

The Flat Tax Spreads to Serbia

By Alvin Rabushka

On January 1, 2003, the government of Serbia implemented a comprehensive 14% flat-tax reform. Enacted in November 2002, it replaced the previous three-rate, graduated personal income tax system that had been enacted and revised between 1994 and 2001. Assessed on individual employees or self-employed persons, the previous system imposed a rate of 10% on taxable income up to Serbian Dinars (CSD) 60,000, 15% on taxable income between CSD 60,000 and CSD 120,000, and 20% on taxable income exceeding CSD 120,000. The tax rate on investment income was assessed at the highest rate of 20%. (As of March 22, 2004, US\$1 = CSD 55.56)

The new system imposes a flat rate of 14% on labor income, and income from agriculture, forestry, and self-employment, previously taxed at 20%. Withholding tax on salaries is set at 14%. The new law includes an allowance for adults and children, retirement contributions up to twice the average monthly salary paid per employee in Serbia, and redundancy payments determined by the labor law of the Republic of Serbia.

Additional tax on income above CSD 600,000 (\$10,799) was reduced from 20% to 10%, which makes for a combined maximum rate of 24%. This exception to an otherwise uniform flat tax affects a very small percentage of the population.

The new laws also reduced the corporate profit tax rate from 20% to 14%, giving Serbia the lowest corporate profit tax rate in Europe. This eliminates any interest in choosing to incorporate for tax benefits since the personal and corporate tax rates are the same. In addition to a reduction in the corporate tax rate, for the five years beginning January 1, 2003, large investments in underdeveloped areas exceeding CSD 600 million and employing more than 100 workers will receive an exemption on corporate income tax for ten years.

The government has stated its intention to further reduce taxes on income in the near future, with the reduction to be made up by a lottery tax.

It should be noted that Serbia preceded Slovakia's implementation of a 19% flat tax and Ukraine's 13% flat tax by a full year.