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## Amendments to the Law on Personal Income Tax - introduction of the so-called “test of entrepreneur’s independence”

Employment

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Currently, there is an ongoing process in the Republic of Serbia regarding change of the tax legal framework. In that respect, as of 1 November 2019, the Draft Law on Amendments to the Law on Personal Income Tax (the “Draft”) is in the procedure before the National Assembly of the Republic of Serbia, which was previously adopted by the Government of the Republic of Serbia (“Government”). The most significant novelty in the Draft is the announced change to the system of flat-rate taxation of self-employed income. Namely, the Draft explicitly states that the term “other income” inter alia means a remuneration received by an entrepreneur on the basis of carrying out activities for the same principal – a domestic or a foreign legal entity, provided that this entrepreneur fulfils at least 5 of 9 criteria which represent the test of independence. If, however, the entrepreneur does not meet 5 of the 9 criteria, then the general taxation regime continues to apply.

Article 85 of the Draft inter alia introduces the so-called test of entrepreneur’s independence. Namely, the purpose of this test is to determine whether the entrepreneur earns income from self-employment or he/she is actually employed. The criteria for the test of entrepreneur’s independence (in short form) are as follows:

1. The principal determines the working hours of the entrepreneur, or vacations and leaves of the entrepreneur are dependent on the decision of the principal;
2. The entrepreneur usually uses the premises provided by the principal or performs work in the place designated by the principal;
3. The principal organizes vocational training for the entrepreneur;
4. The principal has engaged the entrepreneur by advertising in the media the need to engage natural persons or through an intermediary (e.g. through the employment agency);
5. The principal provides its own essential tools, equipment or other essential tangible or intangible assets required for regular work of the entrepreneur, or the principal usually manages the work process of the entrepreneur;
6. The entrepreneur obtains at least 70% of the income from one principal for the period of 12 months beginning or ending in the tax year concerned;
7. The entrepreneur performs activities in the field of the principal’s business, and for such activities his/her service agreement does not contain a clause under which the entrepreneur bears the usual business risk for the job delivered to the principal’s client;
8. There is some form of non-compete clause (partial or full) in the service agreement, i.e. prohibition of providing services under the agreement with other principals, except for a partial prohibition on the provision of services to a limited number of the direct principal’s competitors;
9. The entrepreneur has been engaged with the same principal continuously or intermittently for 130 or more working days for the period of 12 months beginning or ending in the tax year concerned, whereby doing activities on one working day is considered as activities in any period during that working day between 00 and 24 hours.

If the entrepreneur fulfils at least 5 of the aforementioned 9 criteria, he/she will not be considered as independent, and in that case the income this entrepreneur receives will be taxed as other income in accordance with Article 85 of the Law on Personal Income Tax (the “Law”). Further to that, the contributions for pension and disability insurance at the rate of 26% will be also calculated on this other income, as well as the health insurance contributions at the rate of 10.3% if the entrepreneur is not insured under another basis. By introducing this new legal solution, the legislator has opted to tax the income of the entrepreneurs who do not pass the test of independence as the “other income”, where the tax rate of 20% applies, along with the respective social contributions.

The Draft was proposed by the Government in order to suppress the “grey economy”, create conditions for more efficient suppression of illegal work of natural persons, as well as stimulate the employment. A lot of public attention has been attracted in the previous period regarding this Draft, especially in the IT sector.

One of the drawbacks of the Draft regarding novelties in Article 85 is its unpredictability, primarily because the criteria regarding the test of entrepreneur’s independence are very general and subject to different interpretations. In general, the tax inspectors will have a control function, i.e. they will control whether the test of entrepreneur’s independence has been done according to the regulations, which would inevitably cause a significant level of legal uncertainty.

As per the application date, the Draft prescribes 1 January 2020 as the date of application, while the

regulations for its implementation of the Draft are to be adopted within 120 days from the day this Draft enters into force. However, according to the Draft, the income paid to the entrepreneur within the meaning of Article 31 of the Law (self-employment) ending with 1 March 2020 will be considered to be a income from self-employment regardless of the nature of his/her relationship with the principal within the meaning of Article 85 of the Law. Therefore, the actual implementation of the test of entrepreneur's independence will be postponed until 1 March 2020. Of course, it remains to be seen whether the National Assembly will adopt this Draft and in which form. It is expected that the Draft will be adopted by the end of this year.