

# Reform of Kosovo Tax System after Independence and its key functions

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## Abstract

In this paper we have analyzed the initial circumstances which characterize tax system in Kosovo after independence. After the Declaration of Independence, it is of the paramount importance that Kosovo has undergone through a reform of policy and tax system by exploring more seriously the economic functions.

However, policy and tax system of Kosovo should be more in function of economic development by achieving equilibrium between direct and indirect taxes, increasing efficiency of public expenditures and to offer more tax incentives. Designers' preliminary requirement is to analyze fiscal, economic, etc., effects of each tax form which aims to apply in accordance with tax policy objectives and to analyze the role and effects of tax incentives to each tax form. Taking into account that Kosovo regarding the application of tax incentives of CIT, compared with other countries is the last, designers by using the experiences of other countries should apply more tax incentives in order that tax policy to be more in function for economic development.

**Key words:** tax policy, tax system, tax reform, indirect taxes.

## 1. Introduction

The Balkan states, in distinction to other European countries, made the economic transition, including tax reforms, under the influence of quite specific political factors and circumstances. Reformation of taxation systems constituted only one of the main components of the reforming process within the social-economic transition. The designing of an appropriate and functional taxation reform has not been an easy objective to be reached in any of the Balkan countries. This is due to the fact that all post-communist countries possessed taxation systems drafted for the planned economy and incompatible with the market economy and with a tax administration which needed a complete reorganization for the purpose of a successful operation in new conditions<sup>1</sup>. Difficulties have especially risen in making the reforms acceptable and then successfully implementable. Every Balkan country, involved in making a tax reform, went through a specific path, different from another country.

Each tax reform in each country, therefore, bore in itself certain features. However, the trends were common. In this context, all the Balkan countries in different years applied VAT, corporate income tax, and personal income tax in their tax systems.

In the long historical context, the policy and tax systems of Kosovo were followed during their evolution by many changes that were made based on the challenges of the political and socio-economic structure of Kosovo (initially the structure on the Federal basis, then the structure by the UNMIK administration), as well as those of socio-economic relations in the production process.

The transition process, which in early '90s encompassed many countries of Southeastern Europe, found Kosovo initially in a situation of an undeclared war, which broke out in 1998 and ended with the Kumanova Agreement (Military Technical Agreement) on 10<sup>th</sup> June 1999. On 10<sup>th</sup> June 1999, the UN

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<sup>1</sup> For tax reforms in Balkan countries see - Grabowski M., Tomalak M., Tax reforms in the countries of the central Europe and the Commonwealth of Independent States, [w:] New Europe - Report on Transformation, Instytut Studiów Wschodnich, Warsaw, 2004; Orłowski, L. and Elgar, E., Transition and Growth in Post-Communist Countries - The Ten Year Experience: Cheltenham, UK and Northampton, MA, USA, 2001; Nord, R., "Central and Eastern Europe and the New Financial Architecture", Finance and Development, 2000, Vol. 37, No.3; Dabrowski, M. and Radziwill, A., International public goods for economic development: the case of post-communist transition, Poland: Center for Social and Economic Research - Paper Prepared for the Conference on 'International Public Goods for Economic Development', Weatherhead Center for International Affairs, Harvard University, September 7-8, 2005; Tanzi, V., Transition to Market - Studies in Fiscal Reform, Washington : IMF, 1993; Bruno S. Sergi, "The Balkans Jump on the tax Rivalry Bandwagon", SEER, 01/2005, fq. 7-18. Cited by Bedri Peçi, Tax reforms in Balkan countries - Kosova case, Thesis Kosova, no.2,2009, pp.46.

Security Council approved Resolution 1244, by which UNMIK was created<sup>2</sup> and therewith the sovereignty of the SFRY over Kosovo was abolished. Until final status settlement (2008), resolution 1244 vested UNMIK with legislative, judicial and executive powers<sup>3</sup>. Upon UNMIK installation in Kosova, the Central Fiscal Authority in cooperation with World Bank, The European Commission and the International Monetary Fund, started the work in formulation of measures and strategy for creating an efficient tax system in the spirit of the overall economic and social development of Kosova. The creation of the policy and tax system in Kosovo by UNMIK is a *sui generis* case, as it was created in practice without any internal influence and without a political dialogue of Kosovar actors.

The highest authority of the fiscal power in Kosovo from 1999 till the Declaration of independence of Kosovo, on 17.02.2008, was the Special representative of the Secretary General (SRSG) of the UN together with the Fiscal Economic Council as an advisory body to the SRSG for fiscal policy issues<sup>4</sup>.

Fiscal policy of Kosovo, which was set in 1999 by UNMIK, has had only fiscal functions, and not the function of economic development.

After proclamation of independence, the fiscal sovereignty moves from UNMIK to the Kosovo Institutions, respectively to the Parliament of Kosovo, as the greatest taxing power in applying taxes through tax laws. In this way, Kosovo institutions inherited a policy and tax system designed by UNMIK, which mainly had fiscal functions. This, due to the fact that the main objective of policy and tax system was gathering funds for financing foreseen public costs, by not giving importance to the economic and social functions which can be achieved through policy and tax system. So, policy and tax system inherited from UNMIK had a very limited function vis-à-vis socio-economic needs of Kosovo and trends of taxing competition in Balkan countries. In such a situation, creators of tax policy of independent Kosovo were forced to consider the reformation of system and tax policy. In this context, after proclamation of Independence, Kosovo government has made the first tax reform. Therefore, the aim of this analysis is highlighting some of basic specifics which characterize policy and tax system in Kosovo, after proclamation of its independence in the case of its reformation. For this purpose we have made these questions: which are the specifics which characterize tax structure of Kosovo tax system before and after the independence proclamation? Which are

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<sup>2</sup> See UNMIK at a Glance, ed. 2007, [www.unmikonline.org/intro.htm](http://www.unmikonline.org/intro.htm) [16 October, 2013]

<sup>3</sup> UNMIK Regulation 1999/1, On the Authority of the Interim Administration in Kosovo.

<sup>4</sup> Melinda Bair, Tax Policy as a Mechanism to Secure Kosovo's Independence: A Proposal to Reform the UNMIK Tax Regulations, (2013).

the components that constitute tax reform? Which are tax incentive measures that are applied in the tax system of Kosovo?

In this analysis we have used the research method of case study, based on theoretical and empirical data. Furthermore, the methodology of the research is based on analyzing taxing laws based on which the system and fiscal politics are developed, as well as reports of Ministry of Finances. For comprehensive purposes the analysis of case in Kosovo was made based on different papers which talked about transition countries, based on reports of IMF, World Bank, reports of Ministry of Economy and Finances, as well as other secondary sources.

Apart from introduction, paper is laid out as follows: Part II analyzes the structure of Kosovo tax system after independence. Part III presents the overview of tax reforms in selected Balkan countries - Kosovo Case. Part IV has to do with an analysis of Tax incentives - the Kosovo Case. At the end conclusions are given.

## **2. Tax structure of Kosovo tax system after Independence**

The countries in transition have applied different tax forms as far as the selection of their tax structure is concerned. Countries with higher per capita income and with a more developed tax administration have a tax structure resembling more the European Union countries. This was a result of the efforts of these countries to become the EU members through the harmonization of their tax systems, whereas countries with lower income (revenues) and with a poorer tax administration have built their tax structure on the basis of indirect taxes<sup>5</sup>. For the purpose of analysing the development of Kosovo tax structure after independence, we have analyzed it for the years 2007, 2011 and 2012. From the analysis of tax forms that existed before independence, in 2007, the indirect income tax has in general prevailed.

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<sup>5</sup> Bedri Peçi, Tax reforms in Balkan countries - Kosova case, Thesis Kosova, no.2, 2009, pp .46.

**Table 1:** Estimated tax income (revenue) according to the consolidated budget for 2007 and tax income accomplished for the period 1 January-31 December 2007

Total budget of Kosova 2007	Estimated	Accomplished	% of accomplished	
Total income (revenue)	682.8	894.22	130.96%	
Central budget income (revenue)	654.8	789.99	120.65%	
Income from taxes	578	711.09	123.03%	79.52%
Internal tax income	140.2	180.49	128.74%	25.38%
Border tax income	437.8	530.6	121.20%	74.62%
Non-tax income	40.8	53.2	130.39%	

Source: The book on the budget of 2007, Ministry of Economy and Finance, 2007, p.176; Financial Statement of budgetary accomplishment for 2007, Ministry of Economy and Finance 2008, cited by Bedri Peci, Tax reforms in Balkan countries - Kosova case, Thesis Kosova, no.2, 2009.

From the shown data on table 1 for 2007, it can be seen that the policy and tax system that year relied on indirect tax basis as well. More than 74.62% of tax income was collected from border taxes, customs, VAT and excises. Despite many declarations of fiscal policy creators about the balancing of indirect and direct taxes, this seems far in the prospective, as only 25.3% of the income was collected from internal taxes, respectively from direct taxes. This was very clearly specified in the 2008 report<sup>6</sup> of the European Commission, which, referring to the tax system, says that there was lack of progress.

<sup>6</sup> Commission of the European Communities; Commission Staff Working Document - Kosovo (UNDER UNSCR 1244/99) 2008 Progress Report, accompanying the Communication from the Commission to the European Parliament and the Council - Enlargement strategy and main Challenges 2008-2009, COM(2008)674, pp. 35-36.

**Table 2:** Structure of General Public Incomes for the Years 2011 and 2012

	Revenues 2012	Structure 2012	Revenues 2011	Structure 2011
	€ '000	%	€ '000	%
Customs	844,861	55%	827,704	64%
<i>Customs refunds</i>	(2,074)	0%	(1,112)	0%
Tax Administrations	283,915	18%	261,134	20%
<i>Refunds from tax administration</i>	(32,763)	-2%	(29,774)	-2%
Central level –non tax revenues	41,145	3%	45,525	3%
Municipality own revenues	59,448	4%	55,621	4%
Own revenues – central level	44,835	3%	59,912	5%
Dividends	45,000	3%	60,000	5%
Dedicated revenues of KPA	16,248	1%	-	0%
One of revenues from KPA	28,934	2%	-	0%
Return of loans from the public enterprise	4,000	0%	-	0%
Proceeds from the issuance of the securities	73,313	5%	-	0%
Loans from IFI	93,677	6%	5,076	0%
Grants for budget support	37,417	2%	19,240	1%
<b>Total revenues</b>	<b>1,537,955</b>	<b>100%</b>	<b>1,303,328</b>	<b>100%</b>

Source: Treasury, Ministry of Finance, 2013

From the analysis of the structure of Kosovo's general public incomes, after the proclamation of the independence, it appears that before and after the proclamation of the independence, indirect taxes have dominated, as well as Customs and VAT. In the year 2011 and 2012 we had the same report of participation for direct and indirect taxes such as in previous years.

From the data in the table for the year 2012, it is shown that the policy and the tax system, also after the independence, continue to be based on indirect taxes. Almost 55% of incomes from taxes are gathered from border indirect taxes, customs, customs VAT and excise. From the data given for the level of income gathered from internal taxes (no border) in year 2012, which is 18% of general budget incomes, it results that declarations of creators for carrying tax burden from border to the inside, respectively for creating an internal tax system, still remains far away from achieved. Differently from the year 2012, in the year 2011, the incomes from indirect border taxes were even bigger, respectively they were taking part in general budget incomes with 64%, while tax incomes from the internal taxes were taking part in general budget incomes with 20%. Such structure, was impacted by the low level of incomes, not well consolidated tax administration, as well as the inherited aim from UNMIK, which was the accomplishment of fiscal functions, respectively gathering of foreseen funds, not taking in consideration other functions of fiscal policy, such as those economical, social, etc.

### 3. Tax reforms in selected Balkan countries – Kosovo Case

The Balkan countries, similar to the European countries (states) and other states of South-Eastern Europe constantly reformed their tax systems by reducing the rates, redefining the tax bases, and making amendments and clarifications of the existing laws interpretation. Parallel to the reduction of tax rates, the reduction of tax deductions and exemptions, as counter-reimbursement for the tax rates reduction, was made. In this sense, in the following table we have presented the tax rates reformation in the selected Balkan countries and Kosovo. In the process of tax systems reformation, among other things, two trends should be distinguished –a) the trend of reduction of the main tax rates with a special emphasis on corporate income tax, and b) the aspiration and acts of all the Balkan countries for membership in EU, by adopting the EU rules.

The Government of Kosovo has since 1<sup>st</sup> January 2009 changed only tax rates of main existing taxes, respectively has reduced tax rate of Corporate Income Tax (CIT) from 20% to 10 %, has reduced tax rate of Personal Income Tax (PIT) from 0%, 5%, 10% and 20% to 0%, 4%, 8% and 10%, which means that the highest rate of this tax will be 10% for taxpayers' and business activities. In contrast to above mentioned taxes, tax rate of VAT was increased from 15% to 16%.

In this sense, in the following table we have presented the tax rates reformation in the selected Balkan countries and Kosovo.

**Table 3:** The main changes in personal income tax rates, corporate income tax rates and VAT in the Balkan countries from 1992-2013

Country	Personal Income Tax	Corporate Income Tax	Value Added Tax
<b>Albania</b>	Preliminary 6 rates – 5% to 30% each. Since 1 July 2007 the rate is 10%	Preliminary it was 30% then 20%, whilst since 1 January 2008 the rate is 10%	1996: the rate is 20% and 0%
<b>Bulgaria</b>	1992: 6 rates 20%, 24%, 28%, 32%, 36% and 40% 4 rates from 20% to 40% 2002: the rate from 0% to 29% since 2008 it is 10%	2000: 25% the rate, 20% for small businesses, 2002: the rate 23.5% then it was 15%, whilst since 1 January 2007 it is 10%.	1994: the rate 22%, 1999: reduced to 20%, exempted
<b>Croatia</b>	1994: 0:00 2001: 3 rates 15%, 25%, 35% 2003: additional rate 45% %; From 1 January 2011 (but applied in respect of	1994: the rate 20%	1998- The rate 22%, 0%: Currently the standard VAT rate is 25%.

	withholdings from 1 July 2010) to 29 February 2012 the following progressive rate structure applied 12%,25%,40%:For the period 1 March 2012 to 31 December 2012, the following progressive rate structure applied 12 %, 22.83,25%,37.5%, and 40%: From 1 January 2013, the following progressive rate structure applies:12%,25%, 40%.		
<b>Macedonia</b>	2 rates: 15% dhe 18% (earlier: 3 rates from 23% to 35%) 2002; rates from 0% to 38%; then there were progressive rates 15%,18% and 24%; from 1 January 2007 to 1 January 2008 it was 12%, whilst from 1 January 2008 is 10% .	Earlier 30%; then 15%; in 2007 it was reduced to 12%; in 2008 it was reduced to 10% as much as it is currently	2000: the rate 19%, reduced rate 5% for food products for humanitarian purposes, agricultural tools and mechanisms, books. Currently the standard VAT rate is 18%.The reduced VAT rate of 5% applies to the supply of specific goods and services.
<b>Romania</b>	2003: 5 the rates : 18%, 23%, 28%, 34% dhe 40%; now it is 16%	2003: the rate 25% (earlier 38%) currently is 16%	1993: the rate 22 % and 11% reduced rate; 2003: the rate 19% and 9% reduced rate. Currently, the standard rate of VAT is 24%. A reduced rate of 9% is applicable to the supply of books, manuals, newspapers, medicines, cinema tickets and to the supply of hotel services.



<p><b>Serbia</b></p>	<p>The annual aggregate taxable income is exempt from tax up to an amount equal to three times the average annual salary. The average annual salary for 2012 was RSD 689,160. The estimated average annual salary for 2013 is RSD 750,495.</p> <p>The tax rates are 10% on income between 3 and 6 average annual salaries and 15% on income above 6 salaries.</p>	<p>Preliminarily: 20% - 30%; 2003: the rate was 14%; Since 1 January 2013 Corporate income tax is levied at a rate of 15%.</p>	<p>Preliminarily the sale tax with rates 20%, exempted public utilities and some food: from 2005 it is applied VAT by 3 rates: 18%, 8% and 0% for medicines, books. Currently, the standard rate of VAT is 20% (18% before 1 October 2012). The reduced rate of 8% applies to listed goods and services, including basic foods, certain medicaments, fertilizers, school books, personal computers, public utility services and hotel accommodation.</p>
<p><b>Montenegro</b></p>	<p>Preliminarily the fixed rate 14 % of tax on earned income: from other income the rate of 10%, 15% and 20%.</p>	<p>Preliminarily rates: 20% - 30% 2003: the rate 14%. Currently, the flat rate applicable to the aggregate taxable income is 9%. However, for the period 1 January to 31 December 2013, a special temporary measure applies, under which salary above EUR 720 per month is subject to a 15% withholding tax</p>	<p>The standard rate of VAT is 19% from 1 July 2013 (17% before that date)</p>
<p><b>Kosovo</b></p>	<p>Preliminarily from 2002 : 4 rates 0%, 5%,10% and 20%; from 1 January 2009 reduced progressive rates 0%,4%,8% dhe 10%</p>	<p>Preliminarily from 2002: 20% rates for big companies and of course for small business: from 1 January 2009 reduced rate 10%.</p>	<p>2001: 15% and 0%,some exemptions; 2002-reduction for registration in turnover above 50.2000 euro; from 1 January 2009 rates 16% and 0%</p>

Source: Prepared by author according to Mitra, P. & N. Stern, Tax systems in Transition, WPS 2947, 2003; Këang-Yeol Yoo, Corporate Taxation of Foreign Direct Investment Income 1991–2001, OECD, ECO/ÉKP(2003) 19, Tesche, J. The Role of the State in South East Europe – Fiscal Issues, mimeo, US Treasury; VAT rates applied in the member and accession states of the European Community, DOC 2402/2003 EN, - cituar nga Grabowski M., Tomalak M., Tax reforms in the countries of the central Europe and the Commonwealth of Independent States, [ë:] New Europe - Report on Transformation, Instytut Studiów Èschodnich, v.c. fq. 279; Bedri Peci, Poreski podsticaj kao vazan segment poreskih reformi u balkanskim zemljama i slucaj Kosova, Godisnjak Pravnog Fakulteta u Sarajevu, LVI 2011; 2009 Index of Economic Freedom, February 2009: I. D. Lutilsky, *Croatia - Individual Taxation* sec. 1., Country Surveys IBFD; K. Estatiev, *Macedonia (FYR) - Corporate Taxation* sec. 1. Country Surveys IBFD. O. Popa, *Romania - Corporate Taxation* sec. 8. Country Surveys IBFD (accessed 5 Nov. 2013); I. Loncarevic, *Serbia - Individual Taxation* sec. 1. Country Surveys IBFD (accessed 5 Nov. 2013). I. Loncarevic, *Montenegro - Individual Taxation* sec. 1. Country Surveys IBFD (accessed 5 Nov. 2013). ; B. Peci, *Kosovo - Corporate Taxation*, Country Surveys IBFD (accessed 5 Nov. 2013).

Table number 3 shows that the main orientation of tax reforms in Balkan countries, was reduction of tax norms and that this was done mainly aimed at attracting foreign investors, respectively to create a competitive taxing system in Balkan region. The comparison of CIT norms of Serbia, Montenegro, Macedonia, Albania, Kosovo and Bosnia & Herzegovina, with average norms of EU CIT, we might say that Balkan countries have lower norms and that low norms of CIT can be qualified as tax incentive.

Regarding Kosovo case, creators of tax policy in January of the year 2009 did a reduction of tax norms in two main forms of direct taxing, CIT from 20% to 10% and Personal Income Tax from 0%, 5%, 10% and 20% to 0%, 4%, 8% and 10%.

At CIT, creator's aim was that through reduction of tax norm, to increase the competition capacity of Kosovo vis-à-vis foreign direct investments, respectively CIT norm to be harmonized in the level of existing norms of CIT that were already existing in Balkan countries.

At the case of PIT creator's aim was to achieve another objective; that of fighting fiscal evasion, respectively attracting tax subjects so that by stimulating with tax burden they move from subjects of gray economy to subjects that manage to carry out their tax obligations.

Unlike two above-mentioned forms, by the increase of VAT norm from 15% to 16% creators had fiscal intentions, respectively the aim was to do the

compensation of public incomes that would be lacking along with decreasing of tax norms of CIT and PIT.

Except decreasing of tax norms, Balkan countries have applied few numbers of tax incentives in order to simulate foreign investors, which we will address onwards.

#### 4. Tax incentives - the Kosovo Case

In function of accomplishing such intentions, Balkan countries in their tax systems have applied various mitigating measures that in tax theory<sup>7</sup> are known as tax incentives. Taxing incentives are included in various forms, which are presented as tax relief, tax holidays, and reduction of tax base, or relief from tax obligation. Tax incentives are instruments with which countries are served aiming at favoring specific categories of tax payers (specific sector, enterprise or individual) and in function of simulating specific economic activities.

Through tax incentives, the state intentionally accords for reduction of public incomes which will have in disposition. This for the fact that state achieves the same effect if it would gather this portion of taxes, and which later through budgeting costs in indirect manner it would share through subventions for sectors and specific activities. The incentives' application causes decrease of budgeting incomes and this phenomenon in tax theory is called tax expenditure. In tax theory, single and accepted definition related to tax expenditures doesn't exist. In this context, most proper definition would be that tax expenditures include all the measures, which are undertaken in the existing tax form with which losses of budgeting income are caused due to decreasing of taxing base or tax obligation. In this case a portion of incomes isn't calculated at all, as it flows from specific tax form.

This part of incomes that is not calculated and isn't gathered from this specific taxing represents what is called tax expenditure.

While, according to the classic tax theory, tax incentives do not have any important role in simulating investments and economic developing, in contemporary tax theory, tax incentives are seen as very important and influential in this direction.

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<sup>7</sup> H.H. Zee, J.G. Stotsky, E. Ley, E., "Tax Incentives for Business Investments: A Primer for Policy Makers in Developing Countries", *World Development*, 2002., 30(9): p.1497-1516; A. Easson, "Tax Incentives for Foreign Direct Investment", Kluwer Law International, The Hague; London; New York, 2004; *Tax Incentives and Foreign Direct Investment: A Global Survey*, ASIT Advisory Studies No. 16, UN, 2000, New York-Geneva, 2000, p.19-22 cited by Bedri Peci, Poreski podsticaj kao vazan segment poreskih reformi u balkanskim zemljama i slucaj Kosova, *Godisnjak Pravnog Fakulteta u Sarajevu*, LVI 2011, pp. 250.

More specifically, in old tax theory there is a conclusion that role of tax incentives in relation with foreign investments is secondary compared to basic determinants, such as the size of a state, approach in unwrought materials and availability of a qualified working force.

Investors, in general, attempt to adapt two-steps process in the case of evaluation of one state, as a country for investments. In the first phase, they analyze country based on its basic determinants.

Only those states that have been through these criteria are taken into consideration in the future phase of evaluation, where tax norms, grants and other incentives can be important. Therefore, tax incentives in relation with foreign investments only have the secondary importance.

Different from classical theory, contemporary theory<sup>8</sup> sees tax incentives as a very important factor and decide in this direction. As a base of such stance is the fact that in globalization area, all the countries have undertaken the same measures, as states with full investments, as well as also for economical-regional intentions they have undertaken same measures with those of European Union, where the process of tax harmonization and mutual economical politics are more intensive than ever.

In tax systems of Balkan countries since the beginning of the process of tax reforms, an important number of tax incentives are applied and are still being applied with added intensity.

In this context, tax incentives mainly are related to Corporate Income Tax (CIT).

Relevant literature about tax incentives to CIT, have grouped the tax incentives in few groups such as: reduced norms of CIT, taxes decreasing, incentives for investments in a wide concept, which covers tax incentives as an accelerated amortization, tax credits in disposition for investments, decrease for qualified expenditures, decrease or zero norm, amortization based on employment, etc.

The role of tax incentives of CIT at the foreign direct investments promotion has been the object of various studies, but their disadvantages and advantages never have been clearly defined. In practice, spectacular successes have

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<sup>8</sup> See in general, - UNCTAD-DTCI. Incentives and Foreign Direct Investment. Geneva and New York: United Nations Publications, E.96.II.A.6, 1996; OECD. Investment Incentives and disincentives: Effects on International Direct Investment. Paris: OECD, 1989; Anwar Shah, ed. Fiscal Incentives for Investment and Innovation, New York: Oxford University Press, 1995; J. Alm, J. Martinez-Vazquez & M. Rieder (ed.), "The Challenges of Tax Reform in a Global Economy", New York: Springer, 2006; J.H. Mutti, "Foreign Direct Investments and Tax Competition", Institute for International Economics, Washington, 2003; Bedri Peci, Poreski podsticaj kao vazan segment poreskih reformi u balkanskim zemljama i slucaj Kosova, Godisnjak Pravnog Fakulteta u Sarajevu, LVI 2011, pp.251-252.

happened as well as important deviations in the application moment of tax incentives of CIT in attracting foreign investments.

Another issue that needs to be stated is lacking of proper analysis and reports for tax expenditures that Balkan countries have in the moment of application of tax incentives. While analysis and reporting of tax incentives in developed countries is done regularly in budget process, this doesn't happen in developing countries. And even if Balkan countries do this, these analysis and reports are not adequate and are not described in details.

In the context of this analysis for comparison of Kosovo case the main emphasis will be put just upon tax incentives to CIT. A great number of tax incentives are applied inside of this tax form in contemporary tax systems of the world, excluding Kosovo that still applies them very poorly (Table no. 2)

**Table 4:** Types of tax incentives applied in the world and Kosovo case

Tax incentives	Developing countries (52)	Developed countries (51)	Total (103)	Kosovo
Reduced CIT rates	43	40	83	Is applied to CIT
Tax holidays	37	30	67	Doesn't apply
Accelerated depreciation	26	21	47	Doesn't apply
Investment allowance	18	8	26	Doesn't apply
Social security reductions	5	7	12	Doesn't apply
Import duty exemptions	39	24	63	Doesn't apply
Other	32	13	45	2

Source: Easson (2004) cited by H. Simovic & M. M. Zaja, Tax Incentives in Western Balkan Countries, World Academy of Science, Engineering and Technology 66 2010, Kosovo case is prepared by author according to Kosovo Tax Law.

Note: The majority of more than hundred existing types of tax incentives presented above are actually CIT incentives. In the case of Kosovo tax incentives are presented by referring exclusively to CIT.

In the given table, it can be seen that Kosovo in comparison to the compared countries, applies tax incentives very little, by making that policy and tax system in this segment not being in function of economical development.

From the study done by the American Chamber of Trade through surveying companies which have invested in Western Balkan and Southeast Europe it shows up that one of the main causes of hesitations to invest in Kosovo is the non-existence of enough tax incentives, respectively disadvantaged tax environment<sup>9</sup>.

## 5. Conclusions

In the year 1999 in Kosovo was installed Temporary Mission of United States (UNMIK) which until the proclamation of Independence of Kosovo in February of the year 2008 was creator of fiscal policy. Kosovo's fiscal policy that was created in year 1999 by UNMIK had just few fiscal functions and wasn't in function of simulation of economic development. This due to the fact that the main objective of the policy and tax system was gathering of funds for foreseen public expenditure financing, by not giving an importance to economic and social functions which could be achieved through policy and tax system.

After the proclamation of independence in 2008, it's of a high importance the fact that Kosovo was approached to the reformatting policy and tax system, making Kosovo economy more competitive. In this context creators of tax policy in January of the year 2009 did a reduction only of tax norms for two main forms of direct taxing, CIT from 20% to 10% and Personal Income Tax from 0%, 5%, 10% and 20% to 0%, 4%, 8% and 10%, and increasing VAT norms from 15% to 16%, as indirect tax.

Tax incentives are instruments with which countries are served aimed at favoring specific categories of tax payers (specific sector, enterprise or individual) and in function of simulating specific economic activities. Kosovo compared with other countries is the last, regarding the application of tax incentives of CIT.

Tax evasion is in high proportions. Reduction of tax rates on PIT is not producing the expected results.

In the following, for each finding we have given adequate recommendation:

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<sup>9</sup> Zeka, A, dhe Hapciu, V, Cakuli, H (2010), Kosovo in the eyes of foreign investiture's, American Chamber of Commerce ,pp. 1-20.

- Even though tax reform of the year 2009 has made Kosovo economy more competitive, policy and tax system in Kosovo should be also reformed in many other segments. This due to the fact that the main aim of fiscal policy still remains realization of fiscal functions, respectively gathering of foreseen funds without taking into consideration economical functions of tax policy, with a tax structure where majority of tax incomes come from indirect taxes and where few tax incentives are applied. Kosovo should make dynamic activities for achieving the balance between direct and indirect taxes and creating a tax system that would have neutral approach on competition and trade economy.
- Due to the fact that Kosovo compared with other countries is the last, regarding the application of tax incentives of CIT, creators by using the experiences of other countries must apply more tax incentives (Tax holidays, Accelerated depreciation, Investment allowance, Social security reductions, Import duty exemptions) in order that tax policy to be more in function economic development.
- Creators must as soon as possible create a strategy for combating tax evasion, where legislative and institutional measures must be introduced, in contrary tax evasion will continue to reduce its tax base, which is already small. As combating tax evasion can be efficiently implemented only by synergizing the legislative actions in all the areas of taxation, such as commercial, financial, and criminal law, this strategy must include institutional measures that interfere in all of those areas. So at the same time, institutions as the Ministries of Finance (Tax Administration), Justice and Interior must cooperate to effectively address the issue of tax evasion in a wide range of areas. Therefore it is important not only to take unilateral actions, but also to encourage wider cooperation among all stakeholders and raise awareness of the whole society to participate. Particular significance in the context of these multidimensional measures of strategy must be paid to increasing tax education of citizens through awareness on the role that tax payments have for public benefit.

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