Republic of Serbia

Fiscal Council

ANALYSES, POSITIONS AND SUGGESTIONS

September 29th, 2022

PROPOSED SOCIAL AND TAX POLICY MEASURES FOR REDUCING INEQUALITY AND POVERTY IN THE REPUBLIC OF SERBIA

EXECUTIVE SUMMARY

The crisis caused by the COVID-19 pandemic has shed further light on the problems of inequality in a multitude of countries, including Serbia, where inequality and at-risk-of-poverty rate have stood above the European average for years. In this analysis, the Fiscal Council points out the possibility and necessity for systemic improvements in social and tax policy that would provide additional support to impoverished households, particularly having in mind the recent food and energy price hikes.

Persons under the age of 18 make up the age group that faces the highest at-risk-of-poverty rate of 24.2%, which is notably higher than that of the general population (21.7%). In order to reduce child poverty, increasing *child benefits* and expanding the programme's coverage should be established as a clear priority. Accordingly, a 25% increase in child benefits and a strong expansion of the program by over two-thirds, from the current 245,000 to about 415,000 children would decrease the at-risk-of-poverty rate for children below the level of the general population – to 19.1%. This additional expense brought on by such reform would amount to 14 bn dinars and these funds are possible to make room for in the 2023 budget.

The data show that the number and the extent of material deprivation of senior citizens without retirement income are exaggerated in the general public, while material deprivation of the elderly with low pensions and/or dependent family members, particularly those in rural areas, is not sufficiently recognized. It is necessary to relax the excessively strict property criteria for *financial social assistance* in the case of elderly households by, for instance, raising the permitted land ownership from 1 to 10 hectares. As an additional support measure, we propose the abolishment of pension and disability insurance contributions for agricultural households that own less than 10 hectares of land. The recent introduction of social maps allows the state administration to efficiently implement this improved system of social protection for elderly households at a modest cost of only several billion dinars annually.

As a way to support low-wage earners and/or income taxpayers with dependent family members, the Government could adopt a more progressive tax schedule, as well as a systemic personal income tax reform in line with the best European practice. The basic reform scenario includes doubling the personal allowance, from 19,300 dinars to 40,000 dinars per month, and introducing an additional allowance for dependent family members. In order to maintain tax revenue at an unchanged level, the reform would also propose a limited increase in the personal income tax rate from 10% to 15%, which would not undermine the competitiveness of the domestic labour force. Such a reform would reduce the tax burden for persons with a dependent spouse and two children earning the average wage from the current 61.3% to 45% of the net salary.

Brief summary of proposed measures for reducing inequality and poverty

Issue	Outline	Recommendation
Inequality and at-risk-of-poverty rates in Serbia are notably higher than the European average	The at-risk-of-poverty rate in Serbia is 21.7% - higher than both the EU and the Central and Eastern European average which stand at 16.6% and 16.5%, respectively	- Increase in the expenditure for social protection from 3.0% to about 3.3% of GDP to expand social programme coverage and increase the amount received by the beneficiaries - Apply a more progressive tax schedule to raise the incomes of persons with the lowest wages and/or dependent family members
Persons under the age of 18 represent the most vulnerable age group with the highest at-risk-of-poverty rate	The at-risk-of-poverty rate for children stands at 24.2% and exceeds both the at-risk-of-poverty rate for working-age persons (aged 18 to 64 years) which amounts to 20.9% and for those older than 65 which amounts to 22.0%	- Increase child benefits by 25% (from 3,569.3 to 4,500 dinars) and raise the number of beneficiaries by two-thirds, from 245,000 to 416,000 children - The total cost of the proposed measures would amount to 14 bn dinars and is possible to make room for in the 2023 budget - This reform would reduce the at-risk-of-poverty rate to 19.1%, i. e. below the average for the general population
Approximately 37,000 senior citizens, predominantly in rural areas, do not receive financial social assistance despite very low income	Excessively strict property criteria, primarily concerning land ownership, prevent a large number of vulnerable elderly households from exercising the right to financial social assistance	- Relax the property criteria and raise the upper limit for land ownership from 1 to 10 hectares for elderly households - Apply social maps to ensure that social security reform is efficiently implemented - Abolish the legal obligation to pay pension and disability insurance contributions for insurants in agriculture sectors
Labour market inequality and inadequate support to the most vulnerable workers, i. e. those who earn low income and have dependent family members	The Serbian tax system has fallen behind the European practice and does not allow for tax allowances for dependent family members, while the current personal allowance is relatively low compared to the average salary	Reform the personal income tax and increase the progressivity of labour income tax - Double the personal tax allowance, from 19,300 to 40,000 dinars per month - Introduce an additional tax allowance in the amount of 20,000 dinars for each dependent family member - Raise the tax rate from 10% to 15%, which would prevent a drop in tax revenue and would not undermine the competitiveness of the domestic labour force