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TAX TREATMENT OF FLEXIBLE FORMS OF WORK IN SERBIA IN LIGHT OF THE COVID-19 GLOBAL PANDEMIC

The COVID-19 pandemic has accelerated the development of flexible forms of work, those forms of work that have essentially been enabled by the development of modern technologies. In the case of flexible forms of work, evasion of taxes and, perhaps more importantly, contributions to compulsory social security are quite pervasive. During the COVID-19 pandemic, the Serbian Tax Administration tried to collect taxes from persons who pursued flexible forms of work for employers or clients from abroad, which led to protests. Ultimately, the negotiations with the Serbian Government resulted in an agreement on transitional solutions, as well as future changes in the tax regulations. This paper aims to explain the essence of the problem that arises in Serbian tax law in connection with flexible forms of work, to analyze the proposed transitional solutions, as well as to offer some suggestions that could lead to longer-term solutions to this problem.

Key words: *False self-employment. – Independence test. – Schedular taxation. – Global services market.*

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1. INTRODUCTION

The development of modern technologies has led to significant changes in the ways in which it is possible perform work, and it has confronted us with the increasingly pronounced lack of a clear divide between employment and independent participation in the market. Namely, if we take the legal profession as an example, until only a few decades ago, it required the existence of a specifically designated place of work. Lawyers needed entire libraries of regulations, their basic tools for work and for communication with clients were static. Thirty years ago, lawyers could not pursue their job on vacation for objective reasons. They simply could not take everything they needed for work with them. Today, none of the above is true. The only thing a lawyer needs to do the job is a computer, which can be portable, where communication with clients primarily depends on the existence of (mobile) phone and Internet connectivity, and it is quite possible that all meetings with clients and discussions can be held without physical presence, through platforms intended precisely for these purposes.[1] Given that libraries of regulations are contained in virtual databases, that lawyers can communicate with clients from anywhere on the planet and at any time, where all of the above possibilities no longer entail significant costs, the question arises whether a specially designated work space or an office is needed. All the changes related to the way in which the legal profession is practiced can be seen in many other activities as well, primarily in the service sector, which today accounts for a significant part of the global economy.[2]

From the time being, an office is no longer required to do the job, when the means of work or communication become available to the broadest segments of the population, and certain tools can be provided to employees via the Internet anywhere on the planet,[3] the very need for at least a formal employment relationship, with all the rights and obligations

[1] For example, Webex, Zoom, Teams, etc.

[2] According to data from 2015, the services sector accounted for 76% of the gross domestic product in developed countries, and 55% in developing countries, with a steady increase in the share of the services sector in the gross domestic product of almost all countries. See WTO. 2019. *World Trade Report – the Future of Services Trade*, p. 15. *https://www.wto.org/english/res_e/booksp_e/00_wtr19_e.pdf* (last visited 25 November, 2022).

[3] Where available, for example, an employer may have a subscription to specific software required to perform a certain tasks, and the employee is provided access to that software through appropriate codes, without the need to be at a certain place when accessing (e.g. they can access software from their home and do not have to be located at the premises of the employer).

that such a relationship imposes, can be called into question (Kostić 2021, 767). Moreover, modern technologies open up previously unimaginable opportunities for cross-border cooperation, where individuals have the opportunity to contact potential customers or employers from around the world, while employers, or persons in need of certain services, can search for labor far beyond the borders of the countries in which they are located or do business, without the concomitant need to move that same workforce from the countries in which it is located (de la Feria, Maffini 2021, 164).

The COVID-19 pandemic has significantly accelerated all these processes (Office for National Statistics 2020; Eurofund 2020). Employers around the world are increasingly accepting the model of working from home (more precisely, the model of working without a workplace), and this transition is no longer conditioned only by the emergency circumstances of the global pandemic, but is a future common form of labor relations (PWC 2020), especially if all savings that can result from work without a workplace, as well as hiring labor without concluding an employment contract, are taken into account.

In the past four years, these issues in Serbia have been the focus of the legislator as well as the general public, some of them even leading to civil protests on the streets of the capital, precisely during the time of the COVID-19 pandemic. In this paper, we will attempt to determine the basic elements of the development of Serbia's tax legislation related to flexible forms of work, which were essentially caused by the advancement of modern technologies and crucially accelerated by the ongoing global pandemic.

2. CONCEALMENT OF EMPLOYMENT AND ABUSE OF FLAT-RATE TAXATION OF INDEPENDENT ENTREPRENEURS

Tax-wise, the very beginning of the COVID-19 pandemic in March 2020 was marked by the introduction of the so-called independence test to the Law on Personal Income Tax,[4] as well as the accompanying three-year transitional regime aimed at enabling a painless restructuring of parts of the Serbian economy and the cessation of aggressive techniques of tax optimization of labor costs.[5]

[4] See Law on Amendments and Supplements to the Law on Personal Income Tax, Art. 18, *Official Gazette of the Republic of Serbia*, No. 86/19.

[5] See Law on Amendments and Supplements to the Law on Personal Income Tax, Art. 10, *Official Gazette of the Republic of Serbia*, No. 86/19.

Already during 2017 and 2018 it was noted that in certain segments of the Serbian economy, and especially in its fast-growing IT sector, employers increasingly ceased to hire their workforce by establishing formal employment relationships, but rather did so through service contracts with seemingly independent service providers. The problem of so-called bogus self-employment (Hayes, Hastings 2017) is not particular to Serbia and is present in many countries worldwide, but its specificity in Serbia is that the use of this model of labor hiring was almost exclusively related to tax reasons. More precisely, the main reasons for such measures were the savings in taxes and contributions for compulsory social insurance, while the need to find ways to achieve them came not only from evasive motives, but also from the need to offer the workforce a higher net income with as little expenditure as possible, thus becoming more competitive in the labor market, which is increasingly global and cannot be limited by national borders.

Namely, if an employer in Serbia hires labor through an employment contract, they must first take into account that Serbia has a *net culture*, i.e., that an employee, when negotiating the earnings, does so in terms of net earnings, those that will remain after taxes on such income and related social security contributions have been assessed and paid. Therefore, if the employer wants to offer an employee a net salary of, e.g., 2,000 EUR, it will cost them a total of about 3,500 EUR. However, if a potential employee accepts (instead of employment) a model whereby they will be registered as an entrepreneur who pays the taxes on income from self-employment and contributions for compulsory social insurance on a lump sum basis, and therefore conclude a service contract with the employer (who now appears in the role of the principal), based on which they will perform all those tasks that they would otherwise perform under the employment contract, thus allowing either the achievement of significant savings or increase of the employer's competitiveness in the labor market. These benefits are primarily due to the shortcomings of the existing lump sum taxation system in Serbia, which primarily leads to aggressive tax planning in the case of high wages.

Let us explore how savings are achieved in the described case. While an employer is required to withhold and pay taxes and contributions for compulsory social insurance at the time of salary payment, in the name and on behalf of the employee,[6] in the case of remuneration paid to a registered entrepreneur based on services provided, the principal has no tax

[6] See Art. 99, para 1, point 1 of the Law on Personal Income Tax, *Official Gazette of the Republic of Serbia*, Nos. 24/01, 80/02, 80/02, 135/04, 62/06, 65/06, 31/09, 44/09, 18/10, 50/11, 91/11, 93/12, 114 / 12, 47/13, 48/13, 108/13, 57/14, 68/14, 112/15, 113/17, 95/18, 86/19, 153/20, 44/21, 118/21 (hereinafter: PITL).

obligations whatsoever. The entrepreneur, if they pay the tax on income from self-employment on a lump sum basis, determines their obligations without taking into account the actual income and expenses, but on the tax base assessed by the Tax Administration, based on a number of presumptions.[7] Bearing in mind that when assessing the tax base, the Tax Administration is led by certain binding guidelines, which by their nature imply generality, it is quite possible that an above average successful taxpayer is provided with a base that is significantly lower than their actual profit generated from their business.[8] For example, if the independent entrepreneur has the tax base for income from self-employment assessed in the amount of 140,000 dinars per month, and they receive a monthly payment from their principal in the amount of 420,000 dinars per month, their tax burden (including the burden related to contributions for compulsory social insurance) is three times lower than the one they would have been subjected to had they paid the tax on their actual income. Moreover, we recall that the net salary of 240,000 dinars per month (2,000 EUR) would cost the employer a total of 420,000 (3,500 EUR), and that an independent entrepreneur who pays the lump sum tax on a basis of 140,000 dinars per month, after paying taxes and contributions for compulsory social insurance from the 420,000 dinars of service payment, still keeps over 350,000 dinars. We note that tax planning through hiring labor through service contracts, instead of employment contracts, provides that engaging registered entrepreneurs, who pay taxes on income from self-employment on a lump-sum basis, allows for the hired person, taking as a reference point a 2,000 EUR net salary, either with up to 1,000 EUR per month higher net income (also avoiding the payment of the annual personal income tax)[9] or to provide them with the same net income at a significantly lower total cost to the employer. Finally, if one adds all the possibilities for optimizing the lump sum tax base, such as reporting a different code of activity from the one actually performed or a different place of activity from the one where it is actually performed, which implies a lower lump sum base (which are possibilities that are significantly increased

7 See Art. 40 of the PITL.

8 See Art. 41 of the PITL and Arts. 3–5 of the Decree on detailed conditions, criteria and elements for lump-sum taxation of taxpayers of income from self-employment, *Official Gazette of the Republic of Serbia,* Nos. 94/19 , 96/19 – correction, 156/20 (hereinafter: the Decree).

9 Taxpayers who pay tax on income from self-employment on a lump sum basis, and for whom income from entrepreneurial activity is the only source of income, do not meet the conditions to be considered taxpayers of the annual personal income tax. In this example, if the service provider had earned a gross salary of 420,000 dinars as an employee, they would have met the conditions to be considered taxpayers for the annual personal income tax.

by the limited audit resources available to the Serbian Tax Administration), the room for tax savings is expanded even more. In addition to the abovementioned, an employer who hires its workforce through a service contract also avoids the obligations imposed by labor law regulations, and the hired worker essentially exchanges protection for a higher net income.

The described phenomenon not only jeopardized the state's public revenues, but it also began to create serious problems within the economy itself. Namely, employers who were unable to hire labor through service contracts (e.g., due to obligations to their unions, in the country or abroad) or who were not willing to take the risk of liability for illegal tax evasion (which can certainly be considered real), they were put in a situation where they simply could not afford certain labor. The service providers agreed to conclude employment contracts but demanded the same net income that they earned as entrepreneurs, which the potential employers simply could not afford.

Having in mind not only the danger to public revenues, but also economic development as such, the Serbian legislator decided to introduce a mechanism into the legislation that has come to be known as the *independence test*.

3. INDEPENDENCE TEST

Three options were available to the Serbian legislator to fight against concealment of employment and abuse of lump-sum taxation by independent entrepreneurs and their respective employers.

Firstly, the principle of facticity is referred to in Article 9 of the Law on Tax Procedure and Tax Administration,[10] regarding individual audit procedures conducted on taxpayers by the Serbian Tax Administration. If the audit finds that the economic essence of the relationship between the principal and the independent service provider is the one of an employment relationship, then the Serbian Tax Administration would be entitled to consider the service contract a simulated legal transaction, where the tax dues would be assessed on the basis of the dissimulated legal transaction, i.e., the employment that the taxpayers tried to cover up.

[10] *Official Gazette of the Republic of Serbia*, Nos. 80/02, 84/02, 23/03, 70/03, 55/04, 61/05, 85/05, 62/06, 61/07, 20/09, 72/09, 53/10, 101 / 11, 2/12, 93/12, 47/13, 108/13, 68/14, 105/14, 112/15, 15/16, 108/16, 30/18, 95/18, 86/19, 144/20, 96/21 (hereinafter: LTPTA).

However, the legislator here faces several challenges. Firstly, without clear guidelines for determining the economic essence of the relationship, answering the question of whether the formal-legal relationship is simulated, and what exactly the dissimulated relationship is (the one that taxpayers tried to cover up), the practice of the Serbian Tax Administration could go astray. To exemplify, is it sufficient for a certain service provider to be considered an employee from the point of view of the economic essence of their relationship with the client, and the client as the employer, if, for example, the service provider generates more than 70% of their income from that principal. Legislation of some countries would answer affirmatively this question, while in others this fact would be only a possible indicator of the independence of service providers. Furthermore, the question also arises as to how to tax a dissimulated legal transaction, i.e., how to limit the wider scope of its recognition as an employment relationship. Namely, the field of labor legislation around the world is under great pressure to provide answers regarding the increasingly unclear divide between labor relations and independent entrepreneurship, where modern technologies have enabled the emergence of forms of work that do not belong to either category (Harris, Krueger 2015, 8–9). In Serbia, when it comes to public policy makers, this topic has not yet been on the agenda, so the unequivocal determination of the tax legislator that all insufficiently independent forms of work represent employment could adversely affect the further development of Serbia's labor law, i.e. hinder the introduction, for example, of a third category (following the example of a number of comparative legislations).[11] Finally, having in mind the scale of the described phenomenon, leaving the identified problem exclusively to the administrative management of the Serbian Tax Administration would open the issue of misdemeanor or criminal liability, primarily of persons who engaged workers by concealing labor relations, through service contracts with apparently independent service providers, where consistent implementation of such regulations could lead to extremely unfavorable consequences for the country's economic development.[12]

Another possibility was to solve the problem by amending the regulations on lump-sum taxation and the procedure for assessing the profit of taxpayers on income from self-employment, which was done to a significant extent in 2019.[13] However, the fact that lump-sum taxation cannot avoid a high level

[11] For example, that of the United Kingdom.

[12] Engaging seemingly independent service providers, instead of establishing employment with these people, was so widespread in Serbia's IT sector that its very survival would be called into question had the Serbian Tax Administration resorted to criminal sanctions for tax evasion against those responsible in such cases.

[13] By passing the Decree that replaced the previously applicable regulations in this area.

of generalization, and that problems related to inadequate reporting of activities, or the location of activities are largely due to extremely limited audit options available to tax authorities, have led to the conclusion that providing a solution in this field only would be insufficient.

Therefore, the legislator opted for the introduction of a complex test with nine criteria, where a taxpayer cannot be considered independent if at least five of them are met.[14] In other words, the legislator has explicitly prescribed what it considers the correct application of the general anti-abuse rule in specific circumstances of tax avoidance and abuse of rights. A tax inspector could certainly reach the same solution through independent work, relying exclusively on the provision of Article 9 LTPTA, but without a special regulation of this particular issue, a uniform administrative practice could not be expected, while it would take years before the jurisprudence of the Administrative Court would ensure uniform application. The consequence of failing the independence test is that the income of the taxpayer, a registered entrepreneur, earned from a relationship in which they cannot be considered independent is no longer taxed as income from self-employment, but as other income (and associated contributions for compulsory social insurance applied), which is significantly less favorable.

Having in mind the degree to which the Serbian economy (primarily its IT sector) relied on this form of tax planning to ensure its competitiveness in the global market, the legislator also provided for a three-year transitional regime for all those who conclude an employment contract with their principals, enabling thus the gradual increase in the total cost of labor, i.e., providing a relatively long period for taxpayers to adjust to the new reality.[15] In addition to the transitional regime, taxpayers also received something that is quite unique to Serbia's tax practice: all those who conclude an employment contract within the set time frame, both the natural persons and their employer (previously their principal), provided amnesty by the legislator.[16]

Despite the application of the new independence test and the accompanying transitional regime coincided with the onset of the COVID-19 pandemic, and the Serbian public voicing very loud warnings that the independence test would *bury* the Serbian IT sector, unofficial data shows that the number of extinguished or frozen entrepreneurial businesses that

[14] See Art. 85, para 1, point 17 of the PITL.

[15] See Art. 21ž of the PITL.

[16] See Art. 24 of the Law on Amendments to the PITL, *Official Gazette of the Republic of Serbia*, No. 86/19.

work under the corresponding activity codes has not only coincided with the number of newly employed persons by domestic employers in the IT sector, but was lower by 1000 than the number of newly created jobs in 2020 in this sector of country's economy.

4. COVID-19 AND THE SO-CALLED FREELANCERS

In October 2020, the Serbian Tax Administration publicly called on all taxpayers who earned income from abroad to settle their tax dues, thus opening a very serious issue in Serbia's society. Namely, the Serbian tax legislation requires resident[17] taxpayers who earn income abroad or from abroad to report it themselves within 30 days from the day of collection and to simultaneously assess and pay the corresponding taxes and contributions for compulsory social security insurance.[18] Initial audits by the Serbian Tax Administration during 2020 showed that (a) a significant number of Serbian citizens earn income from abroad, primarily by providing services to foreign clients, and that (b) most of them did not pay their tax dues resulting from these earnings. The reason why 2020 was the year in which the Serbian Tax Administration decided to address this issue is that the COVID 19 pandemic had highlighted the importance of cross-border provision of services by individuals, where modern technologies had not only made this form of business possible, but also provided tax authorities with far more advanced tools for taxpayer audits. The Serbian Tax Administration was not alone and there are similar examples worldwide where tax authorities focused on the same phenomena during the same period, with the case of Pakistan possibly being the most notable (Malik, 2020).

The resulting problem is colloquially known as "freelancer taxation", which may lead an uninformed participant in the discussion to think that freelancers truly represent a special category of taxpayers.

Namely, the call of the Serbian Tax Administration did not apply to all those natural persons who provided services to foreign clients as registered entrepreneurs. These persons duly settled their tax liabilities by paying taxes

[17] According to Art. 7, para 2 of the PITL, a tax resident (taxpayer who is required to pay tax on their entire income generated worldwide) is a natural person who has registered their place of residence in the territory of Serbia, or who has a center of their business and life interests in Serbia, i.e., a person who, intermittently or continuously, resides in the territory of Serbia for more than 183 days in a period of 12 months which begins or ends in the respective tax year.

[18] See Art. 95, para 6 of the PITL.

on income from self-employment and related contributions for compulsory social insurance. In the case of the registered entrepreneurs who failed the independence test in regarding to their foreign clients, as a rule, the solution was that they, since they could not be directly employed by a foreign client, establish single-member limited liability companies, employ themselves in these companies, and benefit from the three-year transitional regime provided for in support of the independence test. The call of the Serbian Tax Administration was aimed at those domestic individuals who earned income from abroad by providing services on the international market, but who were not registered as entrepreneurs, nor did they pay taxes and contributions for compulsory social security insurance on such income. In case of a taxpayer who is not registered as an entrepreneur but provides services on the market, the PITL stipulates that the income generated on this basis is taxed as other income, by virtue of the tax on other income, and this obligation is also accompanied by the duty to pay associated contributions for compulsory social security insurance.

Having in mind the number of "freelancers", but also the rather low level of tax culture and knowledge of the basic elements of tax law in Serbia, a public outcry against the Serbian Tax Administration arose quickly, and extremely unfounded accusations against its work were frequently made (most commonly stating that it stipulates retroactive application of regulations, which was completely incorrect). It was somewhat surprising that organizations that aimed to represent a fairly diverse population of freelancers in talks[19] with the authorities appeared in the public space very quickly. These organizations were quite successful in their efforts.

Leaving aside the arguments that were presented in the sometimes passionate exchange of opinions between representatives of different parties, we can see that the issue of "freelancers" revealed some of the key shortcomings of the existing personal income taxation system in Serbia.

Namely, this system is based on a clear dichotomy between the tax on salaries, on the one hand, and the tax on income from self-employment, on the other hand. A taxpayer who earns income from their work is either independent (entrepreneur) or dependent (employee), so in accordance with this status, their income is subjected to the corresponding tax treatment. The tax on other income is provided for the taxation of income that a taxpayer who is not registered as an entrepreneur earns outside their employment, by providing services on the market. Since permanent activity

[19] For example, Association of Internet Workers (*https://uri.rs*).

on the market would imply registration as an entrepreneur, the conclusion is that the Serbian legislator intended for income generated occasionally, exceptionally, or which is only a supplementary source of personal income be taxed as other income.

The call of the Serbian Tax Administration and what followed as a public reaction revealed the fact that a large number (tens of thousands) of taxpayers in Serbia rely on other income as their only source of income, and that only in a certain number of cases their failure to register as entrepreneurs can be explained by evasive intent, i.e., a conscious attempt to avoid tax which can otherwise be settled. Unfortunately, a far larger number of them are taxpayers who are forced to choose between meeting the most basic needs of life on the one hand and paying taxes and contributions on the other, or taxpayers for whom payment of taxes according to existing regulations would mean condemning them to starvation. It is this conclusion that raises the question of the inadequacy of the existing tax system and the system of contributions for compulsory social security insurance for a very large number of taxpayers in the country.

5. ENTREPRENEURS WHO DO NOT PAY TAXES AND THE UNCONSTITUTIONALITY OF THE EXISTING TAX FRAMEWORK IN THE CASE OF POOR TAXPAYERS

Taking into account all examples of "freelancers" covered by the Serbian Tax Administration's call, we note two clearly expressed poles, and each of these two poles again can be divided into two categories.

In order to illustrate the observed divisions, it is enough to consider what exactly is the difference between, for example, the English teacher who tutors students in China, via a virtual platform, and the English teacher who tutors local students in their homes. Both teachers perform exactly the same activity, and the income they earn is taxable in Serbia under the same conditions, regardless of where the student is located (bearing in mind that in both cases the tutoring is conducted from Serbia). What diametrically distinguishes these two teachers is that one will be paid by bank transfer, while the other will, as a rule, be paid in cash. In other words, the only difference between these two entrepreneurs, but a crucial one when it comes to their tax treatment, lies in the fact that the Serbian Tax Administration will very easily be able to track the income of one English teacher, while in the

case of another it will be practically impossible.[20] Therefore, from the very beginning we notice a certain injustice caused by objective circumstances, that those freelancers whose clients pay by bank transfer will be in a more difficult position than those who can conduct business in cash, which will usually be those freelancers who provide their services on the international market, using opportunities provided by the unprecedented development of modern technologies. In the situation of a global pandemic, quarantines and curfews, opportunities for providing services in the domestic market decreased for a large number of activities, but for some of them there are opportunities to make up for the loss in the domestic market by entering the international market. However, entering the international market implies electronic payment, and thus significantly reduced opportunities to successfully avoid reporting income and consequently paying taxes.

Within the segment of freelancers who provide their services on foreign markets, i.e., those whose ability to avoid paying taxes is significantly limited due to the existence of clear trail of cash flow, there are two distinctly separated categories.

On one end there are those taxpayers who earned a substantial income, and who simply did not consider it necessary to report the same and pay pertinent taxes. The Serbian system of taxation of self-employment income enables taxpayers earning more than EUR 1,500 per month to bear the total tax burden (including taxes and compulsory social security contributions) which can in no way be considered excessive, especially when compared to the tax burden to which these taxpayers would be subjected in similar countries (Ranđelović 2021, 199–200). In addition, the tax regime to which the income of registered entrepreneurs is subjected is significantly more favorable and provides a lot of room for legal tax optimization compared to that prescribed for taxation of other income. Therefore, it can be concluded that in the case of these freelancers there are no arguments (except that they were unaware of their tax obligations and that no one pointed out to them when they communicated orally to tax officials) that would justify their avoidance of reporting their income and settling the pertinent dues.

However, with the decrease of the taxpayers' income, the above conclusion loses credibility. For example, a registered entrepreneur earning EUR 2,000 per month (i.e., since the income may vary from month to month, EUR 24,000 per year), subject to taxation of income from self-employment, could reduce

[20] Mechanisms of cross-assessment of the tax base, i.e., those provided by the Law on Determining the Origin of Property and Special Tax, imply high amounts of undeclared income, i.e., a significant amount of newly acquired property whose origin cannot be justified by the saved part of declared income (gift or inheritance).

their total tax burden (which includes contributions for compulsory social security) to around 18% (e.g., if they keep business books and decide to pay the entrepreneur's personal salary in the amount of the minimum wage), including the cost of keeping business records. A registered entrepreneur earning EUR 500 per month (EUR 6,000 per year) would have to face a total tax burden of close to 40% (regardless of which form of taxation they choose). In both cases, most of the burden is due to compulsory social security contributions. If, however, a registered entrepreneur earns less than EUR 500 per month (EUR 6,000 per year), not only does its tax burden increase in percentage (especially in the case of the lump-sum taxation system), but after the payment of taxes and contributions on their net earnings, this taxpayer's available income falls below the net minimum wage. The same conclusion is drawn in the case when such income is generated by a person who is not registered as an entrepreneur, i.e., a person who pays taxes on other incomes and the corresponding contributions for compulsory social security insurance on the generated income.

The previous analysis of tax treatment of entrepreneurs has shown that the current system contains pronounced elements of regression, i.e., that the tax burden on entrepreneurs grows as their taxable income decreases, with this regression being caused primarily by the method of payment of compulsory social security contributions, according to the current regulations.

Furthermore, because a non-taxable minimum has not been prescribed in the law (with the exception in the case of taxation of wages[21]), Serbia's tax system today may require a person who barely manages to earn enough to eat (e.g., 25,000 dinars per month) to pay the state almost half that amount, meaning that after settling the taxes and contributions, they are certainly is not left with enough to feed themselves.

Bearing in mind that the Serbian Constitution[22] explicitly provides that the obligation to pay taxes and other duties is based on the economic power of taxpayers,[23] a very serious question arises regarding the constitutionality of the current system of personal income taxation in Serbia, especially in regard to discrimination of those who are not formally employed (who are not guaranteed a minimum wage), or those who earn low income. Moreover, in the case of taxpayers who earned low income from the provision of services on the market (this being their only source of income), any forced collection of taxes and contributions for compulsory social security insurance would

21 See Art. 15 a, para 2 of the PITL.

22 *Official Gazette of the Republic of Serbia*, No. 98/06.

23 Art. 91, para 2 of the Serbian Constitution.

be impossible (due to the lack of assets against which such collection could be enforced), or it would lead to serious social dilemmas, and even unrest (collection from those who cannot afford to pay in a society of pronounced social inequalities).

All of the above resulted in a temporary solution that completely exempted other income, in the amount of 384,000 dinars per year, from taxation, and thus from the payment of contributions for compulsory social security insurance, while increasing the amount of standard costs from 20% to 50%.[24] However, although this solution was primarily intended to solve problems from the past, its implementation has been extended until the end of 2022. The future taxation of other income has been changed so that a non-taxable amount is now also stipulated for this type of income,[25] i.e., the standard costs are prescribed in a fixed amount of money, instead of the percentage of generated income, as had previously been the case.

6. AN UNCERTAIN FUTURE INSTEAD OF A CONCLUSION

The provision of a fixed non-taxable amount instead of the percentage determination of standard costs, i.e., the solution that is to be applied starting 1 January 2023, as well as the existing transitional regime, are significantly more suitable for taxing the other income category, if other income is the only source of the taxpayer's taxable income. However, tens of thousands of taxpayers in Serbia earn this other income only as one type of supplement to their basic income (usually from employment). In the case of these taxpayers, both the transitional and the solution that is yet to be implemented provide them with special benefits that are not available to others, e.g., to taxpayers who earn their only income from employment or exclusively from performing entrepreneurial activities. In addition to the above, sole entrepreneurs remain a key category of taxpayers who have not been provided with a non-taxable minimum in Serbia in any way, making low-profit entrepreneurs particularly vulnerable.

The issue that Serbia is facing is that it is no longer possible to successfully adjust the legal framework to the modern reality, since it is overwhelmingly designed for the reality of bygone times. The COVID-19 pandemic has only

[24] See Art. 5 of the Law on Amendments to the ZPDG, *Official Gazette of the Republic of Serbia*, No. 44/21.

[25] See Art. 1 of the Law on Amendments to the ZPDG, *Official Gazette of the Republic of Serbia,* No. 44/21.

accelerated the necessity to face the conclusion that Serbia's schedular system of taxation can no longer respond to the increasingly pronounced demands for tax fairness. Working from home and the entry of a huge number of taxpayers into the international labor market, without leaving the country, has revealed a whole new *world of tax* for which Serbian legislation does not have adequate solutions. Not only are new forms of employment emerging, and it is uncertain which of *old* tax categories they fall into, but the disappearance of state borders within the global, virtual labor and services market necessitates a different approach to tax revenue collection and compulsory social security contributions. Combined with the challenges posed to Serbia's society by the emigration of the population and its low natural growth rate, the conclusion is that a fundamental reform of the system of personal income taxation and the system of compulsory social security insurance the urgent needed. The preparation for this reform in itself will require much time, because Serbia will have to make tax policy decisions on certain issues for the first time (as these have not existed previously). Unfortunately, at the present there is no discernable readiness for such a thorough and long-term approach, and it seems that the state will continue addressing 21st-century problems using a framework that was archaic even when it was introduced more than two decades ago.

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