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TAX SYSTEM PERFORMANCE IN THE REPUBLIC OF SERBIA

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Key words: Tax reforms, taxation structure, tax principles, conformity with EU tax system.

Abstract: Determination of Serbia to join and integrate into European Union (EU) calls for further reforms in economic laws and standards, among which, taxation policy takes one of the top places. After many years of preparations and delays, the Republic of Serbia adopted a set of laws in the field of taxation policy. However, achieved results are not sufficient to provide full-fledged tax system consistent in its taxation structure and attractive to FDI.

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Introduction

Taxation policy possesses powerful instruments to stimulate development of an economy. Special attention in designing tax system should be given in lack of domestic savings in an economy. Persuading economic development of a country requires also such structure and design of a tax system which makes national economy attractive to international investors. In all cases in which the state came forward as a guarantor to foreign investors, tax system was the basic platform for attracting foreign direct investments (FDI).

Countries in transition, such as Republic of Serbia, must draw up a fiscal strategy where its basic performances would be stability, consistency of tax rates, tax relief and other benefits that will be contributive for domestic economic development and attractive for international investors. Given that the Serbia intends to become a member of the EU, it is necessary for the country to harmonize performances of tax system with the requirements of the European Union.

Ability to recognize performances of tax system of Republic of Serbia within European tax policy depends on a number of factors, out of which, we especially highlight stability of tax system, rates of tax burden, flexibility, encouragement of tax payers, development of market economy and even fair burdening of all social and economic structures (tax payers).

Principles and developments in tax system of Serbia

Tax revenues generated from legal entities and individuals play the most important role in financing public expenditures. Besides tax, budgetary revenues include custom duties, dues, contributions and benefits. Among fiscal revenues, the honorable place is taken by those taxes which make 70%-90% (Durovic-Todorovic et al., 2007) of the structure of public revenue. Our research tells us that the percentage share of taxes in the Republic of Serbia is at the level of developed countries.

Before we move to performances of tax system in the Republic of Serbia we should highlight the fact that there are other revenues besides fiscal ones (Table 1). These are revenues collected by the state not on the basis of fiscal

sovereignty, voluntary or on the basis of its own "economic" arrangement. This group of revenues, better known under the name of non-tax revenue, consists of the following: earnings from public loans, income from currency issue, income from state property, state-owned companies income, income from services rendered by state agencies, donations and other incomes.

The key components of fiscal system are tax system, system of excises, system of custom duties, of dues, benefits and contributions. Contemporary theory and progressive practice of market developed countries and the Republic of Serbia indicate that the tax system is the most important segment of fiscal policy, namely, of fiscal system as its narrower segment. Tax forms in the Republic of Serbia differ among themselves from the aspect of definition, from the very tax object, tax base and tax rate.

The tax system that is drawn up well should meet the following criteria (Durovic-Todorovic et al., 2008; Raicevic, 2004): 1) provide rational allocation of resources and to be allocatively neutral, 2) provide stable and optimum amount of public revenue for financing public spending, 3) provide that tax burden is evenly distributed to tax payers according to principle of fairness, 4) be clear and understandable to tax payers, 5) be flexible, meaning, have the possibility of adapting to changes in economic policy, 6) necessarily stimulate all structural changes that aim at developing market economy. Basic principles of tax system in Serbia (Durovic-Todorovic et al., 2008; (Durovic-Todorovic et al., 2008; Raicevic and Randelovic, 2007) assume the achieving conformity with the EU tax system, as well.

In this context, the designing and structuring of tax system appear important tasks for fiscal authorities, require their optimal decisions in choosing certain tax forms and their structure. Structuring of tax system in Serbia for the purpose of harmonizing it with tax system of EU should consider the following elements: personal income tax, corporate income tax, value-added tax (VAT), social insurance contributions, etc. Of course, we should also study the principles underlying the EU entire tax system. By doing so, we create presumptions for harmonization of our tax system with the tax system of EU.

Tax system of Serbia underwent numerous changes end of 20th century and in the first decade of 21st century. The basic target of tax reforms has always been to create

efficient tax corresponding to the European standards. General sales tax and excises have been changed several times. After many years of preparations and delays, Serbia introduced new tax system on January 1, 2005. The motive for adopting new tax system was to overcome weaknesses of the previous tax system, and avoid shortcomings of different forms of sales taxes used to be basic form of consumption taxation. The VAT was introduced in Serbia on January 1, 2005 and we were among the last countries in South-Eastern Europe who introduced it. In other words, till the time our tax system has been burdened by traits of the former system. Experience of developed countries indicates that theoretical and methodological application of VAT

resulted in more efficient and effective performances of tax system in those countries that applied it.

VAT introduction conditioned reduction of tax gap in economy and lead to greater equality among different tax payers. Abolishment of tax on financial transactions reduced costs of payment operations, created favorable environment for development of domestic financial markets, especially capital market. Abolishment of firearms tax, excises on fuel oil, jet fuel and airplane gasoline, beverages and other goods provided tax relief for citizens and rationalization of administrative costs of tax administration. Simultaneously with VAT introduction, the corporate income tax was redefined (Law, 2004-2007).

TABLE 1. TAX AND NON-TAX REVENUE IN THE BUDGET OF SERBIA

| | 2006 | | 2007 | | 2008 | |
|-----------------|-----------------------|--|-----------------------|--|-----------------------|--|
| | In billions of dinars | Percentage share in total budget revenue | In billions of dinars | Percentage share in total budget revenue | In billions of dinars | Percentage share in total budget revenue |
| Tax revenue | 390.1 | 93.2 | 436.8 | 87.5 | 511.0 | 88.0 |
| Non-tax revenue | 28.3 | 6.8 | 62.3 | 12.5 | 69.4 | 12.0 |
| Total | 418.5 | 100.0 | 489.1 | 100.0 | 580.4 | 100.0 |

Source: Research based upon data taken from: Bulletin of public finance, Ministry of Finance of Republic of Serbia, January 2009

TABLE 2. REVENUE STRUCTURE IN THE BUDGET OF THE REPUBLIC OF SERBIA

| | 2006 | | 2007 | | 2008 | |
|----------------------|-----------------------|--|-----------------------|--|-----------------------|--|
| | In billions of dinars | Percentage share in total budget revenue | In billions of dinars | Percentage share in total budget revenue | In billions of dinars | Percentage share in total budget revenue |
| Tax revenue | 390.1 | 93.2 | 436.8 | 87.5 | 511.0 | 88.0 |
| Citizen's income tax | 50.6 | 12.0 | 63.7 | 12.7 | 62.7 | 10.8 |
| Corporate income tax | 9.4 | 2.3 | 16.9 | 3.4 | 27.2 | 4.7 |
| Value added tax | 215.9 | 51.6 | 225.1 | 45.1 | 265.4 | 45.7 |
| Custom duties | 39.0 | 9.3 | 45.3 | 9.0 | 57.4 | 9.9 |
| Excises | 71.3 | 17.0 | 81.6 | 16.3 | 93.2 | 16.1 |
| Other tax revenue | 3.9 | 0.9 | 4.3 | 0.85 | 5.5 | 0.86 |
| Non-tax revenue | 23.3 | 6.8 | 62.3 | 12.5 | 69.4 | 12.0 |
| Total | 418.5 | 100.0 | 489.1 | 100.0 | 580.4 | 100.0 |

Source: Research based upon data taken from: Bulletin of Public Finance, Ministry of Finance of Republic of Serbia, January 2009

In the period of 2006-2008 (VAT) had the greatest share in the structure of taxation (Table 2). It is not accidental, if one knows that this tax is imposed upon final consumption. The second largest share in budgetary revenues is taken by excise income, which provides 16%-17% of total revenue. Custom duties participate with 10%. So, altogether these taxes make 2/3 of total public revenue. This indicator is criticized by theoreticians, saying that it represents disregard of fairness principle in taxation (Durovic-Todorovic et al., 2008; Raicevic and Randelovic, 2007). Looking into this problem, the author of this paper talked to representatives of Tax Administration Office of Serbia and was explained that above mentioned data indicated there was a non-consistent taxation policy, primarily when it came to corporate income

tax and to so called synthetic tax.¹ Experience of developed countries indicates that personal income tax has the greatest share in total public revenue, which results from application of synthetic progressive taxation on personal income.

Conclusion

Following our research and the results to which it brought us, there are several questions to be posed:

¹ Based on discussions and information got during the visit of the author to Tax Administration Office of Serbia, December, 2008.

- a. How much our tax system is harmonized with EU standards and rules?
- b. How efficient our tax system is from the aspect of the level of tax rates?
- c. Is our tax system encouraging from the aspect of development policy?
- d. Is our tax system encouraging for attracting FDI?

In conclusion, we should to emphasize that our tax system is mostly harmonized with tax system of EU. We could also say that it is competitive in terms of tax rates, as well. However, these achievements are insufficient and we should consider other elements as well, such as: transparency of tax system, collection and control of public revenue, legal regulations and oth.. Therefore, we may conclude that the tax system of Serbia is insufficiently competitive in terms of attracting FDI. The latest reports of Serbian magazine *Ekonomist* (No. 2829, dated 19.12.2008) saying that Serbia could not boast attracting FDI inflows in the near two years, indicating inconsistency of Serbian tax system as one of key reasons, besides the world financial crisis. Then, we expect fiscal and economic authorities will recognize these arguments and consider them in further reforms of national tax system.

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