The Percentage Tax Designation Considered in Serbia: What Difference Can It Make?

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Serbia, a republic in southeastern Europe and formerly a part of Yugoslavia, has been a stand-alone sovereign republic since 2006. Serbia signed the SAA with EU in 2008 and officially became an EU candidate country in 2012. The country has 7.14 million inhabitants[1] and a taxpayer base (# of employed) of 1,697,000. Serbia is a member of the UN, Council of Europe, and OSCE. Serbia is an upper-middle income economy with a dominant service sector, followed by the industrial sector and agriculture. The country ranks well in the Social Progress Index (45th), the Global Peace Index (46th), and the Human Development Index (66th).

Background on Tax Designation System as a Policy Option

Serbia is among the countries of the region that does not currently possess a tax percentage designation system.

In the early 2000s, the FENS CSO Network, under the leadership of Civic Initiatives, a leading Serbian NGO, explored the feasibility of the introduction of tax designation in Serbia, but no real concrete results or steps resulted.

During this same period, several of the larger CSOs in Serbia at the time participated in a series of study trips to Slovakia and Hungary during which they became acquainted with the tax designation mechanisms in both countries. While they came back with more information about the mechanism and their application in each country, no serious efforts were made to either open a debate within the civil sector about the advantages of having the tax designation mechanism in Serbia or to advocate with the authorities for such a solution.

A possible explanation for why tax designation as a policy option was not seriously discussed at the time is that major advocates in the civil sector were really focused on their struggle to introduce a new Law on Associations and to create a better basic legal environment for the operation of CSOs. While this law was finally adopted in 2009, other issues were then on the agenda, and the tax designation option never discussed or debated in the wider community of CSOs and the topic fell off the radar.

In 2014, representatives of the Serbian Government's Office for Cooperation with Civil Society (OCCS) went on study trips to both Hungary and Poland to look at the mechanism in each country as well its implementation, thus beginning a renewed interest in the topic. At the time, the OCCS was in the draft stages for the National Strategy for Creating an Enabling Environment for the Civil Society Development (2015-

[1] slightly more than 9 million when the population of the disputed Kosovo territory is included

2019). By the time the draft was published in August 2015 and the public debate period initiated, neither a percentage tax designation law nor mechanism was envisaged in the Action Plan of the Strategy.

To date, no champion or advocate of the percentage tax designation has emerged to lead the public discussion on its potential pros and cons in Serbia.

Civil Society Sustainability in Serbia

Current Legal Framework for Civil Society

The legal framework governing CSOs in Serbia is comprised of the Law on Associations and the Law on Endowments and Foundations.

The Law on Associations was adopted in 2009 after a very long and active advocacy process by the civil sector. This Law regulates both domestic and foreign associations registration and work. The law is quite progressive for Serbia in terms of freedom of association since it allows for either individuals and/or legal entities to be founders and a minimum of three founding members. It also requires an internal governance structure that includes an assembly of members as well as a board of trustees. Persons above 14 years old can be founders as can foreign citizens. The law provides a wide definition of activities that are within the realm of public benefit, although this wide definition also comes with some non-specific language that could be improved upon.

The Law on Endowments and Foundations was adopted in 2010 with its predecessor law having been adopted during the time of Yugoslavia. This law regulates endowments as well as domestic and foreign foundations. The law requires only one individual or legal entity to be a founder and it mandates the formation of a board of trustees with a minimum of three members.

The law allows for endowments with private benefit purposes and requires founding capital of no less than 30,000 EUR, which is the distinguishing difference between an endowment and a foundation (which requires no founding capital).

All foundations and those endowments that are established for public benefit purposes are exempt from the payment of taxes levied under the law.

Non-formal associations or groups may also be established and operate freely, but registration is requirement to be able to take part in legal or financial transactions—such as opening a bank account, registering property, or having employees.

The registration process is reasonably efficient and decentralized, and is conducted with due process in a timely fashion with appropriate rights of appeal or resubmission of further documentation. After filing, Serbian law requires that the government formally record a qualified applicant into the Register within 30 days. Registration is relatively affordable and fees usually amount to approximately 400 EUR. The list of required documentation is clear and these documents are relatively easy to create or obtain. Legal guidance may be advisable when registering CSOs with more complicated governance structures, but templates for by-laws and other required documents are easy to obtain and edit for basic governance structures.

It is important to note that the registration process for both associations and endowments and/or foundations is not a process of review and approval, but rather a form of registering a CSO's planned or existing structure in order to participate in legal and financial activities. Both associations and endowments and/or foundations are free to determine their own goals, regulate their internal affairs and operate in accordance with their statutes and by-laws.

Current Tax Framework for Giving

While both associations and foundations (and endowments registered for public benefit activities) are exempt from paying income taxes on revenues derived from donations, any unspent or carried-over income that is derived from the provision of services or sales of goods are taxable beyond an established annual threshold.

Donations or gifts exceeding 100,000 RSD (app. 830 EUR) by a single donor in a calendar year must be reported by the recipient organization to tax authorities so that a tax determination can be made, although they are generally exempted from income taxes. Gifts to associations, foundations and endowments pursuing public benefit activities as defined in their respective framework regulation which exceed the prescribed threshold are exempted from income taxes, insofar as they are used to pursue the organization's public benefit purposes.

Regarding tax benefits for donors, exemptions do exist for corporate donors under the Legal Entity Profit Tax law, but no benefits are foreseen for individuals under the Personal Income Tax Law.

The Legal Entity Profit Tax Law allows companies to deduct up to 5% of their gross income to entities (both nonprofit and/or government) for a range of activities considered to be public benefit[2]. Deductions are recognized as tax deductible only if given to legal entities which work to further those purposes.

The Personal Income Tax Law does not envisage any tax benefits for giving to public benefit purposes. While it can be argued that a tax deduction mechanism may not have a significant impact of the levels of individual philanthropic giving, it is certain that the lack of any tax advantage certainly does not encourage individual giving. It is also a factor to consider when envisioning the impact of a percentage tax designation mechanism.

[2] medical, educational, scientific, humanitarian, religious, environmental protection and sport purposes, as well as for giving to institutions of social protection established by the law governing social protection; also, investments in cultural purposes and cinematography.

While the types of activities done by CSOs (and state-owned institutions) are designated as having public benefit, the concept of an entity applying for or possessing public benefit status is not developed in the tax laws. Some elements of the concept are addressed in the CSO framework regulation with respect to CSOs that are eligible to receive state funds, however.

Issues in the Tax Framework That Impact Civil Society

The list of public benefit activities in the Legal Entity Profit Tax Law is narrow. Thus, there is a discrepancy between the Legal Entity Profit Tax Law, and the Laws on Associations and on Endowments and Foundations. There is a further discrepancy between the Legal Entity Profit Tax Law and the Law on Donations and Humanitarian Assistance, which provides for customs clearance and other benefits for a wider scope of donations.

The amendments to the Legal Entity Tax Law in 2012 put an emphasis on the type (nature) of public benefit activities, but not on the institutional forms to engage in those activities. The same law also does not specifically recognize in-kind donations as tax deductible. According to information received from CSOs, tax authorities occasionally interpret the Law so as to recognize only donations in money as tax deductible.

Furthermore, for companies within the VAT system, in-kind donations are treated by the tax authorities as a transfer of goods or services which is subject to the payment of VAT tax. In practice, CSOs as recipients of in-kind donations are often asked to pay the VAT tax, which amounts

The Property Income Tax Law also gives rise to several issues:

- Tax authorities require CSOs to file for a tax exemption for any gift given by a single donor that exceeds the 100,000 RSD threshold in a given calendar year.
- The Law does not specifically provide for a carry-over rule or for a specific time line, which will allow unspent donations to be carried to subsequent fiscal years. This gives the tax authority a great deal of discretionary power to decide on those issues.
- The Law does not provide for specific rules with respect to institutional grants to CSOs and overhead expenses of the organizations. As already noted, tax authorities occasionally levy taxes on any portion of a donation used for overheads.

Perhaps the greatest impact to CSOs is the uneven interpretation by local tax administration office of the laws mentioned above, resulting in a great variance in their application.

Civil Society Development in Serbia

Current State of the Civil Sector: By the Numbers

As of 2015, the Serbian Business Registry Agency has recorded 26,096 association registrations and 918 registered foundations and endowments. There are 3.25 CSOs for each 1,000 citizens in Serbia.

Data from the OCCS for 2014 records total CSO income at 261.33 million EUR. Assuming all registered organizations are active (which is certainly not the case, although there is no definitive data for this), the average annual revenue of a CSO is 9,675 EUR.

State Support for CSOs in 2014 totaled 68.34 million EUR. The ways in which decision-making is done and how CSOs are or are not able to access states support is discussed further in a section below.

Private giving (from companies and individuals) in Serbia is on the rise, reaching 18.329 million EUR in 2014. However, only 14% of this of this amount was given to or through CSOs, making a marginal impact on their overall income.

The vast majority of the income that CSOs receive still come directly from foreign governments or foreign foundations. While there is a steady change taking place, this change is slow and incremental.

Civil Society Development: Key Issues

While there are a myriad of factors that affect civil society development, there are three main issues that influence civil society development in Serbia and that can be tracked both historically and viewed as pathways for positive change in the future:

- Legal and Policy Environment
- Long-Term Sustainability
- Financial Viability

Apart from these three key issues, it is important to note that Serbian civil society is going through a process that could rightly be referred to as a generational transition. While this is certainly normal in any sector, both in terms of leadership and in the maturity of ideas, goals and initiates, this multi-year process is quite slow and has caused numerous challenges that are difficult to deal with. For example, many of the organizations that were considered as leaders in their field have either lost their focus and or a clear brand/identity in the process of leadership change at both the top and mid management levels. Yet, many of the emerging new leading organizations and their leaders are still finding their feet.

Inevitably, these types of changes have caused a certain amount confusion within civil society as they struggle in their relationships with other sectors (government, business, academia, etc.) and consequently their role in society in general. The relation to both state as well as business sector is at best ambivalent, with civil society overall being indecisive or lacking clarity in how to act/react toward them. Is the state an enemy or a partner? Is the business sector an ally, client or donor? Leaders of this transitional period work to clarify their approach and find a common voice.

While this may be a natural process, it feels as though it is taking longer than desired, and is effectively keeping civil society from taking a united and strong position on important issues that may well shape the future and tone of successful civil dialogue in Serbia.

Civil Society Development – Legal and Policy Environment

In the last few years, there has been significant progress in improving the legal and policy environment for the work of civil society in Serbia.

After very long processes, both the Law on Associations and the Law on Endowments and Foundations were adopted. The registration process for a CSO is simplified and quick in most cases and, in general, the right of freedom of association is improved.

The Serbian Government established its Office for Cooperation with Civil Society (OCCS) which has significantly contributed to improved management of civil society-government cooperation. Indeed, civil society now has a partner in government.

The national policy document, entitled *Needs of the Republic of Serbia for International Assistance 2014-2020*, was adopted and includes measures focused on the further development of a favorable environment for civil society sustainability, partnership with the government, and further capacity building to help CSOs participate in decision-making processes.

Several important procedures and regulations were adopted that have improved the overall framework. These include an improved procedure for CSOs to apply for funding for public benefit programs, a regulation that improves opportunities for CSOs to participate in the policy planning processes, and, importantly, a simplified accounting system for CSOs.

On the other hand, there remain a number of key challenges. One of the key challenges is in how newly adopted procedures and regulations are implemented, especially in a decentralized environment where not all local representative offices of a given government institution seems to be armed with the same information or use the same interpretation when applying these new regulations and procedures. This is especially true in terms of the new mechanisms for systemic inclusion of civil society and citizen input to policy and decision-making processes. This problem is seen on both the local level and ministerial/agency level.

The legislation on earned income (from provision of goods and services or from property) for CSOs remains vague and open to varying interpretations, which fosters a confused environment and ultimately discourages CSOs from taking bold and clear steps to initiate income-generating activity. The vagueness of the legislation is further muddled by a set of bylaws that offer conflicting information on the levels of tax deductible income and the application of VAT regulations. Clarity and harmonization of these laws, bylaws and regulations is needed.

Civil Society Development – Long-Term Sustainability

Although many refer to the sustainability of the sector having in mind only financial aspect, several of that challenges faced by Serbian civil society are actually connected with other sustainability aspects, which, in turn influence its financial viability.

<u>Strategy/Focus</u>. It has been observed that there is lack of strategy and focus among non-profit organizations, especially over the last few years. This has affected the ability of these organizations to influence change in their chosen areas of work. It has also resulted, at times, in organizations getting side-tracked form their primary mission and addresses a variety of issues outside of their primary scope or concentration.

<u>Public Image</u>. While the public image and perception of civil society has been improving somewhat over the years, it still remains more negative than positive. The general public has little insight into the results and work of CSOs in number of areas, due in large part to the lack of a culture of transparency and an understanding of constituency by CSOs. Rare cases of misuse of funds or corruption have been however widely discussed and used as an example of how the non-profit sector works.

<u>Communication</u>. There is a general lack of investment into promoting the activities, the goals, the theory of change, the outcomes, the results and the impact of civil society organizations. The ordinary citizen in many cases would be hard-pressed to explain how their life has been affected or changed for the better as a result of the work of any of the leading CSOs in Serbia. This inability of citizens to express the perceived or felt benefits of the work of CSOs is indicative of a communication failure. The time and money required to invest in better and more pro-active communication will certainly help in efforts to sustain the relevance and legitimacy of the civil society sector as a whole.

<u>Building constituency</u>. The anemic efforts of Serbian civil sector to build a base of supporters among citizens remain insufficient. Indeed, it appears that many organizations do not yet understand the importance of developing and nurturing a constituency. A vast majority of non-profit organizations consider and act as if their donors (and not citizens) are their main constituency. In order to further the sustainability of the civil society sector, a paradigm shift is required in the way that nonprofits think about their relationships with the various segments of their public audience, their community, their beneficiaries and other stakeholders.

Organizational capacity. While civil society organizational capacity has definitely increased over the years, a constant rise in both the number of organizations and the human resources involved requires further efforts in this area. The ongoing generational transition has also caused some weakness in this area as well. Internal governance structures and decision-making are still not well developed and impact the ability of organizations to function as organizations free from the control of a strong leader.

Services and Quality Assurance. Many CSOs have worked to develop and offer services in their respective areas of expertise over the last few years. This is especially true in the social and human services sector. However, there are no clear mechanisms for measuring either the results of or monitoring the quality of services. This prevent nonprofits not only in ensuring quality service provision, but also in communicating their results to the public.

Civil Society Development – Financial Viability

Civil society organizations currently source their revenue from a variety of sources, including foreign sources, state funds, private philanthropy, and earned income.

Foreign sources. Foreign funding comprises The bulk of foreign funding comes through EU and Norwegian bilateral/embassy funds. Other foreign donors (both bilateral and private) while still present, mostly scaled down both their activities as well as their funding.

State funds. State funds are becoming most significant source for number of CSOs, amounting to slightly more than 26% of overall CSO income in 2014. Public funding of civil society occurs on three levels: national (through ministries and governmental agencies), provincial (the autonomous province of Vojvodina) and municipal.

Public funding is generally regulated by number of laws, including the Law on Associations; however, provincial and municipal governments have a number of additional bylaws which further define the mechanism for and distribution of resources.

Public funding of nonprofit organizations on the national level is currently distributed through six different budget lines. 85% of national resources are through budget line 481, which is defined as ‘Donations to CSOs’, although churches, sport clubs, and political parties are also funded through this budget line. The way that the national budget is currently structured makes it quite difficult to analyze or understand what programs and projects are funded from this budget line. The National Strategy for Public Administration Reform envisages the introduction of a programmatic budget instead of the current line budget, which, when implemented, should help in addressing a number of issues connected with the public funding of CSOs, including both transparency and allocation.

Key challenges in public funding include:

- *Lack of strategy in funding.* It is not clear how priorities for RfAs are determined, since they are rarely in line with national strategies and/or public policies.
- *Lack of information about potential funding opportunities*. RfAs are often published without advance notice and frequently with short submission deadlines.
- *Non-transparent allocation of funding.* There is often a lack of clear selection criteria and/or process in published RfAs. Furthermore, despite regulations to contrary, many funding allocations are made to CSOs without the publication of a competitive RfA. In 2012, 39,22% of budgetary resources for CSOs were distributed by the direct decision of the head of departments without the issuance of a public RfA. Due to this lack of transparency, potential corruption or cronyism is often raised as an issue.
- *No institutional grants.* Public funding focuses on single budget year project funding rather than investments into CSOs for either multiple years or for capacity building or operational costs.
- *Insufficient practice of co-financing.* While there are a few examples to the contrary (i.e. the OCCS co-funding of Europe for Citizens), the standard practice of public funding schemes is to finance stand-alone programs or projects. This results in reduced results and potential duplication of efforts by two funding streams through two different CSOs for the same activity rather than maximizing on the possibility of partnership and collaboration between stakeholders, including donors.
- *Recent increase in administrative hurdles.* More recently, the application and selection process has been made more difficult through the introduction of rules that lack in logic and resulting in the rejection of applications for insignificant reasons (e.g. an application is sent by express post and not by ordinary post, and is therefore rejected for that reason, despite both forms of delivery having the required postal time stamp).

<u>Private philanthropy</u>. There has been a steady increase in the levels of private philanthropy sourced both from companies, individuals and the Serbian diaspora. This increase has been accompanied by a concerted effort of some segments of the CSO community to more actively approach and engage private sources of funding. Yet, the estimated 18.329 million EUR in total private funding recorded in 2014 from private sources in Serbia has had only minor impact on the income levels of CSOs, since only 14% (app. 2.56 million EUR) of that giving has been directed to or through nonprofit organizations. Companies tend to give more to/through nonprofits than individuals do. The diaspora is still an untapped resource, except for a handful of organizations and foundation who have purposely dedicated efforts to raises funds from Serbian communities abroad. practically not tackled as source of income.

Key challenges in private philanthropy funding of CSOs include:

- *For companies -*
  - Narrowly defined set of public benefit causes allowed realizing tax deductions
  - Complex process/unclear instructions for companies to realize tax deductions
  - Lack of corporate giving strategies and clarity of what they want to achieve.
  - RfAs are rarely published, with companies choosing to work with a limited number of partners, making it difficult for new organizations to approach companies.
  - Primarily support soft issues (support to marginalized groups, healthcare and education) and limited beneficiary groups (children and youth, population of specific communities)
- *For individuals -*
  - Lack of tax incentives
  - Complex administration of individual donations (requiring a signed donation contract)
  - Anonymous donations are not allowed due to money-laundering laws
  - Methods of payment not easy; online donations are difficult to set up
  - Giving is mostly ad hoc and not strategic, often emergency giving. Mass giving mostly directed to individuals/families (i.e. for medical treatments)
  - Primarily support soft issues (health/medical treatments, poverty reduction and support to marginalized groups)
  - Wealthy individuals most often give through companies they own. Theory of change or giving strategy are not still developed.
  - General lack of trust in civil society both in terms of handling funds as well as the results or impact achieved.
- *For CSOs -*
  - Lack of capacity/understanding of how to approach and work with business sector
  - Lack of understanding of how to build trust among individual donors
  - Lack of communication toward citizens/constituency
  - Lack of administrative capacity to deal with individual donors/donations

Earned income. Due to vague and/or conflicting legislation and local tax offices’ arbitrary or inconsistent treatment of earned income, revenue from income generating activities like the provision of services, sales of good or income from owned property are not significant revenue sources for CSOs.

Percentage Tax Designation as a Policy Option

In conducting this research, and taking into account the current state of civil society development and funding in Serbia, three perspectives were taken on the potential for introducing the percentage tax designation mechanism in Serbia. The first was to look at the pros and cons of how the behavior of both civil society and of taxpayers (whether they be individuals or companies) would be affected through the introduction of such a mechanism. The second perspective was a summary analysis of the financial potential for directing funding to CSOs through the introduction of the percentage tax designation mechanism using a simplified set of assumptions. The third perspective was to develop a set of questions that would need to be addressed so that a more comprehensive financial analysis of such benefits could be produced.

Pros and Cons

The interviews conducted by the researchers in preparation for this paper and the subsequent desk analysis of relevant issues demonstrates a number of pros and cons that should be considered regarding the introduction, which are illustrated in the table below:

Pros	Cons
1. Would foster a needed diversification of funding / resource development skills among CSOs 2. Citizens would have the possibility to directly influence the distribution of their taxes – democratization of public funds 3. Popularity contest instead of a connection racket, creating a healthier competition between organizations / public benefit legal entities 4. Increased level of information / awareness of citizens about civil society and their role in addressing issues of public benefit importance 5. CSOs would be encouraged to improve communication with public 6. CSO would be encouraged to develop/nurture constituency – grassroots organizations would benefit from their engagement efforts 7. One pathway to restoring public trust in the CSO sector	1. As with other countries, the primary recipients of tax designation would likely be the well-known, larger organizations, with offices in the capital city that work on humanitarian and “soft” issues 2. Human rights issues or advocacy efforts may not receive that attention they deserve 3. The state could be encouraged to reduce public funding available through other budget resources 4. There could a potential negative influence on philanthropic giving, with both people and individuals believing that they had already given through the tax designation mechanism 5. A potential perception from citizens that CSOs already have access to large amounts of funding.

Potential Financial Impact of Introduction the Percentage Tax Designation in Serbia

Serbian tax system has still not undergone a systematic reform. As a result, it is quite complicated and made even more so by recent efforts to decentralize budgetary control and expenditures without completely overhauling the tax system itself. As a result, there are significant differences that exist in both the interpretation and application of tax regulations by municipal tax offices which can be quite problematic to the normal taxpayer.

Serbia’s personal income taxation system is quite complex, with taxation occurring at two primary levels: each salary cycle and at the end of the year. The first income tax of 12% is paid by the employer on behalf of the employee to the state at the time the salary is issued. For agricultural or small enterprises with an annual revenue below 6 million RSD (app. 48,700 EUR), a flat tax of 10% is assessed. In both cases, the actual level of tax is assessed based on the municipality in where the employee is registered as living, since a portion of these tax revenues are currently allocated for use by the municipality.

There is an additional Individual Annual Income Tax law was initiated several years ago and is based on a progressive scale. Individuals whose annual income is 3 times greater than the national annual average income is assessed at 10%, but only on the basis of that difference, rather than on the entire income. Income that is greater than 6 times the national annual average income is assessed a 15% tax, again only on the basis of the income that is between 3 and 6 times that average, on top of the 10% level already assessed. This tax is assessed and collected annually by the national tax authorities.

The table below illustrates how this tax would be assessed:

Annual Avg. Income: 4,000 EUR 3 Times Threshold: 12,000 EUR 6 Times Threshold: 24,000 EUR

	Person A	Person B	Person C
Annual Income	10,000 EUR	20,000 EUR	30,000 EUR
Basis of Calculation for 10% Tax	0	8,000	12,000
10% Tax Assessed	0	800	1,200
Basis of Calculation for 15% Tax	0	0	6,000
15% Tax Assessed	0	0	900
Total Additional Income Tax Assessed	0	800	2,100

The number of employed people in Serbia in 2014 was 1,697,000. This does not include the number of agricultural households or small entrepreneurial agencies who pay via the flat tax and are not subject to the additional personal income tax. The estimated number of employees subject to the

For the purpose of a summary analysis of the financial potential of introducing the percentage tax designation, the following assumptions have been made:

- 1% tax designation by individuals only
- Estimated income distribution: 25% at minimum wage; 40% between minimum and average; 20% between average and 3 times average; 15% above 3 times average income
- Basis for tax designation on either the basic income tax or additional personal income tax
- Designation of tax by individuals would emulate the distribution of personal giving with a breakdown of 70% being given to institutions and 30% to CSOs after removing the option for individuals to designate to individuals and/or families for medical or humanitarian assistance.
- 30% of eligible taxpayers could be expected to designate their 1% within 5 years of the introduction of the mechanism

It is very important to note that these are purely hypothetical models that use the available data as best as possible and then extrapolate based on the above set of assumptions. The variance in the distribution of income, the allocation of designation, and other factors could significantly influence the results of either of the below two models. However, on the basis of these assumptions, the below two models are laid out:

	Basic Income Tax	**Personal Additional Income Tax**
Est. # of Eligible Taxpayers	1,697,000	254,550
Tax Rate	12%	10% and 15% progressive
Est. Total Tax Base	10.28 billion EUR	267.22 million EUR
Est. 1% Designation Potential Revenue	102.83 million EUR	2.67 million EUR
Est. Distribution to Institutions (70%)	71.9 million EUR	1.87 million EUR
Est. Distribution to CSOs (30%)	30.85 million EUR	801,000 EUR
Est. 1% Revenue from 30% of Eligible Taxpayers	30.85 million EUR	801,000 EUR
Est. Distribution to Institutions (70%)	21.59 million EUR	560,700 EUR
Est. Distribution to CSOs (30%)	9.26 million EUR	240,300 EUR

Acknowledging that both above models are theoretical for the basis of starting the conversation about whether the introduction of such a tax designation system into the already complex personal income taxation system, it can be seen that it would be far more advantageous to target the mechanism to the basic income tax level. Yet, because of the current system where taxes are assessed and collected at the local tax office level, with some of the revenues retained by municipalities for local budget expenditures, the likelihood of advocating for and seeing the adoption of such a mechanism applied to the basic income tax level prior to the full and complete reform of the taxation system is Serbia is very low.

Pairing the perceived pros and cons mentioned above with the revenue potentials, one can now see the arguments for why such a system could potentially be counterproductive if it resulted in either the reduction of public funding and/or personal giving.

Key Questions to Consider

This now also provides an opportunity to pose a series of questions that dig deeper than the simple assumptions used for the financial models above, the answers to which would also radically change the revenue potentials for the mechanism. Key questions include:

1. Which taxes would be subject to the tax designation? The discussion in this paper has focused only on personal income tax (either the basic income tax or the additional personal income tax). But what about applying this to property taxes or other tax bases which are common in Serbia?
2. What percentages would be the basis for the tax designation? 1% or something higher?
3. Would tax designation be obligatory or voluntary?
4. Would tax designation be available only to individual taxpayers or would companies be able to designate as well?
5. Who decides which organizations are eligible as recipients? Would institutions, churches and sport clubs also be potential recipients?
6. Would there be general limitations on how the monies are used (on specific projects/programs, institutional support, overhead costs?). If not, could citizens decide on the use from a menu of options?
7. Would funds be directly distributed to nonprofits and institutions from the tax authorities or would they first be placed in a national fund, or something similar, and then be distributed to recipients from there?
8. Who would control/monitor how the money was spent? Would citizens/public be informed on results? If so, in what way?

Many other questions remain, of course, in order to examine both the potential for to mitigate any potential difficulties that could arise from introducing a percentage tax designation system in Serbia.

Recommendations for Further Steps

There are a number of steps that should be taken to build upon this research and to further examine the feasibility of introducing a tax designation mechanism in Serbia. While the researchers share the opinion that attempting to introduce a tax designation mechanism prior to comprehensive tax reform in Serbia, the core recommendations from this research are to continue to examine the possibilities and wait for the right opportunity in Serbia for moving forward. Recommendations include:

- Building on the financial modelling presented in this research, develop additional models that would examine potential revenue from other tax sources and using other assumptions
- Examine each of the above questions in depth and develop a set of answers that will address the various models and potential revenue frameworks
- Develop a cost model for the administration and distribution of tax designation funds
- Produce a cost benefit analysis using a variety of models
- Identify carefully all necessary pre-conditions for successful implementation (e.g. introducing public benefit status, large informational campaign etc.)
- Open a wide debate among both civil society, government and private sector stakeholders on all of the above issues with the intention of coming to consensus on a way forward
- If a model is decided up and there is a critical mass to move forward, potentially launch a pilot on a small scale, perhaps on a local of provincial level.

Conclusion

A serious examination of introducing the percentage tax designation mechanism in Serbia has never been made, beyond initial study visits and case study examination by a limited number of CSO and government stakeholders. This research has provided an opportunity to dig deeper into the issue and to develop models and arguments, both pro and con, for the introduction of such a mechanism.

With the recent emergence and quick expansion of private giving, both corporate and individual, it is important to not introduce a mechanism that could potentially reduce levels of giving. As a result, the researchers believe it would be best to wait until private giving is more established as a practice in Serbia.

The taxation system is ripe for reform and is expected to occur as part of a broader set of public administration reform efforts in the coming years in Serbia. A better proposed timing for the introduction of the tax designation mechanism would be as a part of those reforms within in a more simplified taxation system.

Civil society, private sector and government stakeholders should open a serious and prolonged discussion on both the advantages and disadvantages of introducing the tax designation mechanism in Serbia and should work to come together to a consensus on the way forward.

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