Article title: Fiscal system and policy, with a special focus on Kosovo
Authors: Arijeta Neziraj Elshani[1]
Affiliations: Managing Director - Deposit Insurance Fund of Kosovo[1]
Orcid ids: 0000-0001-5765-5380[1]
Contact e-mail: Arijetaelshani84@gmail.com
License information: This work has been published open access under Creative Commons Attribution License http://creativecommons.org/licenses/by/4.0/, which permits unrestricted use, distribution, and reproduction in any medium, provided the original work is properly cited. Conditions, terms of use and publishing policy can be found at https://www.scienceopen.com/.
Preprint statement: This article is a preprint and has not been peer-reviewed, under consideration and submitted to ScienceOpen Preprints for open peer review.
DOI: 10.14293/S2199-1006.1.SOR-.PPO9JEU.v1
Preprint first posted online: 17 May 2022
Keywords: Fiscal Policy
Fiscal system and policy, with a special focus on Kosovo

by: Arjeta Neziraj Elshani
Managing Director at Deposit Insurance Fund of Kosovo

Abstract

As it is known, the fiscal system and policy are closely related to the socio-economic system of the country in which they operate. Therefore, each country has its own fiscal system and policy, which adapts to its socio-economic system and the achieved level of economic development. Although, regardless of these differences, there are also common elements, measures and instruments of fiscal policy. The fiscal system and policy are sub-systems of the economic system of the respective country and depend on it. However, the fiscal system and policy differ in countries with market economies and in countries with planned and directed economies.

Therefore, differences in the fiscal system and policy at the time of international integration processes-globalization, represent significant obstacles in economic transactions between different countries of the world. These changes are presented in the type of measures and instruments in the tax scope, in the structure of tax revenues, in the level of customs rates, VAT, the level of the tax rate in revenues, salaries, etc., as well as in facilities different that are implemented not linearly, but according to political relations that one country has with other countries. Globalization, respectively, international economic integration processes, are developing with great intensity, which are affecting the deepening of the advancement of national integration processes between the countries of the world which are facing certain problems in the field of legal infrastructure and fiscal policy instruments. There is no doubt that some fiscal policy measures and instruments play an important role in international economic transactions, but they can also be an obstacle to the internationalization of the flow of goods and services.

The role of the fiscal system and policy from the state point of view, is seen in fact as sources of budget revenues of a country that are provided mainly by the measures and instruments of fiscal policy. Also, the material (financial) position of economic entities significantly depends on the implemented fiscal policy. Therefore, fiscal policy enables the state public (budget) revenues, which allows them to meet the general and common needs of citizens, on one hand, and economic entities to carry out their activity and business, in the other hand.

In this paper, we have addressed public finances including in particular, fiscal system and policy. At the beginning we gave the definition and importance of public finances for the functioning of the state and economic - social development. A particular part of this paper is the fiscal system and policy, implemented in Kosovo in the post-independence period.
1. The notion and importance of public finances

As we know, public finances are among the oldest economic sciences, which deal with revenues and expenditures of the public sector, respectively the state. Economic and social development of any country regardless of the socio-economic system depends, respectively, is closely related to public finances, especially state administration and economic infrastructure (construction of roads, energy capacity, etc.) and social infrastructure (development of education, science, culture, health, administration, army, police, municipal activities, etc.). In other words, public finances serve the state to develop public goods. Public goods represent various public services performed by the state, as mentioned above. Public goods include all goods (services) that serve to meet the needs of the majority of population equally, regardless of nation, religion, race, and so on.

Therefore, public finances are defined as the activity of the state related to the collection of public revenues and the realization of public expenditures, in order to meet the general and common needs of its citizens. According to the economic lexicon, "public finance is a scientific branch which studies the nature and effects of the state's use of fiscal instruments: taxes, public spending, obtaining and granting loans, as well as purchases and sales on behalf of the state."

In a broad sense, public finances materially (financially) support economic and social development, in particular, the public sector, but it also happens that the private sector is assisted in the social sphere, providing financial assistance to the poor, as well as in cases of natural disasters. Hence, the state through public spending affects all ranges of economic and social life.¹

Historically, public finances have been born at a certain socio-economic stage of humanity. With the formation of the state, especially the presentation of money as the general equivalent of exchange, public finances also emerged. Therefore, public finances are related to the presentation and functioning of the state and money. In other words, public finances are closely linked to the functioning and role of the state, as the sole bearer of the collection and expenditure of public finances. Society is defined as a natural organism. In this context it should be emphasized that each individual is part of this organism and the state can be said to be its heart. Consequently, the individual matters only as part of the whole. Thus, the state, through various measures and instruments of fiscal policy, takes part of the subjective economic revenues and citizens, to create

¹Dr. Sabri Kadriu, Financat publike, Prishtinë, 2012, fq. 8.
public revenues, which serve to ensure its function, guaranteed by the highest legal act, which is the Constitution.

2. Fiscal system and policy - their function

**Fiscal systems.** The fiscal system is also part of public finances. As mentioned above, the fiscal system is closely linked to the existence of the state and its functioning. The fiscal system is part of the implemented economic policy and represents its sub-system.

The fiscal system has evolved along with the expansion of functions and the role of the state in socio-economic development. The fiscal system in itself "**includes all measures and instruments determined and implemented by the state in the field of public revenues**".\(^2\) In other words, the fiscal system must be such as to respond to the general and common needs, which the state must meet towards its citizens, and which must be in accordance with the material possibilities of the country's economy. All these needs have a public character, which require significant financial means. Therefore, for this reason, the state through the measures and instruments of the fiscal system, must provide financial means.

**Fiscal policy.** Fiscal policy is one of the most important segments of the economic policy. In a more general way, fiscal policy in itself includes all measures and instruments by which the state provides public revenues (budget revenues) for the economic and social development of the country. Relying on the form of state intervention we distinguish **active** and **automatic fiscal policy**. Within active fiscal policy, we have **expansionary** and **restrictive policies**. Expansionary fiscal policy is implemented when the country's economy is in the last stage of development, i.e. in the lowest stage of development called the recession phase, which is characterized by a lack of domestic products, high unemployment rate, low wages, foreign trade balance deficit etc. In this case, the state increases public spending through public works, which usually build roads, schools, hospitals, etc. With the opening of public works, aggregate supply increases, and at the same time aggregate demand, in which case the economic recovery begins. Although, in the case of this active expansionary policy, inflation may occur, which disrupts economic flows and reduces the

\(^2\) Dr. Musa Limani, Ekonomia e Kosovës-nëpër periudha historike, Kolegji i “Biznesi”, Fakulteti Ekonomik, Prishtinë, 2018, fq. 401.
purchasing power of consumers, then the state, among other measures, must reduce public spending, on one hand, while raising taxes (various taxes) progressively, in the other hand.\(^3\)

Automatic fiscal policy, meanwhile, is about the automatic operation of some fiscal policy instruments, depending on the change of the tax base. Fiscal policy has a short-term character, as opposed to a fiscal system that has a long-term character. Although, there is a close connection between politics and the fiscal system. Fiscal policy makes unilateral direct decisions about often short-term and less long-term interests. The fiscal system as a whole of instruments or forms of public revenues, achieves the long-term goals in economic and social development.\(^4\)

3. Tax system and policy

**Tax system.** The tax system is also closely linked to the state and its function. We call the tax system the entirety of harmonized, rational, effective, flexible and appropriate tax forms in achieving the economic and social development goals of a country.\(^5\) Both in the theory of financial sciences and in practical life, we distinguish several forms of the tax system. As a result, in practical life, we distinguish two views of the formation of the tax system: the monistic system and the pluralistic system.\(^6\) The first model has a historical character, whereas the first advocates of this system were the physiocrats. The second model is now used in every country and consists of many different types of taxes. Although, forms of taxes and their rates are not unique to all countries, they vary from one country to another. In defining the categories and rates of taxes, different factors influence, but mainly they rest on the structure and the achievement level of economic development of the respective country. Taxes have a mandatory character where every citizen is obliged to declare and make the mandatory payment of tax according to the tax base, respecting the time limit of collection. Therefore, based on what was mentioned above, it is not difficult to derive the definition of the tax system, which in itself "includes all types of levies, contributions and taxes undertaken by the state in the field of public finances."\(^7\)

---

\(^3\) Po aty, fq. 403.
\(^4\) Dr. Sabri Kadriu, v. c. bq. 235.
\(^5\) Po aty, bq. 149.
\(^6\) Dr. Musa limani, Politika ekonomike, Universiteti i Prishtinës, Fakulteti Ekonomik, Prishtinë, 1994, bq. 261.
\(^7\) Dr. Musa Limani, Ekonomia e Kosovës-nëpër per iodha historike, Kolegji “Biznesi”, Fakulteti Ekonomik, Prishtinë, 2018, bq. 407.
**Tax policy.** Tax policy is also a segment of special importance in the fiscal policy system, namely an important instrument in the implemented economic policy. Therefore, *tax policy consists of the necessary measures and provisions for the determination (allocation) of types of taxes and the collection of public revenues.*  

Types of taxes vary by country, but globally they are divided into two main groups: *direct taxes* and *indirect taxes.*

**Direct taxes** are the oldest type of fiscal system, which is still used today, but with a different form and structure. With these taxes, the taxpayer is directly charged, in a ways such as: income tax, property tax, inheritance tax, gifts, etc. This type of taxation has its pros and cons. Its positive sides are that they represent the main and stable source of state budget revenues, while the negative sides are that they are expensive to collect, in case of assignment or collection there may be abuses in reducing the tax base, corruption, bribery, nepotism etc. **Indirect taxes** include value added tax (VAT), material goods and services, excise duty on luxury goods, customs on imported goods, etc. Indirect taxes are mainly imposed on consumption.

In finance theory we come across various definitions on taxation, i.e. tax is the price that the citizen pays to the state in return for public services, tax is a cash payment (tax is paid in cash, which the state collects from ordinary and legal persons), etc. Taxation is a compulsory payment without the right to request immediate consideration. Collection of taxes and its category/type determination, is the exclusive right of the state only, although some types may also be assigned at the local level. When determining the tax, respectively the amount of the tax rate, the state must take into account the following principles:

- **Financial principle,** which means that the tax is paid only in cash, and in no other form,

- **Economic-political principle,** which means that the amount of tax must not be at the level that, from an economic point of view can be bearded by the taxpayer. In other words, the tax must be real and objective and not have negative effects,

---

8) Po aty, f.q. 408.
10) Dr. Sabahudin Komoni, Financat, Enti i Teksteve dhe i Mjetëve Mësimore i KSA të Kosovës, Prishtinë, 1983, f.q. 477.
11) Dr. Musa Limani, Politika Ekonomike, Universiteti i Prishtinës, Fakulteti Ekonomik, Prishtinë, 1994, f.q. 263-266.
- **Socio-political principle**, which in itself means that taxes should be general and the burden should be equal, in the sense of material power of the taxpayer,

- **Technical-organizational tax**, which in itself means that all types of taxes are determined by law and are mandatory for all ordinary and legal persons who have a tax base. The tax rate can be *proportional* or *linear* and *progressive*.

**4. Tax policy in Kosovo after liberation (1999)**

At the end of the XX century and the beginning of the XXI century, in both Eastern Europe and Yugoslavia, changes were made in the socio-economic system. In the last decade of last century, there was the dissolution of Yugoslavia, and the formation of new states, in which case Kosovo from the status of a province became an independent state. On this occasion, Kosovo as a new state, faced radical socio-economic changes. From the political point of view, it passed from a monistic system to a pluralistic political system, and from the economic point of view, it passed from a planned and directed economy, to a market economy.

Consequently, after the liberation (1999), Kosovo's economy faced many challenges and problems. It inherited from Yugoslavia a low level of economic development, high unemployment, tax evasion, large foreign trade deficit, economic smuggling, corruption, nepotism, and so on and so forth. A problem in itself is the issue of privatization, which through the Spin-Off model and liquidation, destroyed the existing economy, terminated the vast majority of employees, and presented the main source of corruption. Thus, all these negative phenomena that accompanied Kosovo after the liberation, greatly influenced each in its own form, and in the formation and implementation of the implemented economic policy, and within it, also the fiscal policy.

In the first years, in order to create the largest possible budget revenues to ensure the functioning of the state, fiscal policy had a purely fiscal character, which means that all instruments of fiscal and tax policy, took on a fiscal character, and less to create conditions for the economic and social development of Kosovo. Another characteristic of fiscal policy in Kosovo was the inadequate definition and implementation of some tax instruments by goods; as a result, the excise tax was set on crude oil, which in the producers of construction material, participated 70.0%, in the process of production, even VAT was applied to raw materials, and so on and so forth. However, even for all
the shortcomings, it can be concluded that, in the post-liberation period, Kosovo created a modern fiscal system and policy according to European standards. Given the operation, functioning and types of instruments, tax policy in Kosovo in the post-liberation period, can be divided into two main periods, such as:¹²

- **The first period** deals with the tax system and policy based on UNMIK Regulations, covering the period 1999-2007 and

- **The second period**, deals with the tax policy based on the legislation of the Republic of Kosovo, which includes the period after Independence (2008) and onwards.

In the first period, the Tax Administration of Kosovo was formed, harmonized with the legislation of the European Union, where the following taxes were foreseen:

- sales tax,
- biased tax,
- service tax
- customs tax.

These measures were not enough for fiscal policy to be effective. Therefore, in order to ensure higher budget revenues, in the period 2001-2002, the following new types of taxes were added:

- Value Added Tax (VAT),
- payroll tax,
- profit tax,
- property tax.

Completion with new instruments changed the structure of taxes and made it possible to increase budget revenues and increased the possibility for the Government to be more efficient in performing its functions.

¹²Dr. Musa Limani, Ekonomia e Kosovës-nëpër periudha historike, Kolegji “Biznesi”, Fakulteti Ekonomik, Prishtinë, 2018, fq. 411.
In the second period, the formation of the tax system and policy is based on the Constitution of the Republic of Kosovo and the laws approved by the Assembly of the Republic of Kosovo. Therefore, starting from Independence, the tax system and policy in Kosovo was enriched with new types of tax. Currently the types of taxes applied in Kosovo are:\(^{13}\)

- payroll tax,
- corporate income tax,
- value added tax (VAT),
- customs tax,
- excise,
- property tax.

As it is known, tax policy is not static, it has a dynamic character and varies depending on the function of the state in economic and social development. In the post-independence period, Kosovo took some steps in some minor fiscal policy reforms. In 2009, minor changes were made to the fiscal system and policy, as shown below:

- wage tax rate, was reduced from 0 - 20.0% to 0 - 10.0%,
- the corporate income tax rate was reduced from 20.0% to 10.0% and
- VAT rate was increased from 15.0% to 16.0%.

The above mentioned changes are presented in the table below.

<table>
<thead>
<tr>
<th>Applicable tax rates</th>
<th>At the level of monthly salaries</th>
<th>At the level of annual salaries</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 - 0%</td>
<td>0 - 80</td>
<td>0 - 960</td>
</tr>
<tr>
<td>4 - 0</td>
<td>80 – 250</td>
<td>960 – 3.000</td>
</tr>
<tr>
<td>8 – 0%</td>
<td>250 – 450</td>
<td>3.000 - 5.400</td>
</tr>
<tr>
<td>10 - 0%</td>
<td>Above 450</td>
<td>Above 5.400</td>
</tr>
</tbody>
</table>

Source: Law no. 05 / 1-028, on personal income tax, article 6. Pristina, 2015, pg. 6.

\(^{13}\) Shih për ketë: Legjislacioni tatimor i Kosovës, Republika e Kosovës, Administrata Tatimore e Kosovës, Prishtinë, mars, 2010.
The level of rates for monthly and annual salaries, presented in the table is applied even now. From these data it can be concluded that, when determining the height of these norms, the economic-political principle was not taken into account, a principle to which these norms should have been set on the material capabilities of employees. It is not logical for the monthly salary of 80-250 euros to be charged with a tax of 4.0%, when they are part of the minimum wage, even below it. We think that this is not fair from the social aspect and the material possibilities of the employees who fall into this category of tax.

Changes in the tax system and policy took place even after these years. Thus, in 2015, some changes were made in the height of the VAT rate. According to these changes, the VAT rate was increased from 16.0% to 18.0%, excluding basic products and services. In this case, some inputs, equipment and information technology were released, as well as the reduction of the VAT threshold for businesses with turnover sales from 50 thousand euros to 30 thousand euros and for basic products and services from 16.0% to 8.0%.\textsuperscript{14)

\textsuperscript{14} Dr. Musa Limani, Ekonomia e Kosovës-nëpër periudha historike, Kolegji “Biznesi”, Fakulteti Ekonomik, Prishtinë, fq. 415.
CONCLUSION

Kosovo in the post-liberation period faced many political, social and economic challenges and problems. Kosovo, as well as other countries has its own specifics of economic development. It should be noted that Kosovo after the liberation, especially after Independence achieved significant results in all areas of life, even in the advancement of the fiscal system and policy, as well as in economic development in general. Although, both the fiscal system and policy, as well as economic development, could have developed significantly more. The slowdown in change, both in the implemented economic policy and in the system and fiscal policy, was dominated by political themes, where economic issues remained in their shadow. These challenges have probably presented the main reason that Kosovo failed to make radical reforms in the implemented economic policy and its subsystems, such as: fiscal policy, credit policy and foreign trade policy.

Therefore, in any case, Kosovo managed to now have a modern and functional fiscal system and policy. Although, there are opportunities for further advancement of the system and fiscal policy. Within the system and fiscal policy, there is a need for radical reforms. In this regard, we think that it would be beneficial and support for local businesses by the Government, if the collection of VAT was done after the realization (sale) of goods and services, and not at the borders, as it is now. Moreover, the heights of tax rates should be based on the economic power of taxpayers to be progressive, not linear. The need for these changes is especially required by the creation of conditions for attracting foreign direct investment, particularly of the Albanian diaspora, which will be a great force in the economic and social development of Kosovo. This is because, it is known that Kosovo businesses do not have great investment potential, therefore stimulating with fiscal policy measures and instruments would enable greater attraction of foreign investment.

Finally, for the fiscal system and policy developed in Kosovo, we can draw these conclusions:

- The fiscal system and policy in Kosovo has a mainly one-dimensional character, in terms of their orientation in the collection of budget revenues, but not stimulating, both for businesses, foreign investors, the domestic diaspora, and consumers.,
- Attempts were made to reform the fiscal system and policy, but they were partial, not general, and did not yield the expected results. Those changes were not enough to boost economic activity.

- The main shortcoming of the fiscal system and policy can be considered the implementation of tax policy contrary to the character, destination and type of goods and services.