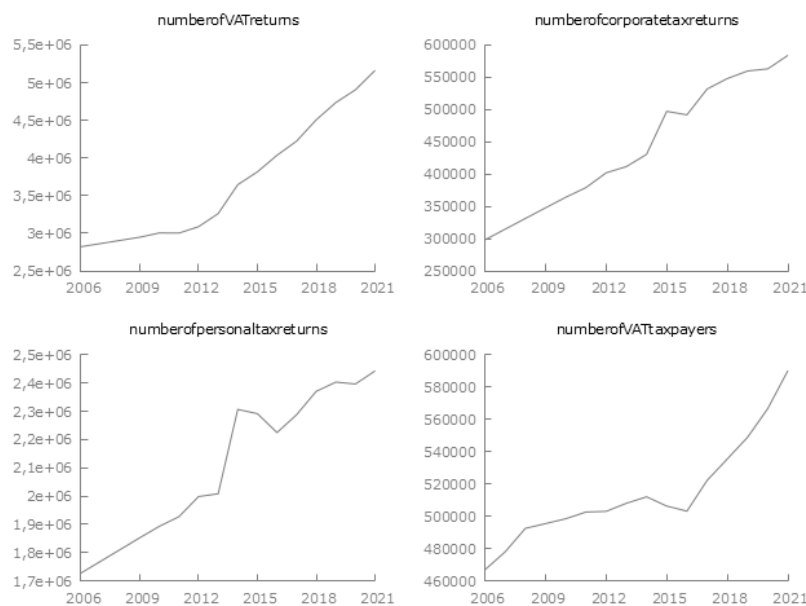
³ The obligation to record payments by credit cards was cancelled on 1 March 2018.

politicians who introduced the ERS defended it and opposition politicians (the current government parties) promised to cancel it (Government of the Czech Republic, 2022).

They argued that the ERS introduction would increase the bureaucratic and financial burden on entrepreneurs, sensitive data were being collected on entrepreneurs and in developed economies no such registration systems existed (e.g. ODS, 2016).

They also argued that the burden of paperwork was increasing on the part of entrepreneurs. This may be true, especially if these entrepreneurs had not needed an internet-connected computer for their work until that moment. But as Boháč (2018) argues, businesses should not be protected at the cost of reduced tax revenue, as taxes are a contribution to the running of public matters. At the same time, arguing is possible through the fact that some form of sales record – whether online or offline – is in operation in 17 EU countries (Financial Administration of the Czech Republic, @2022).

Fig. 2 Development of selected VAT and income tax indicators in 2006–2021



Source: Authors' compilation

Note: The x-axes show the years 2006 to 2021; the y-axes show the number of VAT (*numberofVATreturns*) and personal income tax returns (*numberofpersonaltaxreturns*) in millions, the number of corporate income tax returns (*numberofcorporatetaxreturns*) and the number of VAT payers (*numberofVATtaxpayers*), followed by the inflation rate in % and GDP growth; the resulting curves show the revenues from taxes collected in billions of CZK.

Another counter-argument was the statement that electronic sales records would not bring the desired tax revenue. This was also examined, for example, by Pisková & Semerád (pending reviewer procedure). Using the example of the accommodation services segment and data from the Czech Statistical Office, the authors demonstrated that the introduction of an electronic record of sales contributed to an increase in:

- the number of registered accommodation establishments;
- the number of disclosed admitted guests and the extension of the reported average length of stay;
- the average accommodation prices in individual regions; and
- the sales recorded – which led to an increase in the number of value-added taxpayers.

In this respect, it is useful to put the above in an economic context. The ERS and, along with it, the

establishment of the Control Statement⁴ (CS) in the area of value-added tax, both were implemented in a period of low inflation rate (roughly up to 1%) and relatively low GDP growth (roughly 4%).

In the period following the introduction of the ERS and CS, the number of VAT and personal/corporate income tax returns filed increased significantly, which was generally expected. In this respect, it should be emphasised that the growth in the number of VAT payers and the number of VAT returns filed was extreme compared to the previous period. The above is summarised in Figure 2.

In the year of the introduction of the ERS and CS, GDP was around 4.8 billion CZK; by 2021 it increased to roughly 6.1 billion CZK, i.e. by roughly one-third compared with 2016. Curiously, GDP growth increased from around 4% to 6% after the introduction of the ERS and CS. A negative circumstance that followed the introduction of ERS and CS is the rise in the inflation rate. However, the growth in the inflation rate could also have been affected by the growth in the money supply as the Czech National Bank's (CNB) foreign exchange interventions in the form of the CZK 27/EUR exchange rate fixation came to an end.

Marethová & Snopková (2018) identified the increase in revenue and the resulting growth in the number of new VAT registrations as one of the significant benefits of sales recording. The Ministry of Finance of the Czech Republic itself (2019) published that the net benefit of the ERS was 7.9 billion CZK in 2017 and 12.3 billion CZK in 2018.

A major change in the electronic record of sales occurred during the COVID-19 pandemic. Initially, businesses were divided into four groups and these groups were required to record sales from different dates. While the first two groups⁵ started recording sales on the scheduled dates, there was a gradual delay for the remaining two groups. For example, due to the repeal of part of the Act on Electronic Record of Sales by the Constitutional Court of the Czech Republic (2017), the start date was postponed until 1 May 2020.

At that time, however, a state of emergency was in force in the Czech Republic, and as many establishments were closed, the deadline for mandatory registration was postponed until 1 January 2023 (Financial Administration of the Czech Republic, 2020). At the same time, the obligation to record sales for the first two groups was discontinued. In our opinion, however, the discontinuation of the electronic record of sales was not purposeful and, from this point of view, makes no sense.

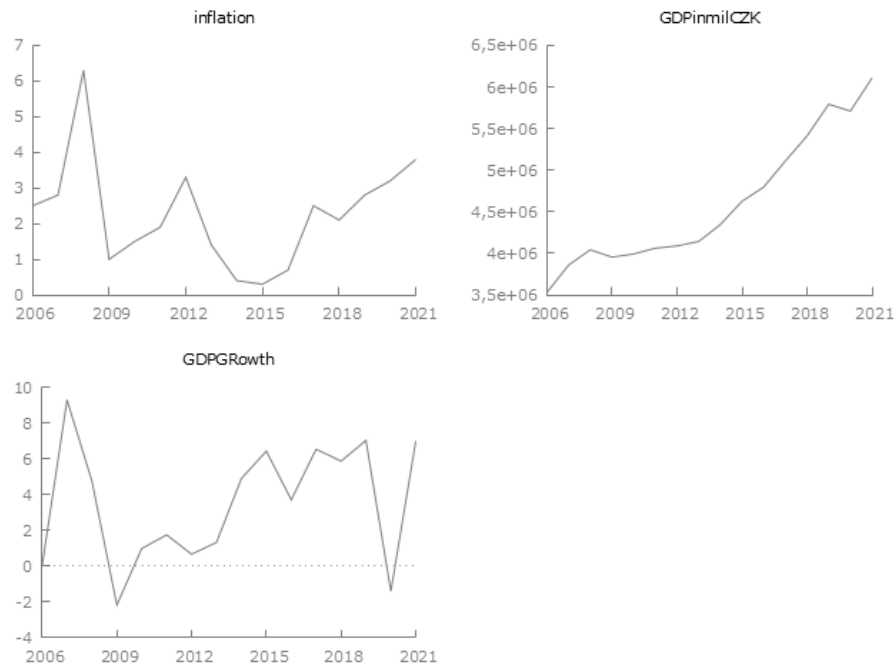
According to the government coalition, the introduction of the ERS aimed to straighten out the market environment, while the unitary nature of the ERS for each of the waves was basically to level the playing field for business entities on the market, as they were all supposed to record sales.

Therefore, as the recording of sales was interrupted, then in principle the ERS has been deprived of its initial purpose and the effect of straightening out the market environment disappeared. In essence, the ERS also meant the electrification of business entities, as they were connected to the internet, which allowed customers to use the cashless payment for goods or services.

⁴ The Control Statement was introduced in 2016 as a tool for continuous detection of discrepancies and fraud in value added tax. For more information on how it worked, see e.g. Semerád & Bartůňková (2016).

⁵ Entrepreneurs in dining and accommodation services and entrepreneurs in retail and wholesale trade.

Fig. 3 Development of selected macroeconomic indicators in 2006–2021



Source: Authors' compilation

Note: The x-axes show the years 2006 to 2021; the y-axes show the inflation rate in % (*inflation*), the size of GDP in CZK million (*GDPinmilCZK*) and GDP growth in % (*GDPGRowth*).

The interruption and subsequent cancellation of the ERS may mean, as is evident in some businesses – especially in the hospitality and retail sectors – that they are switching to cash payments and abandoning cashless payments (Moniová, 2022).

In other countries – e.g. Germany introduced the obligation to record sales from 1 January 2020 – there was no interruption in the recording. Thus, even during a pandemic, states gained valuable information on the economic activities of entrepreneurs and had continuous data on the impact on their entrepreneurs, allowing them to pay aid and compensation more efficiently.

Our article therefore aimed at evaluating the use of electronic record of sales in the Czech Republic while suggesting further possibilities of its use. We particularly focused on the period of the COVID-19 pandemic which was specific in that many entrepreneurs across the world became financially dependent on state aid overnight (e.g. Belitski et al., 2021; or Razumovskaia et al., 2020). For this reason, we also evaluated the way in which compensation was paid to entrepreneurs in the Czech Republic, comparing it with selected EU countries. Based on our findings, we proposed recommendations for amending the system so that the compensation could be paid more efficiently and fairly based on the past activities of the entrepreneur and without unnecessary administrative requirements.

1. METHODOLOGY

In our paper, we used a method of analysis to determine how compensation payments were paid to businesses during the COVID-19 pandemic period (March 2020 to April 2022). At the same time, through data collection and content analysis, we investigated how compensation was paid in selected EU countries to measure the efficiency, speed, formal complexity and fairness of compensation payments using a comparative approach. As we have identified (unnecessary) difficulties in the Czech Republic, we have proposed more efficient and fairer procedures for compensation payments, which can as a side benefit

motivate taxpayers to keep proper records of sales not only in periods when compensation is paid.

The data used in this article were obtained from publications of the Ministry of Finance of the Czech Republic, which contain the monthly values of the state budget's current performance in individual years starting from 2006 and ending in 2021. To capture relevant information, only aggregated data for the whole calendar year were included, i.e. the cumulative value of the current performance of the selected indicator as of 31 December of a given year (Ministry of Finance, 2022).

Any corrections made by the Ministry of Finance of the Czech Republic in a later period were not included in the data for the year in question, as the authors felt that such corrections were not significant. These were corrections of no more than a few billion CZK. In addition, data on income tax and VAT returns from the statistics of the Financial Administration of the Czech Republic (@2022b) were used for the analysis.

The data on the number of VAT payers included in the authors' analysis was applied by taking the value of the first days of the following calendar year into account as this, according to the authors, corresponds more closely to the actual number of payers for the given calendar year. As regards the number of income tax and VAT returns filed, this is the number of tax returns filed by 31 December of the year in question. If the return was filed from 1 January of the year in question onwards, then these returns were included in the statistics for the year in which the return was filed. Summary statistics are available upon request from the authors.

The data were analysed in Gretl, a multiplatform econometric analysis software package written in the C programming language. It is free and open-source software. It may be distributed and/or modified under the terms of the GNU General Public License (GPL) as published by the Free Software Foundation (Gretl, 2022). This program allows, among other things, to plot multiple graphs involving time series, which the authors used in their analysis.

2. RESULTS AND DISCUSSION

The turn of February and March 2020 has had a huge impact on the daily lives of people around the world. The disease, which has spread uncontrollably across the planet, has not only caused millions of deaths but there have also been significant encroachments on human rights and freedoms (Forman & Kohler, 2020).

Not only was the movement of the population restricted to the minimum necessary (e.g. for shopping and occupational purposes), but shops and establishments were also closed. Only shops with essential goods such as groceries, drugstores and pharmacies continued to be open (Ministry of Industry and Trade of the Czech Republic, 2020), along with online stores. For some activities, such as the operation of restaurants, it was possible to sell through a serving hatch. Other shops and services had to remain closed to prevent the spread of COVID-19.

These measures have affected most entrepreneurs and, logically, members of the community addressed the Czech Government to help them overcome these difficult times. The Government of the Czech Republic (2020; 2021) satisfied these demands and introduced across-the-board programmes for entrepreneurs, mostly based on a form of cost-recovery contribution:

Examples include *Antivirus A* – later designated as *Antivirus Plus* (contribution of 80%, but not more than 39,000 CZK per employee and month) and *Antivirus B* (contribution of 60%, but not more than 29,000 CZK), through which the state contributed to employers to co-fund the wage costs of employees who found themselves quarantined, isolated or prevented from working, or if the employer had to limit its operations (Ministry of Labour and Social Affairs, 2022).

Another programme was *Covid 2021*, for which entrepreneurs who proved that their turnover had fallen by at least 30% in the applicable period were eligible. The amount of aid was calculated as the product of 300 CZK times the number of employees in employment (converted to full-time equivalents).

Businesses that also demonstrated a decrease of at least 30% from the same period in 2019 were eligible for the *Covid – Uncovered Costs* subsidy scheme. The aid amounted to 40% of the uncovered costs with a maximum limit of 20 million CZK per applicant. However, this scheme could not be combined with the

compensation bonus.

The compensation bonus was intended for self-employed persons and partners of selected limited liability companies⁶. The amount of the compensation bonus was set at 500 CZK and later increased to 1,000 CZK (for more information, see Financial Administration of the Czech Republic, 2022).

While the above subsidy schemes had a maximum (or as evidenced) amount available to everyone, the state also issued calls for proposals for which it allocated a maximum amount for which all applicants competed. Examples include the *COVID-Rent* scheme calls. Compared to the previous programmes, the *COVID-Rent* scheme posed one major challenge for payers. If the recipient of the aid was a VAT payer, then the aid had to be included in the tax base (it was a subsidy to compensate for the rent price) and VAT had to be calculated on this. At the end (unless agreed otherwise with the tenant) the landlord did not receive the full amount of the aid, but only part of it less VAT. This way the aid thus established had at its core a disproportionate impact on the beneficiaries.

Based on publicly available data, several problems occurred during the disbursement and payment of individual state aids:

- The public administration servers were overloaded as the applications were submitted (Barták, 2021).
- Entrepreneurs did not know what type of aid they were entitled to and when (Hovorková, 2020).
- The manager of the compensation bonus in some cases did not follow the methodological setting (Morávek, 2022).
- Aid payments were delayed (Petr, 2021).
- There were speculations as to whether the compensation payments were effective, as one of the largest beneficiaries of the aid involved casinos and gambling firms (Mačí & Nohl, 2022).
- There were also suspicions of undue use of aid; these involved, for example, entrepreneurs who received the aid but operated their businesses without restrictions (Semerád et al., 2021).
- The application process was also demanding in terms of bureaucracy, resulting in applications from eligible entrepreneurs not being granted (Diro, 2021). For example, around 70% of applications for part-time jobs (*kurzarbeit*) were rejected by the authorities because they were filled in incorrectly (Frolík, 2020).

As can be seen from these examples, the disbursement of aid during the COVID-19 pandemic¹⁹ was preceded by a lot of administrative steps and mandatory evidence on the part of the entrepreneurs and in some cases their applications were unjustifiably rejected due to formal shortcomings, making it meaningful to look at whether these problems could have been tackled more effectively, in a more targeted way and without unnecessary red tape burden as what did not work in the Czech Republic was applied effectively by other countries.

If we look at some of the EU countries, they paid compensation as well, ranging from 50% to 80% of the costs – such as Austria, Poland and Germany, for example. The amounts depended on sales or turnover for the previous period (Ministry of Industry and Trade of the Czech Republic, 2020b). In this respect, the Czech Republic followed a comparable approach. However, subsidies abroad, e.g. in Germany, were granted to cover fixed costs and thus enable firms to survive (FinTag, 2020).

Unlike the Czech Republic, for example, in the UK the whole application process operated in such a way that the British tax administration contacted the taxpayers who were entitled to receive compensation themselves (Židek, 2020). This is in line with the European Parliament's proposal (2021), which recommends that the Member States reduce red tape as it hinders small businesses from thriving.

⁶ Outside the focus of this article, the above scheme also covered persons working under the agreement to perform work or agreement complete a job.

3. SUGGESTIONS AND RECOMMENDATIONS

Aware of the requirement to reduce the red tape burden, we have focused on more effective support for entrepreneurs from the state. Our proposal can also be used in other cases where business is restricted or banned and entrepreneurs cannot operate in the long term without state assistance because of these restrictions.

We also recognise that every new measure brings costs along with it on the side of businesses and public authorities. Ideally, the design elements that are already available and can be extended to other groups should be used with more efficiency.

Our suggestion, therefore, is that the state should have used the ERS to allocate the subsidies. The tool was introduced for individual groups from 1 December 2016 onwards, which is a sufficiently long time to monitor the development of sales (turnover) of entrepreneurs in individual sectors.

According to the authors, the state should have also taken into account payments received by payment card and bank transfer in this measure. This way it could provide, in a targeted and relatively automated manner, aid to specific entrepreneurs who were eligible.

In addition, the obligation to provide evidence of income for the previous period would be eliminated, as the tax authority had relatively sufficient documentation that could be used for entrepreneurs who recorded their sales, whether they did it compulsorily (dining and accommodation services, retail and wholesale businesses) or voluntarily.

By looking at the aggregated data of selected tax revenues of the state (Figures 4–6), it was possible to focus on the major types of tax revenues and determine the amount of aid for businesses from these. As mentioned, the aid for business entities was designed quite differently, and it entailed a considerable financial and personal burden on the applicants for aid. Last but not least, it is necessary to mention that the aid so designed partially paralysed the activities of the financial administration, which had to process and evaluate hundreds of thousands of applications for aid beyond the scope of its normal activities. In the field of VAT, there was a significant increase in the number of taxpayers; however, the growth in the collection of this tax does not look quite adequate compared to income taxes.

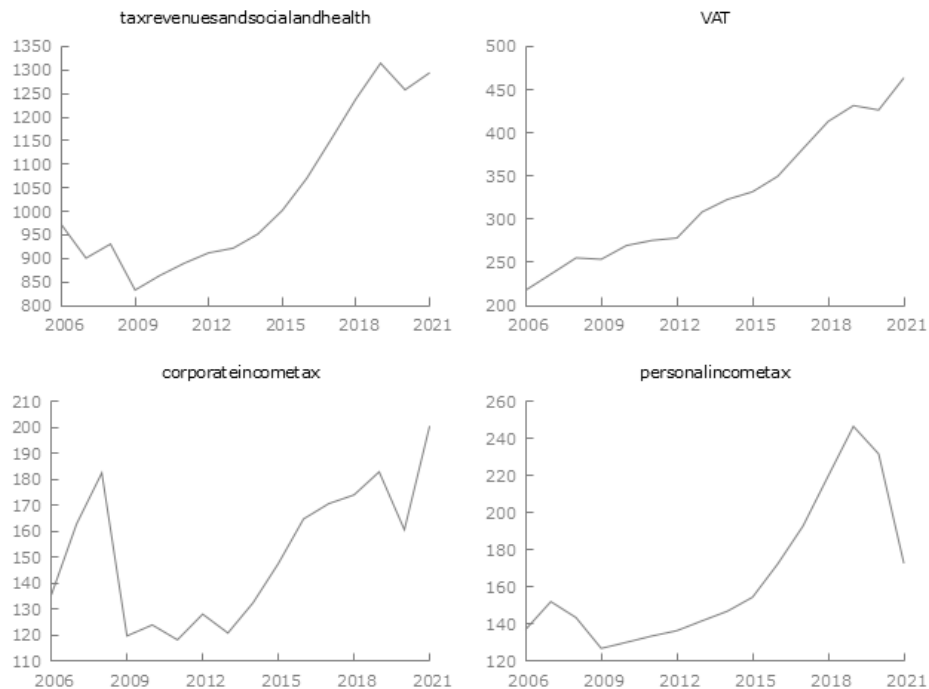
The advantage of this procedure would be that the state administration would show opponents of the electronic record of sales that the system is not a political instrument and that it is not intended to restrict the business environment. Indeed, it was possible to use to provide targeted assistance to entrepreneurs at times when they needed financial help from the state due to unforeseen influences.

In addition, the fact that the payment of compensation would come automatically without the need to prove the relevant facts is benefitting the entrepreneur when recording sales. This would provide aid without delay. Entrepreneurs would thus not be placed in unnecessary financial difficulties and would not bear the costs of establishing the relevant facts, especially in the form of the costs of consultancy and the submission of applications for aid as such.

Another significant benefit for both taxpayers and the state administration is that taxpayers are influenced to declare their sales properly since if they record all their sales, the state will provide them with adequate compensation. Conversely, if they cheat, they risk receiving aid only to some extent, which compensates them for losses only up to the amount of the sales declared. Such an approach would have a major educational effect on the business environment.

However, this would mean that the state would maintain the ERS and would not discontinue this obligation during the COVID-19 pandemic. It would thus provide adequate aid to those who did not have the opportunity to execute their own business activities and could distinguish them from those (e.g. online stores) whose sales did not fall or, on the contrary, increased.

Fig. 4 Development of the most important tax revenues in the period 2006–2021



Source: Authors' compilation

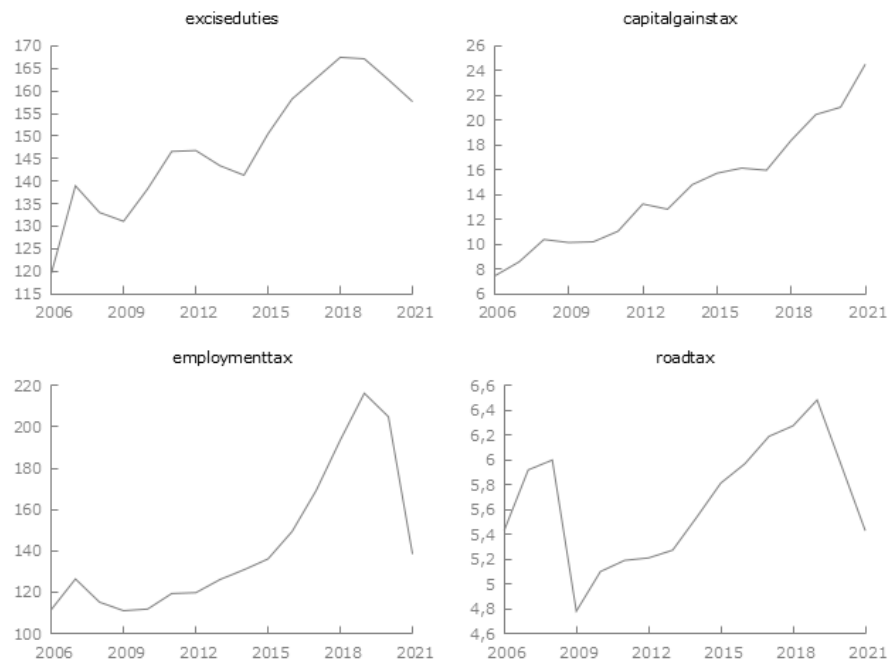
Note: The x-axes show the years 2006 to 2021, and the y-axes show the values of revenue from selected types of taxes in CZK billion (Tax Revenues and Social and Health – *taxrevenuesandsocialandhealth*; Value Added Tax – VAT; Corporate Income Tax – *corporateincometax*; Personal Income Tax – *personalincometax*).

Instead, the Czech Government discontinues the ERS system, removing an efficient tool that not only cultivates the environment and increases tax literacy, but is also one that a large number of entrepreneurs already use (even voluntarily) and for which they have built infrastructure. Should the government change its view of the ERS and not consider it just a political tool of the current opposition parties, little would be necessary for the remaining entrepreneurs from the third and fourth waves to join the system. If the government wanted to, it could amend the law to satisfy its voters and continue to use this measure.

The cancellation of the ERS can be described as a backward step, as the government has no suitable alternative in hand. For this reason, it can be assumed that market conditions are going to return to pre-2016 conditions with the customer being challenged by a question of whether they want to issue a tax receipt and pay the amount plus VAT or save and pay the amount, VAT excluded.

In addition, public money will be wasted because the funds invested in the electronic record of sales system as such have been spent unnecessarily, as no one will use the tool anymore.

Fig. 5 Development of tax revenues for excise and capital taxes, including employment tax and road tax, 2006–2021



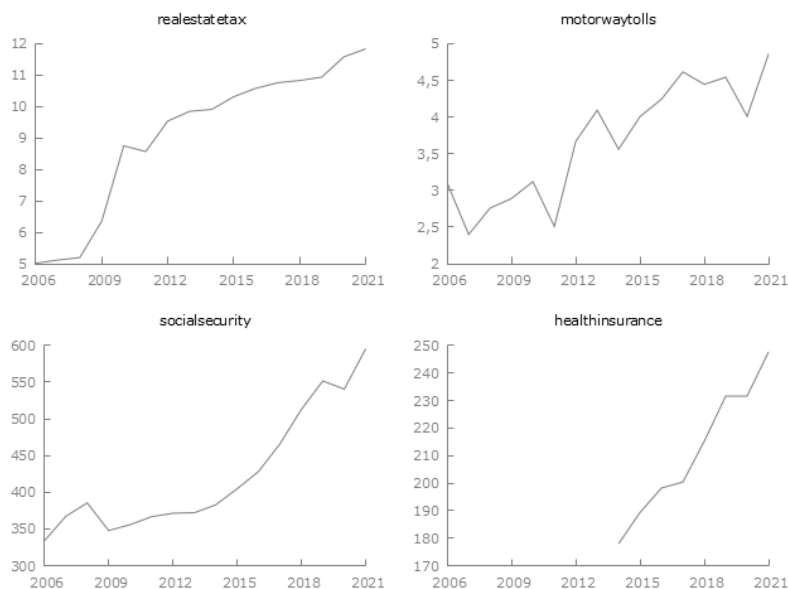
Source: Authors' compilation

Note: The x-axes show the years 2006 to 2021, and the y-axes show the values of revenue from selected types of taxes in CZK billion (Excise Duties – *exciseduties*; Employment Tax – *employmenttax*; Capital Gains Tax – *capitalgainstax*; Road Tax – *roadtax*).

The discontinuation of the ERS is also an ill-conceived action with regard to the taxpayers who had purchased a recording device just and only because of the ERS. Unfortunately, this is just another signal of the foolish expectation of a stable business environment on the part of the state; such an environment is a basic prerequisite for the economic development of the Czech Republic. All changes and reforms will thus be valid only for the election period without a long-term prospect, while in the economic transformation of the Czech economy a long-term perspective is seen as one that is assumed to have positive effects on the future of the country.

Similarly, the Czech pension reform has had a similar fate as now the numerous populations born in the 1970s are waiting to see how their pensions will be funded, while without any reform, funding pension accounts seems unsustainable. We believe that conceptual and strategic changes should not be based on political party affiliation and that it is actually appropriate to look for ways to reward more effectively and fairly (meritoriously) those who properly perform their duties.

Fig. 6 Development of tax revenues for excise and capital taxes, including employment tax and road tax, 2006–2021



Source: Authors' compilation

Note: The x-axes show the years 2006 to 2021, and the y-axes show the values of revenue from selected types of taxes (*realestatetax* and *motorwaytolls*), social insurance (*socialsecurity*) and health insurance (*healthinsurance*) in CZK billion.

CONCLUSION

The electronic record of sales is a tool used by 17 Member States in the European Union. Yet the Czech Republic has decided to cancel the measure introduced in 2016 in full without providing any replacement. While this is certainly legitimate, in our opinion, abolishing this instrument is an ill-concept and risky action as it can be expected that the business environment will worsen in individual sectors with dishonest entrepreneurs gaining a competitive advantage by not issuing documents and not declaring sales.

Since its introduction, electronic record of sales has been a political issue and its promoters have failed to convince the professional and lay public of its usefulness.

In our article, we have therefore focused on how else the electronic record of sales could be used. The period during the COVID-19 pandemic, when many entrepreneurs became financially dependent on the state overnight, was a good example. Although the state prepared some compensation schemes to help entrepreneurs, there were many problems during the application and drawdown process that complicated and delayed the assistance.

To see how other countries fared during this period, we made comparisons with selected EU Member States. We found that the level of aid was comparable to the Czech Republic, but that the process of usage may have operated in a non-targeted manner and was complex in terms of bureaucracy.

Subsequently, we proposed that the state should have used the data it had available from entrepreneurs since 2016. It involved electronically recorded sales. The totals for a particular entrepreneur was making it possible to determine what impact the restrictions had on his/her business and to provide him/her with an adequate amount within a quite automated compensation process.

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