

Wage tax cut down

State Secretary Janko Guzijan for Economist magazine, June 23, 2008

Can wage tax be reduced from 12 to ten percents, as suggested by Minister of Economy Mladjan Dinkic, keeping in mind the fact that the state budget is facing problems as it is, caused by higher expenditure than revenue levels?

The issue of wage tax cut down is again a live one. Wage tax reduction is one of the major economic topics not only here but in many other countries being the interest of both employed and unemployed. The employed take interest because it affects lower levels of funds' appropriation for the state, thus increasing the earnings, and unemployed because of increased opportunities of job finding due to the positive trends on work force demand caused by lower labor costs. The politicians are very interested to achieve economic prosperity in their term of the office, so they are making efforts of balancing more favorable tax policy with projected budgetary allotments.

Also, the employers, now more numerous, are openly supporting every tax reduction being it eases their work and makes it more successful. Latest changes in wage tax policy occurred in early 2007, when the rate was reduced from 14 to 12 percent, and when non-taxable level of earning of 5.000 dinars was introduced (annually adjusted). The result of this measure was lowering tax and contributions burden on average net wage in the Republic from 74 to 64 percent. In the same month of wage tax reduction, significant increase in earnings was recorded, meaning that major part of the ease was not used for what this measure was aiming at: on competitiveness increase, and on increase of employment and legalization of labor. Also, this has caused budget revenues reduction for 1 percent of GDP annually.

The wage and contribution burden in Serbia is at average Central and Eastern Europe level. Although most important is overall level of levies, in that structure wage tax burden is lower than regional average, while contributions are relatively higher. That would imply that possible local economy's lack of competitiveness or low level of employment can not be explained by wage tax policy measures.

Even though I am not arguing the need for further amendments and reforms in the area of wage taxation, I have to point out that above mentioned initiative for rate reduction from 12 to 10 percent, followed with increase of non-taxable earnings level to 8.000 dinars, leads to budget revenues reduction for 0.7 percent of GDP annually. With public spending rigid structure additionally burdened with latest announcements of more generous public spending, budget deficit would increase, followed with public debt increase, and stability would be jeopardized. Thus, the option is to make the amendments regulating wage taxation while not jeopardizing public revenues, i.e. a parallel solution for shortage compensation should be found.

Tax treatment on wages in Serbia is not progressive enough. Total number of citizens' tax returns referring to the registration of triple average wage earnings in 2007 (1.4 million dinars) is somewhat above 20,000, which is some 1 percent of total number of employed persons in Serbia. At the same time we are looking into ways of reducing tax burden on lower earnings in economically active branches aimed to increase level of employment, competitiveness and exports. One of the ways is to introduce single, but increased wage tax rate and a significant increase of non-taxable earning levels.

That would make wage taxation more progressive and reduce burden on lower wages, while budget revenues would not be significantly jeopardized. Let me illustrate it with two examples of earning levels. Let the tax rate be 20 percent and non-taxable share 15,000 dinars. Salary of 30,000 dinars would have effective rate of 10 percent, while 200,000 wage would have effective rate of 18.5 percent. Although, other solutions are also feasible.