

Vladimir Tiutiuriukov\*

## LEGAL CONSEQUENCES OF SPECIAL TAX REGIMES FOR INDIVIDUAL ENTREPRENEURS IN POST-TRANSITION ECONOMIES

**Abstract:** *This paper provides a comparative legal analysis of the practice of four post-transition economies (Czechia, Kazakhstan, Russia, and Serbia) with special tax regimes for individual entrepreneurs from 1990s till now. We analyze the eligibility criteria and main elements of each special tax regime – whether based on lumpsum tax, on taxation of imputed income, or on taxation of actual income – on a country-by-country basis, for both existing and abolished regimes. The legal implications are also explored. In the conclusion, the paper compares and contrasts their features to identify the advantages (such as consistency of tax system, decrease in compliance burden, automatic adjustment for inflation) and deficiencies (taxpayer uncertainty, susceptibility to abuse of law and tax avoidance).*

**Key words:** Special Tax Regime, Lump sum Tax, Imputed Income Tax, Personal Taxation, Individual Entrepreneurs, Self-employed.

### 1. INTRODUCTION

The OECD examined the practices of 38 countries (OECD and G20 members) regarding the taxation of small and medium enterprises (SMEs). It found that more than 95% of all firms are SMEs, and that they “are important for their contribution to employment, economic growth, innovation and the diversity and competition that they can bring to markets.” The study also highlighted that the “common” cost of tax compliance is relatively higher for SMEs than for large businesses, especially considering their more limited access to equity and debt financing.<sup>1</sup>

\* Assistant Professor, Union University Law School Belgrade; e-mail: vladimir.tiutiuriukov@pravnofakultet.edu.rs ORCID ID: 0000-0003-3772-4689. The author is grateful for the comments of anonymous reviewers, which helped the author to improve the article.

1 OECD, 2015, *Taxation of SMEs in OECD and G20 Countries*, OECD Tax Policy Studies, No. 23, Paris, OECD Publishing.

Therefore, the governments employed various tax-related measures to support SMEs; the OECD cited 17 countries employing special presumptive tax regimes for small enterprises and six using special SME replacement taxes.<sup>2</sup>

The governments of transition economies also considered this issue. In 1997 the Interparliamentary Assembly of the Commonwealth of Independent States (CIS) adopted the CIS Model Law on state support for small enterprises, aimed at increasing people's solvency, economic recovery, expanding the tax base and increasing budget tax revenues (as per Preamble). Its Article 5 lists recommended support measures for CIS Member States, among them "an introduction of simplified system of registration, taxation, accounting and reporting for small enterprises."<sup>3</sup> Later, in June 2003, the CIS Interparliamentary Assembly adopted Chapter 3 of the CIS Model Tax Code called "Simplified tax system for subjects of small and medium entrepreneurship", outlying a special tax regime (STR) which replaced VAT, individual income tax (IIT, for individual entrepreneurs), and corporate income tax (CIT, for legal entities) with a simplified tax on gross income.<sup>4</sup> This was *de facto* a compilation of existing practice of some CIS Member States so that other Member States would be able to introduce similar regulations with less efforts in law designing and drafting and a higher degree of uniformity. Overall, the policy makers and society of the CIS Member States have been commonly regarding STRs as methods to reduce the shadow economy by reducing the tax and compliance burden on micro and small businesses.

The countries of Eastern and Southern Europe chose different approaches. In 1992 Czechia introduced fixed deduction for individual entrepreneurs amounting to 30% or 50% of their gross income (later increased to 40%, 60%, or 80%) to simplify tax accounting (to avoid accounting of actual expenses), from 2001 it introduced "lumpsum part of individual income tax" (*daň stanovená paušální částkou*) and from 2021 it also introduced "lumpsum tax for individual entrepreneurs" (*paušální režim*), covering income tax and social security contributions.<sup>5</sup>

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2 *Ibid.*, p. 14.

3 CIS: Model law on state support of small business, adopted on 8 June 1997 [Модельный закон о государственной поддержке малого предпринимательства, принят 08. 06. 1997], ConsultantPlus legal information system, translated by author.

4 CIS: Model tax code for CIS Member States. Special part. Chapter 3. Simplified tax system for small businesses, adopted on 16 June 2003 [Модельный налоговый кодекс для государств-участников СНГ. Специальная часть. Глава 3. Упрощенная система налогообложения для субъектов малого предпринимательства. Принят 16. 06. 2003], ConsultantPlus legal information system.

5 CZ: Law No. 586/1992, on income taxes [Zákon č. 586/1992 Sb., o daních z příjmů], Zakony pro lidi legal information system; Financial Administration of the Czech

Serbia adopted “lumpsum taxation” (*paušalno oporezivanje*) along with the general IIT regime, which it retained during the tax reform of 2001.<sup>6</sup> In the analysis of SME taxation in EU countries, the European Commission (2015) also mentioned that Romania taxed micro enterprises on turnover and Slovenia offered a lumpsum deduction of 70% instead of accounting for actual expenses.<sup>7</sup>

Thus during 1990s and 2000s the transition economies developed a plethora of STRs for SMEs with different consequences. This article focuses on STRs for individual entrepreneurs, compare several cases, and discuss their legal implications.

This article discusses the legal consequences of STRs employed by different post-transition countries, aiming at identifying the optimal features and deficiencies of the regimes.

It uses a comparative legal analysis of law provisions, analyzing the eligibility criteria and main elements of STRs for individual entrepreneurs. Where possible, it also considers publicly expressed opinions and critiques of these STRs, including court cases. This follows the approach similar to that in existing research.<sup>8</sup>

The country cases were selected based on the author’s experience during previous work, alphabetically: Czechia, Kazakhstan, Russia, and Serbia. All four countries are post-transition economies, and in 2022 all of them were ranked 50<sup>th</sup>–100<sup>th</sup> worldwide according to GDP per capita.<sup>9</sup>

Republic, Lump-sum tax – General information [Paušalni daň – Obecné informace], (<https://www.financnisprava.cz/cs/dane/dane/dan-z-prijmu/pausalni-dan/obecne-informace>, 10. 09. 2024).

- 6 RS: Individual Income Tax Law [Zakon o porezu na dohodak građana, *Official Gazette of the RS*, Nos. 43/94...16/2001], Paragraf.rs legal information system.
- 7 European Commission: Directorate-General for Enterprise and Industry, 2015, *SME taxation in Europe: an empirical study of applied corporate income taxation for SMEs compared to large enterprises*, (<https://data.europa.eu/doi/10.2769/027673>, 10. 09. 2024).
- 8 Smith, S., Grabowski, D. M., 1995, *DP1166 The Taxation of Entrepreneurial Income in a Transition Economy: Issues Raised by Experience in Poland*, CEPR Discussion Paper No. 1166, (<https://cepr.org/publications/dp1166>, 10. 09. 2024); Engelschalk, M., 2005, *Small business taxation in transition countries*, Washington, D.C., World Bank Group, (<http://documents.worldbank.org/curated/en/151041468331754316/Small-business-taxation-in-transition-countries>, 10. 09. 2024); Engelschalk, M., Loeprick, J., 2016, The Taxation of Micro and Small Businesses in Transition Economies: Country Experience of the Introduction of Special Tax Regimes, *Journal of Tax Administration*, Vol. 2, No. 1, pp. 145–197.
- 9 World Bank, World Development Indicators, (<https://databank.worldbank.org/source/world-development-indicators>, 18. 10. 2024).

## 2. CZECHIA

Czechia operates Law No. 586/1992 on income taxes adopted in 1992, which covers both IIT and CIT.<sup>10</sup> This law has included some special features for individual entrepreneurs (but none for small legal entities).

From 1992 Article 7 para 7 of Law 586/1992 has allowed the replacement of accounting for actual expenses with fixed deduction for individual entrepreneurs, amounting to 50% of the income in the case of agricultural activities and 30% in the case of royalties, entrepreneurial and independent activities. Subsequently the fixed deduction increased to 80% of the income in the case of agricultural and artisanal activities, to 60% for individual entrepreneurs, to 40% for independent activities, and to 30% for renting out property. In all these cases the entrepreneurs applied the general IIT rate (progressive until 2007, flat 15% from 2008 onwards).

From 2001 to 2020 Law 586/1992 included “lumpsum part of individual income tax” (*daň stanovená paušální částkou*, Art. 7a). Under this regime, a taxpayer who carried out agricultural and other entrepreneurial activities (except for use of authorship and similar rights, renting out property and independent activities) had the option to file a request with the tax authority, submitting the estimate of income and expenses, for a ruling on the amount of lumpsum tax. Apart from the type of activity, another condition was that in the previous three years such income did not exceeded CZK 5 million (by 2020 – around EUR 191,000<sup>11</sup>) per year. The tax inspector had the right to issue such a ruling based on submitted estimates, the general tax rate and available tax credits (for unemployed spouse, underage children, etc.). However, the Financial Administration reported that this option was not very popular.<sup>12</sup>

From 2021 Law No. 540/2020<sup>13</sup> introduced into Law 586/1992 the option to pay a “lumpsum tax” (*paušální daň*, new version of Art. 7a, Arts.

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10 CZ: Law No. 586/1992, on income taxes [Zákon č. 586/1992 Sb., o daních z příjmů], Zakony pro lidi legal information system.

11 In this paper, the amounts in EUR are for information purposes. The exchange rates for the respective years were obtained from InforEuro. Amounts above EUR 1,000 are rounded for the nearest EUR 100.

12 Financial Administration of the Czech Republic. Lump-sum tax – General information [Paušální daň – Obecné informace], (<https://www.financnisprava.cz/cs/dane/dane/dan-z-prijmu/pausalni-dan/obecne-informace>, 10. 09. 2024).

13 CZ: Law No. 540/2020, amending Law No. 586/1992, on income taxes, as amended with later legal acts, and some laws related to lump-sum taxes [Zákon č. 540/2020 Sb., kterým se mění zákon č. 586/1992 Sb., o daních z příjmů, ve znění pozdějších předpisů, a některé další zákony v souvislosti s paušální daní], Zakony pro lidi legal information system.

38lc–38lq), and related provisions into Law No. 589/1992 on social security contributions and Law No. 592/1992 on general medical insurance contributions.

Taxpayers who are eligible for the lumpsum tax are individual entrepreneurs without the obligation to register for VAT (*i.e.*, whose income in the past 12 months did not exceed CZK 2 million, or around EUR 80,000), with some other applicable limitations. Article 7a of Law 586/1992 defines three tiers (*pásma*) for the purposes of lumpsum tax based on intended income, with a specific fixed monthly rate of IIT, social security and medical contributions for each (see Table 1). There is no requirement to file a tax return, but the taxpayer must account for income and notify the Financial Administration if their income falls into a different tier or exceeds the maximum threshold.

Table 1. Thresholds and monthly rates under lumpsum tax

	Maximum annual income	IIT	Social security contributions	Medical insurance contributions
Tier 1	CZK 1 million (EUR 40,000)	CZK 100 (EUR 4)	CZK 4,430 (EUR 177)	CZK 2,968 (EUR 119)
Tier 2	CZK 1.5 million (EUR 60,000)	CZK 4,963 (EUR 198)	CZK 8,191 (EUR 327)	CZK 3,591 (EUR 143)
Tier 3	CZK 2 million (EUR 80,000)	CZK 9,320 (EUR 372)	CZK 12,527 (EUR 500)	CZK 5,292 (EUR 211)
Note	There are also higher limits in Tiers 1 and 2, depending on the taxpayer's activity	Fixed in CZK in Law 586/1992	Standard rates apply for the contribution base, fixed in CZK	Standard rates apply for the contribution base, fixed in CZK

Source: Financial Administration of the Czech Republic, Law 586/1992, Law 589/1992, Law 592/1992.

Overall, the legal consequences of Czech STRs of “lumpsum part of individual income tax” and “lumpsum tax” appear rather straightforward. However, this article discusses only high-level features of STRs across several countries, so it may have missed intricate details that trigger local legal consequences.

These STRs were designed for registered individual entrepreneurs, so there is no separate taxpayer status. However, as a person may be both an employee and an individual entrepreneur (*e.g.*, the old version of Art. 7a of Law 586/1992 mentioned such a situation), the tax control may get somewhat complicated, and a person may need to keep separate sets of documents for income from employment and from entrepreneurship.

The maximum threshold for the lumpsum STR is the same as the minimum threshold for VAT purposes – which is moderate, but may present an additional compliance burden for those entrepreneurs who exceed the limit and have to apply both the general IIT regime and VAT.

However, the tax burden under the lumpsum STR is under 2% of the gross income, which makes it rather attractive (along with the reduced compliance burden) and may trigger business splitting in practice. The author did not find Czech sources discussing this issue, so please refer to sections on Kazakhstan and Russia, where this problem has been the subject of heated discussion for over a decade.

As provisions for the lumpsum STR are incorporated in social security laws, the taxpayers are covered by the state pension, unemployment and medical insurance, so no ambiguity here. While current STR features very low tax burden, the old “lumpsum part of individual income tax” STR, based on general tax rate, featured a nice design touch of tax credit for taxpayers and their dependents.

The STRs are part of IIT law, which make them eligible under double taxation avoidance treaties (DTTs). In fact, the new version of Article 7a para 5 of Law 586/1992 explicitly says that the foreign tax may be credited against lumpsum tax.

### 3. KAZAKHSTAN

Kazakhstan introduced STRs for both individual entrepreneurs and legal entities “predominantly working with cash or having limited number of employees” in 1995, in Article 138 of the Law on Taxes and Other Compulsory Payments to the Budget. It authorized the tax administration to determine the procedure for paying taxes “based on patent or simplified system of determining the tax base.”<sup>14</sup>

In January 2001 both patent and simplified tax return STRs were introduced into the law.<sup>15</sup> The taxpayers, both individual entrepreneurs and legal entities, were granted the right to opt for these STRs, provided that

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14 KZ: Decree of the President of the Republic of Kazakhstan with the power of a law dated 24 April 1995 No. 2235 “On taxes and other compulsory payments to the budget” [Указ Президента Республики Казахстан, имеющий силу Закона “О налогах и других обязательных платежах в бюджет”], Adilet legal information system, translated by author.

15 KZ: Law of the Republic of Kazakhstan dated 23 January 2001 No. 147 “On introduction of amendments and additions to the Law of the Republic of Kazakhstan ‘On taxes and other compulsory payments to the budget’” [Закон Республики Казахстан от 23. 01. 2001. г. N 147 “О внесении изменений и дополнений в Закон Респу-

they meet the criteria of turnover or number of employees (they also could not perform gambling activities). The criteria and procedures of tax calculation for patents were to be set by the Ministry of State Revenues. The law defined the criteria for application of simplified tax return system as 15 employees, 5 kinds of activities, and KZT 4,500,000 (around EUR 33,300) of turnover for individual entrepreneurs, and 25 employees, 7 kinds of activities and KZT 9,000,000 (around EUR 66,700) of turnover for legal entities; some other limits existed. The law also provided that the tax base was the gross revenue, and that tax rates were progressive, from 4% to 11% for individual entrepreneurs and from 5% to 13% for legal entities.

Later in 2001 Kazakhstan adopted the Tax Code (replacing the previous law from 1 January 2002),<sup>16</sup> which incorporated the abovementioned rules but added some more details. It prohibited the use of STRs for businesses with branches and subsidiaries, as well as for those engaged in production of excisable goods, consulting and financial services, sale of petroleum products, collection of glass for recycling, use of mineral resources, and certain licensed activities (gambling business was also beyond the scope due to separate STR).

In particular, Articles 372 and 373 of the Tax Code also introduced the “one-time coupon” STR for individuals whose activities were of an episodic nature (for not more than 90 days per year). The value of the coupon was set by municipal authorities and the taxpayers were not obliged to register as individual entrepreneurs – an important novelty that has reemerged in the past decade in other former USSR countries.

The first issue appears here: the introduction of “one-time coupon” STR resulted in taxpayers with ambiguous legal status – they pursued entrepreneurial activity without any special registration, which was a violation of Article 19 of the Civil Code requiring all individuals pursuing entrepreneurial activity to register as individual entrepreneurs and rendering unregistered activities illegal. A change to that article made an exception for the cases allowed for by the Tax Code, which resolved this issue.<sup>17</sup>

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блики Казахстан ‘О налогах и других обязательных платежах в бюджет’], Art. 1 paras 54–55, Adilet legal information system.

16 KZ: Code of the Republic of Kazakhstan dated 12 June 2001 No. 209 “On taxes and other compulsory payments to the budget (Tax Code)” [Кодекс Республики Казахстан от 12. 06. 2001. г. N 209 “О налогах и других обязательных платежах в бюджет (Налоговый кодекс)”], Adilet legal information system.

17 KZ: Civil Code of the Republic of Kazakhstan dated 27 December 1994 No. 268-XIII [Гражданский кодекс Республики Казахстан от 27. 12. 1994. г. N 268-XIII]; KZ: Law of the Republic of Kazakhstan dated 24 December 2001 No. 276 “On introduction of amendments and additions to certain legal acts of the Republic of Kazakh-

Patent STR (Arts. 374 and 375) became available to individual entrepreneurs without employees, with gross income not exceeding KZT 1,000,000 (around EUR 7,400); the tax was set at 3% of estimated income, to be paid in advance, but later the taxpayer had to account for the actual income and pay the tax on the positive difference (or request the reimbursement in case of overestimated income). The amount of tax covered IIT and social tax liability in equal shares. Gradually the maximum income threshold was increased to KZT 2,000,000 (EUR 11,800 at the end of 2008), while the rate was reduced to 2%.

The simplified tax return STR was initially the same as previously. Gradually the maximum thresholds were increased:

- for individual entrepreneurs – a maximum of 25 employees and a maximum gross income of KZT 10,000,000 (EUR 58,800 at the end of 2008);
- for legal entities – a maximum of 50 employees and a maximum gross income of KZT 25,000,000 (EUR 147,000 at the end of 2008).

The tax rate became a flat 3% of gross income. As it was available for both individual entrepreneurs and legal entities, the amount of tax covered IIT or CIT and social tax liability in equal shares.

This raises the second issue: the extra low tax burden urges the entrepreneurs to keep the burden that way to retain more money for their business and private needs. There appeared a practice known as business splitting (*дробление бизнеса*), when an entrepreneur registers new businesses in the name of their relatives or trusted individuals and arranges part of the business transactions in their name. The type of activity, the actual place of activity, the employees, the suppliers and the clients remain the same – but the names of entrepreneurs on the contracts differ. While current digitalization may help identify cases of business splitting, this was almost impossible in the early 2000s.

The third issue is related to the abovementioned: the mere existence of STRs allows people to use two or more tax regimes (*e.g.*, general IIT on salary and patent STR for the side business). Thus, tax compliance and tax control become complicated, as a person needs to keep two (or more) sets of documents for two (or more) types of income.

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stan due to the adoption of the Code of the Republic of Kazakhstan ‘On taxes and other compulsory payments to the budget’ [Закон Республики Казахстан от 24.12.2001. г. N 276 “О внесении изменений и дополнений в некоторые законодательные акты Республики Казахстан в связи с принятием Кодекса Республики Казахстан ‘О налогах и других обязательных платежах в бюджет’”], Art. 1 para 6, Adilet legal information system.



Starting on 1 January 2009 Kazakhstan had a second Tax Code (effective in 2009–2017)<sup>18</sup>, which inherited the same STRs. Over time, it introduced additional rules on how to determine income and changed the criteria for STRs:

- General criteria – added restrictions for nonprofit organizations, users of mineral resources, and lawyers;
- Patent STR – the maximum income was 200 minimum monthly salaries,<sup>19</sup> as of 1 January 2013 – 300 minimum monthly salaries (in January 2009 – KZT 2,694,000 or EUR 15,800; in December 2017 – KZT 7,337,700 or EUR 18,400), the tax rate remained flat 2%, the amount of tax covered IIT or CIT and social tax liability in equal shares;
- Simplified tax return STR – from 1 January 2013 the maximum income was increased to 1,400 minimum monthly salaries for individual entrepreneurs and to 2,800 minimum monthly salaries for legal entities (in December 2017 – KZT 34,242,600 or EUR 86,000, and KZT 68,485,200 or EUR 172,000, respectively), the tax rate remained flat 3%, the amount of tax covered IIT or CIT and social tax liability in equal shares.

The unavailability of STRs to users of mineral resources triggered a fourth issue, as an individual entrepreneur (or a legal entity) using a water well for its own technical purposes was legally a user of mineral resources and could not therefore enjoy STR.<sup>20</sup>

Since 1 January 2018 Kazakhstan has operated the third version of the Tax Code,<sup>21</sup> which inherited the same STRs and introduced four new ones – STR with mobile application, STR with fixed deduction, retail tax, and unified cumulative payment. The criteria for STRs changed again:

18 KZ: Code of the Republic of Kazakhstan dated 10 December 2008 No. 99-IV “On taxes and other compulsory payments to the budget (Tax Code)” [Кодекс Республики Казахстан от 10. 12. 2008. г. N 99-IV “О налогах и других обязательных платежах в бюджет (Налоговый кодекс)”], Adilet legal information system.

19 This sum in KZT is determined in the annual Law on the republican budget, the change is correlated with official inflation rate. The minimum monthly salary is used for protection of employees’ rights and for calculation of certain state-related payments.

20 Smurygina, I., 2015, *Should individual entrepreneur, a taxpayer of mineral extraction tax who rents out gas station, change the simplified tax regime to a general one, if it has a water well for its own needs?*, Paragraph legal information system.

21 KZ: Code of the Republic of Kazakhstan dated 25 December 2017 No. 120-VI “On taxes and other compulsory payments to the budget (Tax Code)” [Кодекс Республики Казахстан от 25. 12. 2017. г. N 120-VI “О налогах и других обязательных платежах в бюджет (Налоговый кодекс)”], Adilet legal information system.

- Patent STR – a maximum income of 3,528 monthly assessment indices (MAI; *месячный расчётный показатель*),<sup>22</sup> no employees, activities from a specific list, a IIT rate of 1% of planned income (to be adjusted to the actual income), social security contributions (SSCs) calculated separately;
- Simplified tax return STR – a maximum income of 24,038 MAI, a maximum of 30 employees, a flat tax rate of 3%, the amount of tax covering IIT or CIT and social tax liability in equal shares;
- STR with mobile application – a maximum income of 3,528 MAI, no employees, activities from a specific list (for income from other activities the entrepreneur may apply another STR or a general tax regime), a IIT rate of 1% of income reported via application, SSCs are calculated separately by the application;
- STR with fixed deduction – a maximum income of 144,184 MAI, a maximum of 50 employees, the taxpayer may deduct certain expenses and an additional “fixed deduction” amounting up to 30% of the gross income, but the total amount of deductions must not exceed 70% of the gross income; general CIT, IIT and SSC rates apply;
- retail tax – taxpayers are individual entrepreneurs and legal entities, with a maximum income of 600,000 MAI, a maximum of 200 employees, activities from a specific list provided by the Government, the tax rates are 8% on sales to businesses, using general tax regime, and 4% in other cases; the municipalities have the right to reduce the rate down to 50%;
- unified cumulative payment (2019–2023) – taxpayers were Kazakhstani citizens or *kandas* (Kazakh repatriates, *i.e.* naturalized persons) not registered as individual entrepreneurs, performing services to other people or selling them products from a private plot of land. The maximum income was 1,175 MAI (around EUR 8,278), the lumpsum monthly tax rate was 1 MAI (around EUR 7) in the capital and the cities of national and regional significance, and at 0.5 MAI (around EUR 3.50) in other settlements.<sup>23</sup>

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22 An indicative amount in KZT (in 2018 KZT 2,405 or EUR 6.1; in 2024 KZT 3,692 or EUR 6.90) used for calculation of various state-related payments, determined in the annual Law on the republican budget, the change is correlated with official inflation rate. Introduced by the Law of the Republic of Kazakhstan dated 10 December 1999 No. 492-I “On introduction of amendments and additions to the Law of the Republic of Kazakhstan ‘On taxes and other compulsory payments to the budget’” [Закон Республики Казахстан от 10. 12. 1999. г. N 492-1 “О внесении изменений и дополнений в Закон Республики Казахстан ‘О налогах и других обязательных платежах в бюджет’”], Adilet legal information system.

23 Amounts quoted per Tyutyuryukov, V., 2023, Special tax regimes for self-employed people in EAEU Member States: worth the bother?, *The future of public administra-*

An additional restriction that two or more STR taxpayers cannot render hotel services on the premises of a single hotel reduced the possibility for business splitting (abovementioned second issue) in this particular industry. However, other industries, especially cafes and restaurants, still use this tax optimization method.<sup>24</sup>

The availability of six STRs worsens the abovementioned third issue – the complexity of tax compliance and tax administration, when certain people or businesses may use two or more tax regimes (especially when some may prefer to combine, say, IIT for salary and unified cumulative payment for other activities, while other prefer IIT and patent STR).

In the address in September 2022 President of Kazakhstan Kassym-Jomart Tokayev announced the work on a new, fourth version of the Tax Code, aimed at differentiated tax rates for different industries, expansion of retail tax and combatting business splitting.<sup>25</sup> While the plan was to adopt it in 2023, the actual work took longer, and the draft was published for public discussion in June 2024, including:

- Three STRs for self-employed persons. Generally, an individual qualifies if their maximum monthly income is below 340 MAI (EUR 2,300), they have no employees, and perform activities from a specific list (for income from other activities the entrepreneur may apply another STR or a general tax regime). There were three options: employment via platform (IIT rate is 0%, but platform must calculate and withhold SSCs), patent (IIT rate is 0%, patent value include SSCs, it is assessed and paid in advance based on estimated income and adjusted based on actual income), and SRT with mobile application (IIT rate is 0%, SSCs are calculated separately by the application);<sup>26</sup>
- STR for small enterprises. Generally, an individual entrepreneur or a legal entity qualifies if their maximum monthly income is below 135,000 MAI (EUR 931,500) and do not engage in activities from a specific list (production and wholesale trade of excisable goods,

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*tion enabled through emerging technologies. e-Proceedings of the 31<sup>st</sup> NISPAcee Annual Conference, Bratislava, NISPAcee Press.*

24 Discussion during the Open dialog: Business and State forum, 27 June 2024 (<https://www.youtube.com/watch?v=pFE-c005SkM>, 10. 09. 2024).

25 KZ: President Kassym-Jomart Tokayev's State of the Nation Address "A Fair State. One Nation. Prosperous Society", 1 September 2022, (<https://akorda.kz/en/president-kassym-jomart-tokayevs-state-of-the-nation-address-181857>, 10. 09. 2024).

26 KZ: Draft Tax Code of the Republic of Kazakhstan dated 21 June 2024 [Проект Налогового кодекса Республики Казахстан от 21. 06. 2024], Arts. 693–701, (<https://legalacts.gov.kz/npa/view?id=15096317>, 10. 09. 2024).

sale of petroleum products, lotteries, gambling, financial services, etc.). Other disqualifying factors included existence of branches, especially in other municipalities, parent entities enjoying STRs, and nonprofit organizations. There was no maximum number of employees. Tax rates were 2% for B2C sector, 2% for processing industry, and 8% for sales to businesses using general tax regimes, the tax base being the gross income.<sup>27</sup>

However, the immediate criticism targeted the merger of the simplified tax return STR (used by 1.9 million taxpayers) and retail tax (used by 30,000 taxpayers) into the STR for small enterprises. While the entrepreneurs were happy with the 5.6-fold increase in maximum allowed income under STR and corresponding increase in the threshold for compulsory VAT registration (seeing it as discouragement of business splitting), many were concerned with reduction in the retail tax threshold. However, the tax authorities reported that the income of almost all 30,000 retail taxpayers were below the new threshold, and it was above the limit in only 49 cases. Another point of critique was the two-rate system based on the nature of the client (customer), which raises the necessity to track and prove the tax regime of every client (and being under constant threat of penalties). Other taxpayers cited compliance issues. One more suggestion was to gradually increase the tax and compliance burden from micro business, to small and medium, to large business.<sup>28</sup>

With respect to combatting business splitting *per se*, a search for academic discussion did not return any results, and the practitioners cite the practice of tax control as anecdotal evidence, but no decision of the Kazakhstani courts.<sup>29</sup> Instead, they tend to analyze Article 8 para 2 of the current Tax Code and Article 15 para 2 of the draft Tax Code, considering

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27 KZ: Draft Tax Code, Arts. 702–706.

28 Discussion during the Open Dialog: Business and State forum, 27 June 2024 (<https://www.youtube.com/watch?v=pFE-c005SkM>, 10. 09. 2024); Atameken, 2024, Бизнес и государство: важен открытый и прямой диалог [Business and State: open and direct dialog is necessary], Atameken, 27 June, (<https://karagandy.atameken.kz/ru/news/52266-biznes-i-gosudarstvo-vazhen-otkrytyj-i-priamoj-dialog>, 10. 09. 2024); Andreeva, D., Baryshev, M., 2024, What is wrong with the project of the new Tax Code of Kazakhstan, *Forbes Kazakhstan*, (<https://forbes.kz/articles/chto-ne-tak-s-proektom-novogo-nalogovogo-kodeksa-kazahstana>, 10. 09. 2024).

29 Press conference of Daniyar Zhanalinov, the Chairman of the State Revenue Committee of the Ministry of Finance of the Republic of Kazakhstan, 9 June 2023, (<https://kgd.gov.kz/ru/news/press-konferenciya-1-129422>, 10. 09. 2024); Discussion during the Open Dialog: Business and State forum, 27 June 2024; Kim, E., Instagram posts, (<https://www.instagram.com/nalogialmaty/>, 10. 09. 2024); members of Facebook group “Tax consultants of Kazakhstan” (<https://www.facebook.com/groups/1504811279785374/>, 10. 09. 2024).

accumulated Russian court practice, implying that there is no available summary of relevant Kazakhstani court cases.<sup>30</sup>

Due to criticism the Draft Tax Code was withdrawn for further development, and on 18 September 2024 the representatives of the Ministry of National Economy and Ministry of Finances presented new ideas for an updated version of Draft Tax Code, including only three STRs – one for farmers and two for SMEs, based on gross income (Table 2).

Table 2. Suggested STRs for SMEs in Kazakhstan (September 2024)

	STR for self-employed	STR with simplified tax return
Taxpayers	unregistered entrepreneurs	individual entrepreneurs and legal entities
Maximum annual income	4,080 MAI (currently EUR 28,100)	600,000 MAI (currently EUR 4,140,000)
Maximum number of employees	None	No limit
Allowed activities	List of explicitly qualified activities	List of prohibited activities (production and wholesale trade of excisable goods, sale of petroleum products, lotteries, gambling, business, legal and financial consulting, financial services, construction, etc.). Not permitted for nonprofit organizations, residents of special economic zones, taxpayers whose owners, affiliate entities or subsidiaries enjoy STR.
Tax rate	4%, split among the state funds for pension insurance, social insurance and medical insurance; no tax component to budget	<ul style="list-style-type: none"> <li>• 4% for B2C sector</li> <li>• 4% for processing industry</li> <li>• 12% for sales to businesses using general tax regime</li> </ul>

**Source:** presentation by Deputy Minister of National Economy Azamat Amrin, and Deputy Minister of Finances Yerzhan Birzhanov, as cited by E. Kim, (<https://www.instagram.com/p/DAEDN4TCA8P/>, 18. 09. 2024).

30 Massatbayev, A. O., 2024, *Дробление бизнеса в Казахстане: анализ, опыт России и предложения по улучшению Налогового Кодекса Казахстана* [Business splitting in Kazakhstan: analysis, experience of Russia and suggestions for improvement of the Tax Code of Kazakhstan], Paragraf legal information system, ([https://online.zakon.kz/Document/?doc\\_id=36432368](https://online.zakon.kz/Document/?doc_id=36432368), 10. 09. 2024); Tax consultants of Kazakhstan Facebook group.

Two more proposed novelties concern tax compliance. First, in general, individual entrepreneurs would submit tax returns once a year. Second, if an individual entrepreneur agreed to disclose their accounting data, the tax authorities could prefill the tax return for the entrepreneur to either approve or amend it (similar to the idea of horizontal tax monitoring, generally used for large taxpayers).

The smaller number of STRs, which are easier to administer, is a positive development. However, there still is an STR for non-registered entrepreneurs with a legally unclear status. The government also still promotes two-rate approach with an even higher tax rate, which is criticized by the taxpayers due to the remaining requirement to track and prove the tax regime of their clients and ring-fence the income, as well as the tax burden too high compared to their profit margin. Thus, the presented approach violates two standards of good taxation – tax certainty and the taxpayer’s ability to pay.

#### 4. RUSSIA

Russia’s history of STRs for small business begins in 1995, with the adoption of the Federal Law No. 222-FZ (effective from 1 January 1996), which introduced simplified tax system.<sup>31</sup> This STR was available for both legal entities and individual entrepreneurs, with the following features:

- for the individual entrepreneurs it replaced the IIT with a regular fee for the right to pursue a particular activity (at the time called “patent”);
- for the legal entities it replaced all federal, regional and local taxes (except customs duties, state duties, license duties, tax on acquisition of automobiles, and social security contributions) with a “unified tax” on profit or on gross income (selected by a taxpayer) based on simplified calculation;
- the eligible taxpayers could have a maximum of 15 employees (on both labor and civil law contracts,<sup>32</sup> in both head offices and

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31 RU: Federal law dated 29 December 1995 No. 222-FZ “On simplified system of taxation, accounting and reporting for small enterprises” [Федеральный закон от 29. 12. 1995. N 222-ФЗ “Об упрощенной системе налогообложения, учета и отчетности для субъектов малого предпринимательства”], ConsultantPlus legal information system.

32 Under USSR legislation, only legal entities could hire employees using labor contract. Civil legislation of the Russian Federation granted individuals the right to conclude civil law contracts (contract to perform work, contract to render services, etc.) with any other person. As of the present an individual may conclude both labor contracts

branches) and a maximum gross income of 100,000 minimum monthly salaries;

- some activities were not eligible for STR, such as producing excisable goods, financial and insurance activities, gambling and entertainment, etc.;
- a simplified tax system for legal entities with tax rates of up to 30% on profit and up to 10% on gross income (compared to the general CIT rate of 35%); in both cases regional authorities had the limited right to reduce them or introduce imputed tax instead;
- Federal Law No. 222-FZ did not establish the rules for the calculation of the tax, the tax rates, or any limits; the regional authorities determined the amount of the patent “considering the rates of unified tax” (while the general IIT rate was progressive from 12% to 35% on profit);
- the taxpayers had the right to keep simplified accounting (ledger of income and expenses), but they still had to issue cash register receipts and file statistical reports.

In the late 1990s Russia launched the process of codification of the tax system, and from 2001 it put into effect the first codified taxes (VAT, excises, IIT and unified social tax<sup>33</sup>, later supplemented by other taxes). From 1 January 2003 two more chapters of the Tax Code came into effect: Ch. 26.2 “Simplified tax system” (*упрощенная система налогообложения*) and Ch. 26.3 “Tax system in the form of unified tax on imputed income for specified activities” (*система налогообложения в виде единого налога на вмененный доход для отдельных видов деятельности*).<sup>34</sup> They evidently took after previous STRs, with more details and some changes, posing certain risks to growing businesses.<sup>35</sup>

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(function-oriented and providing protection of employee rights under Labor Code) and civil law contracts (result-oriented, more flexible, and allowing for a lower tax and SSC burden).

33 In 2001–2009, this tax replaced SSCs, but Russia subsequently returned to separate SSCs.

34 RU: Federal law dated 24 July 2002 No. 104-FZ “On amendments and additions to Part Two of the Tax Code of the Russian Federation and some other legal acts of the Russian Federation, as well as on recognition as terminated some legal acts of the Russian Federation” [Федеральный закон от 24. 07. 2002 N 104-ФЗ “О внесении изменений и дополнений в часть вторую Налогового кодекса Российской Федерации и некоторые другие акты законодательства Российской Федерации, а также о признании утратившими силу отдельных актов законодательства Российской Федерации о налогах и сборах”], ConsultantPlus legal information system.

35 Liapunova, G., 2002, Trap set for the small enterprises, *Kommersant*, (<https://www.kommersant.ru/doc/333811>, 10. 09. 2024).

Simplified tax system has been available for both legal entities and individual entrepreneurs, with the following features:

- for the individual entrepreneurs it initially replaced IIT (for respective income), VAT, sales tax, individual property tax and unified social tax; over years the list was revised and now includes only IIT (for respective income) and individual property tax (for respective property);
- for the legal entities it initially replaced CIT, VAT, sales tax, corporate property tax and unified social tax; over years the list was revised and now includes only CIT and corporate property tax, but the taxpayers are exempt from VAT (except for VAT on import);
- the eligibility criteria have gradually increased: the taxpayers could have maximum 100 employees (130 from 2025), maximum annual gross income of RUB 15 million (EUR 459,200; gradually increased to RUB 200 million or EUR 1,965,600 by 2024 and expected to reach from 2025 RUB 450 million or over EUR 4.4 million), and maximum value of fixed assets RUB 100 million (EUR 3,061,200; from 2025 the threshold will be RUB 200 million or around EUR 2 million);
- some activities have not been eligible for STR, for individual entrepreneurs these include producing excisable goods, manufacturing and sale of jewelry, certain financial activities, mineral extraction (except common minerals), notaries and advocates, etc.;
- the simplified tax system for individual entrepreneurs provide for the tax rates of 15% on profit (calculated under simplified rules) or 6% on gross income (compared to general IIT rate of 13% to 22% on profit), the regional authorities may reduce the rates;
- SSCs for individual entrepreneurs are fixed in Russian rubles (currently RUB 49,500, or EUR 490; amount reviewed annually) plus 1% on gross income above RUB 300,000 (EUR 2,950) per year. However in 2003–2004 the amount of tax under simplified tax system was split among the budgets of respective region, municipality, and three social insurance funds.<sup>36</sup> Later the individual entrepreneurs received the right to credit SSCs against 50% of their tax liability;
- the taxpayers are only obliged to keep simplified accounting (ledger of income and expenses).

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36 RU: Budget Code of the Russian Federation dated 31 July 1998 No. 145-FZ “Бюджетный кодекс Российской Федерации” от 31. 07. 1998. N 145-ФЗ], Art. 48, ConsultantPlus legal information system.



There are several main issues triggered by the application of the simplified tax system.

First and foremost, the low tax burden is an incentive for taxpayers to tailor their business structure and accounting data to meet the eligibility criteria and reduce their tax burden. This has led to the gray-zone practice of business splitting (*дробление бизнеса*) – the very same above-mentioned issue in the section on Kazakhstan, sometimes along with outsourcing, *i.e.*, transferring personnel from the main company into those enjoying STR.<sup>37</sup> The state reacted to these and other aggressive tax planning practices by issuing the binding Plenary Ruling No. 53 in 2006,<sup>38</sup> which introduced the term “unjustified tax benefit” and put into practice two doctrines: the substance over form doctrine and the business purpose doctrine.<sup>39</sup> In particular, the courts could find a tax benefit to be unjustified if the taxpayer’s transactions were not accounted for in accordance with their business nature, or if the taxpayer had no resources (whether material, personnel, premises or other) to perform the operations accounted for.<sup>40</sup> Article 54.1, stating that “[l]imits on the exercise of rights to calculate the tax base and/or the amount of tax, duty, social security contribution” was added to the Tax Code in 2017, with the intent to “set the limits to the execution of rights and liabilities by a taxpayer [by] introducing the principle of ‘bona fide taxpayer’, defining the term ‘abuse of law.’”<sup>41</sup> Article 54.1 of the Tax Code did not replace Plenary Ruling No. 53, but rather introduced a “principal purpose test” and outlined which taxpayer’s actions may constitute abuse of law.<sup>42</sup>

37 Tischenko, S., 2008, The schemes of tax optimization and unjustified tax benefit. Related parties and suspicions of bad faith, *Nalogi*, No. 28, ConsultantPlus legal information system.

38 RU: Ruling of the Plenum of the Supreme Arbitration Court of the Russian Federation dated 12 October 2006 No. 53 “On assessment by the Arbitration Courts of the justified nature of the tax benefit obtained by a taxpayer” [Постановление Пленума ВАС РФ от 12. 10. 2006. N 53 “Об оценке арбитражными судами обоснованности получения налогоплательщиком налоговой выгоды”], ConsultantPlus legal information system.

39 Tyutyuryukov, V., 2016, Chapter 27: Russia, in: Lang, M. *et al.*, (eds.), 2016, *GAARs – A Key Element of Tax Systems in the Post-BEPS World*, Amsterdam, IBFD, pp. 543–567.

40 RU: Plenary Ruling No. 53, sections 3 and 5.

41 RU: Federal law dated 18 July 2017 No. 163-FZ “On amendments to Part One of the Tax Code of the Russian Federation” [Федеральный закон от 18. 07. 2017. N 163-ФЗ “О внесении изменений в часть первую Налогового кодекса Российской Федерации”] and explanatory note to the draft of this law, ConsultantPlus legal information system, translated by author.

42 Ponomareva, K. A., 2018, Tendencies of Legal Regulation in the Sphere of Fight Against Tax Abuse: Application of International Experience in Russia, *Actual Problems of Russian Law*, No. 4, pp. 54–63.

On many occasions the courts ruled that businesses with the related owners and sharing employees, premises, suppliers, customers, brands and other resources, were *de facto* a single business violating the principles set by Plenary Ruling No. 53 and Article 54.1 of the Tax Code; however, sharing premises while maintaining different groups of customers or somewhat different activities was considered justified.<sup>43</sup> In a report to the President on systemic problems of Russian business, the Presidential Commissioner for the Protection of Entrepreneurs' Rights in the Russian Federation mentioned that while the legislation does not contain an explicit definition of the business splitting, the use of practice analysis and special explanations by the Federal Tax Service (FTS) is helpful.<sup>44</sup>

The second issue is related to the fact that in Russia the simplified tax system (along with other STRs) replaces the IIT and the CIT and, as a specific tax, do not fall within the scope of the double taxation avoidance treaties. Therefore, if an individual entrepreneur is taxed abroad, the foreign tax cannot be deducted from their Russian tax liability; and vice versa – should a nonresident individual entrepreneur (STRs in Russia are not tied to tax residency) pay tax under STR in Russia, they cannot deduct this tax in the country of their residence.

The third issue is that the obligation to keep simplified accounting can pose a problem if a taxpayer loses the right to use this STR during the year. In such cases the taxpayer is supposed to apply the general tax regime from the beginning of the quarter, in which it stopped meeting the eligibility criteria, but due to simplified accounting it may not have the relevant information and would be forced to spend resources to restore accounting data. However, this was an issue in the early days of the STR,<sup>45</sup> with the current high gross income limit the taxpayer is likely to have the necessary resources.

Imputed income tax was in force from 2003 to 2020. It was available for both legal entities and individual entrepreneurs, with the following features:

- it could be applied along with the simplified tax system (with ring-fencing of the income taxed under each regime);<sup>46</sup>

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43 *Ibid.*

44 Presidential Commissioner for the Protection of Entrepreneurs' Rights in the Russian Federation, 2022, *Register of system problems of Russian business* (<http://doklad.ombudsmanbiz.ru/2022/3-22.pdf>, 10. 09. 2024).

45 Liapunova, G., 2002.

46 RU: Tax Code of the Russian Federation (Part Two) dated 5 August 2000 No. 117-FZ "[Налоговый кодекс Российской Федерации" от 05. 08. 2000. N 117-ФЗ], Art. 346.12(4), ConsultantPlus legal information system.

- it replaced the IIT and the CIT (for respective income), corporate and individual property tax;
- the eligibility criteria initially included a “white list” of activities (personal services, veterinary services, small retail trade, etc.); in time a maximum number of employees (100 people) was added. The sale of jewelry was eligible for imputed income tax, unlike for the simplified tax system, and to the author’s knowledge even jewelry factory retail chains used the imputed income tax regime;
- the tax base was imputed income calculated, using the basic monthly income set in the Tax Code (in RUB, per employee, area of premises or other natural measurement of a business) and multipliers determined by the municipal authorities;
- the imputed income tax rate was 15%; the municipal authorities could reduce it to 7.5%;
- SSCs for individual entrepreneurs have been fixed in Russian rubles, plus 1% on gross income above RUB 300,000 per year, and the taxpayers could credit them against the amount of tax;
- the taxpayers was required to issue sales receipts and keep a ledger of income.

As in the case of Kazakhstan, the existence of manifold STRs and the option of concurrent application of several of them complicated the statistics, public administration and tax control, with as some businesses using two tax regimes and thus not reporting part of their actual income. The last point was somewhat mitigated by the introduction of online cash registers in 2017.

In 2011 a group of deputies submitted a draft law on the patent tax system, which would replace the imputed income tax. While the patent tax system was eventually adopted in 2012, as Chapter 26.5 of the Tax Code, it coexisted with both the simplified tax system and the imputed income tax, until the abolishment of the latter in 2020. The main features of the patent tax system are:

- it applies only by individual entrepreneurs, possibly along with other tax regimes (with ring-fencing of the income taxed under each regime);<sup>47</sup>
- it replaced the IIT and individual property tax, the taxpayers are not subject to VAT (except for import and non-eligible activity);
- the eligibility criteria includes a “white list” of activities (personal services, veterinary services, small retail trade, preschool and

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47 RU: Tax Code of the Russian Federation (Part Two), Art. 346.43(1).

- additional education, transportation, etc.), a maximum number of employees (15 people). Some activities are not eligible for STR, e.g., producing excisable goods, manufacturing and sale of jewelry, certain financial activities, mineral extraction;
- the tax base is the imputed annual income, determined by the regional authorities;
  - the tax rate is 6% of the gross imputed income;
  - SSCs for individual entrepreneurs have been fixed in Russian rubles plus 1% on gross income above RUB 300,000 per year, and the taxpayers can credit them against the amount of tax;
  - the taxpayers are required to keep a ledger of income and issue sales receipts.

The latest addition to STRs was the tax on professional income (TPI), introduced in 2018 by Federal Law No. 422-FZ as a tax experiment for 2019–2028.<sup>48</sup> From 1 January 2019 it was introduced in Moscow, the Moscow and Kaluga oblasts, and the Republic of Tatarstan; in 2020 the experiment spread to the entire country.

The TPI concept is that an individual is granted the right to pursue entrepreneurial activities without registration as an individual entrepreneur, while enjoying very simple tax compliance and low tax burden.

It started with the initiative by the President of the Russian Federation to decriminalize unregistered self-employment in 2016 – later developed into Federal law No. 422-FZ – with the intent to nudge the citizens away from the shadow economy. However, the public discussion about this law was controversial and claimed that TPI would increase budget revenues (from those who had not declared their income previously), or decrease budget revenues (due to tax optimization), or help legalization of micro-entrepreneurial activity (due to simplicity and low tax burden), or threaten the citizens' finances (due to possibility of freezing their bank accounts as a side effect of legislation combating money laundering and terrorism financing).<sup>49</sup>

While Article 23 para 1 of the Civil Code was amended in 2017 to allow peer-to-peer services without registration as an individual entrepreneur, “to

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48 RU: Federal Law dated 27 November 2018 No. 422-FZ “On the experiment of establishing a special tax regime ‘Tax on Professional Income’” [Федеральный закон от 27. 11. 2018. N 422-ФЗ “О проведении эксперимента по установлению специального налогового режима ‘Налог на профессиональный доход’”], Consultant-Plus legal information system.

49 Moystsrapihvili, D., 2019, *The Perspectives of “Self-Employed Tax” and its Perception in Russia*, bachelor thesis, HSE University.

avoid often burdensome liabilities foreseen for the individual entrepreneurs” and “to reduce the informal employment”,<sup>50</sup> the legal status of such individuals remain ambiguous.<sup>51</sup> Due to that ambiguity, the Ministry of Finance found that the “self-employed” individuals must file their lawsuits with the general courts, while individual entrepreneurs must file their lawsuits to the arbitration courts, which further complicates the legal situation.<sup>52</sup>

The TPI<sup>53</sup> replaces the personal income tax in case of professional income of natural persons, regardless of whether they are registered as individual entrepreneurs or not. Due to the strict “no employees” feature, the TPI payers are semi-officially called “self-employed” (*самозанятые*). The TPI payers do not pay VAT (except the VAT on import) and compulsory social security contributions (although a fraction of their tax goes to the Federal Compulsory Medical Insurance Fund and they may opt for voluntary pension contributions). The prospective taxpayer must notify the tax authorities, selecting the region and type of their activity. There are several options for such a notification: a personal account on FTS web site, the *Moi Nalog* (“My tax”) app for smartphones, a bank, or directly with the tax inspectorate.

The individuals and individual entrepreneurs must meet certain conditions to enjoy the TPI regime:

- They must hold citizenship of Russia, a EAEU Member State, or Ukraine;<sup>54</sup>
- Their annual income from professional activities must not exceed RUB 2,400,000 (around EUR 23,600);
- They cannot hire other individuals under labor contracts (although civil law contracting of other self-employed or individual entrepreneurs is technically possible);

50 RU: Explanatory note to the draft of Federal law dated 26 July 2017 No. 199-FZ “On amendments to Articles 2 and 23 of Part One of the Civil Code of the Russian Federation” [Федеральный закон от 26. 07. 2017. N 199-ФЗ “О внесении изменений в статьи 2 и 23 части первой Гражданского кодекса Российской Федерации”], ConsultantPlus legal information system, translated by author.

51 RU: Letter of the Ministry of Finance of Russia dated 7 September 2018 No. 03-11-11/64054, ConsultantPlus legal information system.

52 RU: Letter of the Ministry of Finance of Russia dated 30 April 2021 No. 03-11-10/34022.

53 The following text refers to Tyutyuryukov, V., 2023.

54 Initially Federal law No. 422-FZ included only Russia and other EAEU Member States. When considering amendments to that law in June 2022, several deputies of the State Duma proposed that the list also include the citizens of Ukraine, apparently so that those of them who decided to move to Russia or stayed in the territories claimed by Russia would be eligible for this tax regime.

- They cannot resell goods (except their own personal belongings), sell excisable goods or goods subject to obligatory marking (tires, leather clothing, shoes, linen, dairy products, and some other goods<sup>55</sup>), extract or sell minerals. Contrary to the examples of some other EAEU countries, business consulting, engineering, marketing, research and development, and other professional services are covered by the TPI;
- They cannot act under agency or commission agreement with other parties, but delivery of retail goods, accompanied by the cash receipt from the seller, is possible under the TPI.

Individual entrepreneurs cannot use the TPI regime in combination with the general tax system or other special tax regimes. The employees may use the TPI for their side activities, but not while rendering services to their current or recent employers (two years prior). The federal and municipal service officials may use the TPI only for renting out residential properties.

The taxable item is the income of the natural person. The list of exceptions includes:

- labor income;
- income from the sale of real estate, vehicles, securities, and personal belongings;
- income from renting out nonresidential properties;
- income from simple partnership;
- the professional income of notaries, lawyers, appraisers, mediators, and insolvency officers.

The applicable tax rate is 4% when customers are other natural persons, and 6% when customers are individual entrepreneurs or legal entities. The amount of tax is then split within the budget system between the budget of the respective region (63%) and the budget of the Federal Compulsory Medical Insurance Fund (73%).<sup>56</sup>

When a taxpayer receives payment (in cash, into a bank account, or by other means), they must issue a receipt using a personal account on the FTS web site or the *Moi Nalog* app, and send this receipt to the customer. There is no other obligatory tax accounting or reporting. For each calendar month (which is the tax period), the FTS automatically calculates the tax base and the tax due, and sends the notification to the taxpayer.

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55 RU: Government Executive Order dated 28 April 2018 No. 792-r.

56 RU: Budget Code of the Russian Federation, Arts. 56(2) and 146(1)(3).

As of August 2024, the FTS reports that over 11.2 million people registered as TPI payers. However, their total gross income of RUB 197 billion (around EUR 1.9 billion) in August 2024 results in a per capita income of RUB 17,600 (EUR 173), which is equal to subsistence level.<sup>57</sup> This does not take into account that many TPI payers did not report any income or that both individuals and individual entrepreneurs may use TPI, which complicates the statistics. These data also suggest that the income reported under TPI regime is not the main source of personal revenue. The law aimed to legalize the income earned in the informal economy via simplified tax compliance,<sup>58</sup> so the result may be considered ambiguous: while many people apparently opted for registration as taxpayers, the reported per capita income is not sufficiently high to suggest success in combatting shadow economy with this particular measure.

## 5. SERBIA

The STRs in Serbia were introduced in 1 January 1992 with the 1991 Individual Income Tax Law taking effect (as a part of a general tax reform).<sup>59</sup> However, due to international sanctions, hyperinflation, economic instability (with shadow economy amounting up to 40% of the GDP) and tax administration issues, the effectiveness of the tax laws was questionable and they were replaced in 1994.<sup>60</sup>

The 1994 Individual Income Tax Law did not set the eligibility criteria, but listed the factors that the Government was to consider when adopting detailed rules on lumpsum taxation. The lumpsum taxpayer was also required to keep a ledger of income.<sup>61</sup>

The 1994 Individual Income Tax Law was succeeded by the 2001 Individual Income Tax Law. (2001 IITL), which is still in force (with certain changes).<sup>62</sup> It includes Chapter 3 “Tax on income from independent

57 FTS Data Supply Platform (<https://vpd.nalog.gov.ru/>, 10. 09. 2024).

58 RU: Explanatory note to the draft of Federal law No. 422-FZ, ConsultantPlus legal information system.

59 RS: Individual income tax law [Zakon o porezu na dohodak građana], *Official Gazette of the RS*, Nos. 76/91...28/94.

60 Dobrosavljev, S., 1994, The changes in the tax system, *Glasnik Advokatske komore Vojvodine*, Vol. 54 Nos. 7–8, pp. 36–42; Dimic, S., 2016, *Modern legal solutions within the domain of personal income taxation – alternative models*, doctoral dissertation, Faculty of Law, University of Niš.

61 RS: Individual income tax law [Zakon o porezu na dohodak građana], *Official Gazette of the RS*, Nos. 43/94...16/2001, Arts. 69, 69a, 104, 130, Paragraf.rs legal information system.

62 RS: Individual income tax law [Zakon o porezu na dohodak građana], *Official Gazette of the RS*, Nos. 24/2001...6/2023, Paragraf.rs legal information system.

activity”, which covers the income of individual entrepreneurs and some similar activities.

From the beginning, the 2001 IITL provided for both the general tax regime (20% rate on net income) and for lumpsum taxation (*paušalno oporezivanje*; Arts. 40–42). The initial criteria for lumpsum STR were:

- The individual is a registered entrepreneur, whose activity does not involve wholesale or retail trade (with the exception of trade in kiosks and automobile repair shops), hotel, catering, financial intermediation, or real estate activities, and who has no partners or investors;
- Maximum income of RSD 2 million (EUR 33,900).

The remaining rules for the assessment of tax base were to be adopted by the Government; the tax rate was 20% (the general one for individual entrepreneurs).

By 2024 the tax rate was gradually reduced to 10% for both the general tax regime and for lumpsum taxation, and the eligibility criteria for lumpsum taxation became more detailed:

- The restricted activities now also include advertising and marketing;
- Entrepreneurs are now permitted to sell their own products;
- The maximum allowed income is RSD 6 million (EUR 51,200);
- Individual entrepreneur is not a VAT payer (although compulsory threshold for registration as VAT payer is RSD 8 million, there is option for voluntary registration).

Detailed rules on assessment of the lumpsum tax are still set by the Government within the framework laid down in Article 41 of 2001 IITL.<sup>63</sup> These rules include the average monthly salary in the given municipality as the initial tax base, eligible areas of activities (based on classification) and the multipliers for the tax base for each area of activity, the location of the business, the age of the business, and the age of the entrepreneur. Lumpsum taxpayers must keep a ledger of income, while the tax authorities have the power to require them to switch to general financial accounting if they cease to meet eligibility criteria (Arts. 42 and 43 of 2001 IITL). Overall, this STR became rather popular, as Serbian Business Reg-

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63 RS: Order on detailed conditions, criteria and elements of lump-sum taxation of individual income tax on income from independent activities [Uredba o bližim uslovima, kriterijumima i elementima za paušalno oporezivanje obveznika poreza na prihode od samostalne delatnosti], *Official Gazette of the RS*, Nos. 94/2019...89/2023, Paragraf.rs legal information system.



isters Agency reported that around 43% of all entrepreneurs had chosen this regime as of 2020.<sup>64</sup>

In April 2021 the Law on Amendments and Additions to Individual Income Tax Law<sup>65</sup> introduced the so-called STR for freelancers (Arts. 12b, 56(2), 85(1)(18), etc. 2001 IITL) – an interesting fact is that even while this term is used widely and officially (even in the dedicated information system of the Tax Administration), the law does not contain the word “freelancer”. This STR provides a tax base equal to the reported income, with the deduction of a nontaxable amount (the same as for salary income) and a tax rate for “other income” equal to 20% (and SSCs).

The adoption of this law triggered public discussions and even protests, whereas the Tax Administration discovered and made public the fact that over 41,000 Serbian residents received income from abroad but did not report it or pay any taxes.<sup>66</sup> During the discussions the stakeholders found out that the Serbian freelancers working remotely for foreign contractors were not covered by the social security system, and that the existing tax regimes did not consider their ability to pay.<sup>67</sup> Nevertheless, many freelancers registered as individual entrepreneurs subject to lumpsum taxation thus being taxed much more leniently than in the case of employment (as their tax burden did not correlate with their actual income), even through their relation with the principal(s) were more of employment in nature.

However, Serbia also introduced an “independence test” (Art. 85(1) (17) of 2001 IITL), under which all the “entrepreneurs” who carried out remunerated activities for a single principal, or a person related to the principal, had to meet no more than four criteria in order to keep pay-

64 Popović, D., 2022, *Tax law [Poresko pravo]*, Belgrade, Pravni fakultet Univerziteta u Beogradu, p. 365.

65 RS: Law on amendments and additions to the Individual Income Tax Law [Zakon o izmenama i dopunama Zakona o porezu na dohodak građana], *Official Gazette of the RS*, No. 44/2021, Paragraf.rs legal information system.

66 Nova ekonomija, 2021, Poreska identifikovala uplate iz inostranstva za preko 41.000 frilensera [Tax administration identifies payments from abroad for more than 41,000 freelancers], *Nova ekonomija*, (<https://novaekonomija.rs/vesti-iz-zemlje/poreska-identifikovala-uplate-iz-inostranstva-za-preko-41000-frilensera>, 10. 09. 2024).

67 Savković, Č., 2022, Frilenseri nezadovoljni predlogom države: Plaćaš porez, nemaš prava [Freelancers displeased with state's proposal: You pay taxes, but have no rights], *Nova ekonomija*, (<https://novaekonomija.rs/vesti-iz-zemlje/frilenseri-nezadovoljni-predlogom-drzave-placas-porez-nemas-prava>, 10. 09. 2024); Savković, Č., 2022, Frilenserima potreban jasniji pravni status, kaže Ministarstvo finansija [Freelancers need clearer legal status, says Ministry of Finance], *Nova ekonomija*, (<https://novaekonomija.rs/vesti-iz-zemlje/frilenserima-potreban-jasniji-pravni-status-kaze-ministarstvo-finansija>, 10. 09. 2024).

ing the tax on income from independent activity (possibly lumpsum).<sup>68</sup> The criteria involve setting of time of work and rest, use of the principal's premises, use of the principal's equipment, the hiring of the "entrepreneur" via job advertisement or HR agency, and other criteria distinguishing employee from independent contractor. Those "entrepreneurs" who did not pass the independence test were subject to the tax on other income (reduced by a fixed deduction) at the rate of 20% (plus SSC).

Nonetheless, in December 2022 the STR for freelancers was amended with higher deduction (RSD 96,000 per quarter, or EUR 818) and with second option to reduce the tax base by RSD 57,900 per quarter (EUR 493) plus 34% of gross income and 10% IIT (plus SSC).

The resulting STRs in Serbia are summarized in Table 3.

Table 3. STRs for individual entrepreneurs and freelancers in Serbia

	Lumpsum tax	Freelancers – Option 1	Freelancers – Option 2
Eligible taxpayers	Individual entrepreneurs	Individuals, who earn income from foreign legal entities, individual entrepreneurs or individuals, or other Serbian individuals who are not tax agents	
Maximum annual income	RSD 6 million (EUR 51,200)	Not applicable	
Taxable item	Assessed lumpsum income	Income self-reported via the "Freelancers" portal run by the Tax Administration	
Tax base	Assessed lumpsum income with multipliers	Gross quarterly income with a fixed deduction of RSD 96,000 (EUR 818)	Gross quarterly income with a fixed deduction of RSD 57,900 (EUR 493) plus 34% of gross income
Tax rate	10%	20%	10%
SSC rates	<ul style="list-style-type: none"> <li>• 24% for pension insurance</li> <li>• 10.3% for medical insurance</li> <li>• 0.75% for unemployment insurance</li> </ul>	<ul style="list-style-type: none"> <li>• 24% for pension insurance</li> <li>• 10.3% for medical insurance (minimum RSD 4,789, unless insured otherwise)</li> </ul>	<ul style="list-style-type: none"> <li>• 24% for pension insurance (minimum RSD 25,218)</li> <li>• 10.3% for medical insurance (minimum RSD 4,789, unless insured otherwise)</li> </ul>

**Source:** 2001 IITL and Law on Contributions for Compulsory Social Insurance (versions effective in 2024).

68 RS: Law on amendments and additions to Individual income tax law [Zakon o izmenama i dopunama Zakona o porezu na dohodak građana], *Službeni glasnik RS*, No. 86/2019, Paragraf.rs legal information system.

The legal consequences of Serbia's STRs are somewhat complicated. For example, there is the separate legal status for freelancers, who *de facto* render independent services without registration as an individual entrepreneur (furthermore, STR rules are in the section on IIT on income from other sources). The Tax Administration confirmed that employees, unemployed persons, owners of legal entities, and individual entrepreneurs may also register as freelancers and report their income from respective activities. To a certain extent this is within the logic of the Serbian schedular IIT system, which distinguishes seven types of income (and includes a surtax on excessively high income). However, different statuses may complicate tax control, and also require a person to keep different sets of documents for different sources of income.

The effective tax and SSC burden under the STR for freelancers can be kept at around 20% of gross income, and lumpsum tax burden is also considerable, which makes no sense for business splitting. The inclusion of SSC in STRs means that the taxpayers are covered by the state pension and medical insurance, which provides no ambiguity.

There is a general provision (Art. 12 of 2001 IITL) that foreign IIT can be credited against Serbian IIT. The Serbian Tax Administration confirmed that foreign IIT can be credited against Serbian tax under the STR for freelancers; it is also reasonable to conclude that the tax credit would be valid for the lumpsum IIT.

## 6. DISCUSSION AND CONCLUSIONS

In all four cases the countries introduced STRs in early to mid-1990s, and in all four cases there are apparent trends. There are also three distinct periods:

- 1990s: development of first rules. Czechia introduced a new IIT, including a fixed deduction. Kazakhstan empowered the tax authority to establish the procedure for paying taxes “based on patent or a simplified system of determining the tax base.” Russia opted for replacement taxes (based on gross or net income), which could be amended by regional authorities. Serbia authorized the government to develop rules for lumpsum taxation.
- 2000s: elaboration of the rules. Czechia developed lumpsum taxation based on estimated income and expenses. Kazakhstan formally adopted the Tax Code which included detailed rules on patent and simplified tax return STRs, for both individual entrepreneurs and legal entities, as well as a “one-time coupon” STR for non-

registered individuals. Russia elaborated the simplified tax system and imputed income tax, including both individual entrepreneurs and legal entities, covering taxes and SSCs. Serbia elaborated the rules for lumpsum taxation, but authorized the government to establish detailed rules.

- After 2010: modern rules. Czechia introduced lumpsum tax with fixed rates depending on amount of income. Kazakhstan went through two tax codes, introducing a range of STRs – most for both individual entrepreneurs and legal entities, one for individual entrepreneurs (STR with mobile app) and one for nonregistered individuals (short-lived unified cumulative payment). Russia significantly raised the limits for simplified tax regime, making it a tax regime for SMEs (not just small businesses), replaced imputed income tax with patent tax system (for individual entrepreneurs only), and opted for separate calculation of SSCs (which could be deducted from the tax base or amount of tax). It also introduced the experiment with TPI, based on simplified reporting and calculation, although the status of taxpayers is unclear. Serbia introduced a STR for freelancers, based on simplified reporting and calculation with otherwise standard rules.

There are two regional similarities: Czechia and Serbia opted for special features in their laws on individual income taxes (section of law in the case of Czechia), while Kazakhstan and Russia preferred a plethora of special regimes designed for both individual entrepreneurs and legal entities – and even nonregistered entrepreneurs. The latter case complicates tax control and other administration, as one taxpayer may use different tax regimes for different types of income (which may be out of scope of IIT schedules).

Of these countries, Serbia chose a higher tax burden with simplified compliance burden (in cases of lumpsum taxation and the STR for freelancers). The maximum annual income for lumpsum tax is a moderate EUR 51,200, although there is no such limit in the STR for freelancers. The positive features of such an approach are fundamental adherence to the schedular design of IIT, a lack of incentives for business splitting, and the possibility of application of double taxation avoidance treaties. Another benefit is the coverage of entrepreneurs and freelancers by the social security system. However, the uncertain legal status of freelancers and manifold statuses of the same person may complicate tax administration. Another issue, which triggered heated discussion in Serbia several years ago, is that lumpsum taxation covers highly educated professionals whose high actual income may result in an unproportionately low tax burden (especially if those professionals have relaxed accounting and reporting

obligations, which was the case with attorneys and private doctors). An aggravating factor was the limit for the annual increase of the tax burden, which expired in 2014 and resulted in reported year-to-year increase of the tax burden – in some cases by 300%. This issue is more economic in nature but has different legal solutions, including automated increase of tax rates (like the use of the MAI in Kazakhstan), exclusion of such activities from STR (e.g., both Kazakhstan and Russia excluded notaries and attorneys from STRs), and use of tax audits for timely and careful reassessment of the tax burden.

Czechia only recently reduced the tax burden, which may trigger tax optimization, but there is no relevant data currently available. At the same time, the lumpsum STR incorporated SSCs and foresaw the application of double taxation avoidance treaties, which is a positive development.

Kazakhstan has featured frequent changes in tax regulations (living up to its nickname “tax lab” in an earlier article<sup>69</sup>); the downside of that is uncertainty for taxpayers even in the midterm planning, worsened by the revamping of tax compliance rules with each reform (about every 7 years), which may become inconsistent due to editing process (this also leads to distrust in any tax reform, although this is not a legal issue). Kazakhstan established a low tax burden and moderate to relatively high maximum annual income threshold (currently EUR 24,300 for patent STR, with a tax rate of 1% of gross income, and EUR 165,900 for simplified tax return STR, with a tax rate of 3% of gross income), as well as oversimplified mobile app and unified cumulative payment STRs. This triggered widespread tax optimization – effectively an abuse of the law in the form of business splitting. Tax control helps to identify and rectify some cases, but Kazakhstan apparently lacks review and analysis of its domestic practice of tax dispute resolution. The Tax Code presents all STRs as special rules for the calculation of the IIT (or CIT, respectively), which allows for the application of double taxation avoidance treaties. An interesting and useful feature is the setting of limits in special units (MAI), which are subject to annual (or more frequent) adjustment for inflation, automatically adjusting the tax thresholds (along with rates of state duties, penalties, etc.).

Russia is the only country of the analyzed four to maintain special taxes replacing IIT, CIT and property taxes, which precludes the application of double taxation avoidance treaties. It also allows for multiple tax statuses of one person. Due to the low tax burden, as in the case of Kazakhstan, it has experienced significant abuse of the law in the form of business splitting – even with the annual income threshold for STRs for individual entrepre-

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69 Tyutyuryukov, N. N., Tyutyuryukov, V. N., 2010, Kazakhstan – Tax Laboratory of Eurasian Economic Community, *Taxes and Taxation*, No. 1, pp. 54–60.

neurs being nearly EUR 2 million. It has also experienced substitution of labor contracts with civil law contracts, where “employees” may be individual entrepreneurs or payers of TPI (to save on IIT and SSCs). However, the Russian Ministry of Finance, FTS and courts have been continuously reviewing tax disputes practices and have issued relevant guidance documents, which is definitely a strong point. Another strong point in Russia is the developed and digitalized system of tax control (AIS Nalog 3), which partially reduces the scale of aggressive tax optimization.

Interestingly enough, in public discourse in Kazakhstan and Russia, no one has raised the issue that the mere existence of STRs with low tax burden triggers business splitting and allows for personal tax optimization. While taxpayers reasonably praise the low tax and compliance burden as helping them doing business, the politicians and public officials also support this position as a kind of state aid and a stimulus for economic development (even while it undermines revenues of the regional and municipal budgets – which are the main recipients of the respective tax revenues). Both countries also rely on expensive tax control to fight the abuse of tax law. Even though Kazakhstan developed a set of rules to preclude business splitting in its last Draft Tax Code, it only affects related parties, while business splitting practices involve friends and employees with no formal relations.

Another common feature of STRs in Kazakhstan, Russia and Serbia is the creation of different legal statuses of the same person (employee, self-employed/freelancer, individual entrepreneur). While STRs were intended to simplify tax compliance, this situation, on the contrary, triggers ring-fencing and more complicated evidencing of income earned under each separate status.

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## PRAVNE POSLEDICE POSEBNIH PORESKIH REŽIMA ZA PREDUZETNIKE U POSTTRANZICIONIM EKONOMIJAMA

Vladimir Tiutiuriukov

### APSTRAKT

Ovaj članak daje uporednu pravnu analizu prakse četiri posttranzicione ekonomije (Češke, Kazahstana, Rusije i Srbije) sa posebnim poreskim režimima za preduzetnike od 1990-ih godina do danas. Od zemlje do zemlje analiziramo kriterijume prihvatljivosti i glavne elemente svakog posebnog poreskog režima – bilo da se zasniva na paušalnom porezu, na oporezivanju pripisanog dohotka ili na oporezivanju stvarnog prihoda, i to za postojeće i za ukinute režime. Analiziraju se i njihove pravne implikacije. U zaključku, u radu se porede i suprotstavljaju njihove karakteristike kako bi se identifikovale njihove prednosti (kao što su doslednost poreskog sistema, smanjenje tereta ispunjavanja poreskih obaveza, automatsko prilagođavanje na inflaciju) i nedostatke (neizvesnost za poreske obveznike, podložnost zloupotrebi zakona i izbegavanju poreza).

**Ključne reči:** poseban poreski režim, paušalni porez, porez na pripisani dohodak, oporezivanje fizičkih lica, preduzetnici, samostalna delatnost.

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