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SIGNIFICANCE AND TAX TREATMENT OF REVERSE FACTORING AS AN INSTRUMENT FOR FINANCING SMALL AND MEDIUM-SIZED ENTERPRISES IN THE REPUBLIC OF SERBIA

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Abstract: In modern market circumstances, when competition is becoming more and more ruthless, especially in the period of the continuing immanent duration of the effects of the world economic crisis, which has a vertical depth effect (both those who have significant funds and those who do not have free funds, i.e. they are not liquid, feel it) when fresh capital is getting harder and harder, only those companies can survive that have a constant and regular inflow of fresh capital. In an economic situation in which the dominant role is played by large capital (multinational corporations or regional corporations), where acquisition is increasingly sought, the pressure on small companies becomes more pronounced and stronger. For companies that are organized as small or medium, the inflow of fresh capital is a luxury for the reason that the right to claim is exercised over a longer period of time (30-90 days) with the risk of being unable to collect the claim. It should be emphasized that: a) lack of fresh working capital; b) the frequent absence of own funds (reserve funds) and c) the impossibility of obtaining favorable loans in the current circumstances, inevitably implies that small and medium-sized companies are finding it increasingly difficult to survive. In addition to the fact that globalization has negative effects on the micro-economy, it should be emphasized that the development of the market economy continuously and permanently affects the creation of new and the evolution of existing financial instruments for financing production. Factoring is one of the modern financial instruments that is gaining more and more importance both at the macro and micro level (primarily referring to the countries that belonged to the Eastern Bloc market), and which belongs to the group of parabanking operations. Factoring as a parabanking business in export-oriented economies appears as one of the indispensable financial instruments for financing small and medium-sized companies. One of the specific forms of factoring that has evolved in modern business practice caused by the COVID pandemic is reverse factoring. Reverse factoring as a special type of factoring is contracted between the factor and the debtor from the contract for the sale of goods or the provision of services in the country and abroad, on the basis of which the factor, by taking over invoices from the debtor, assumes his obligation to pay towards the creditors, and has the right to collect from the debtor within from the agreement for the sale of goods or the provision of services in the country and abroad. The legal validity of the reverse factoring deal depends on securing the creditor's consent. The debtor is obliged to secure the creditor's consent, otherwise the reverse factoring contract cannot be concluded. The paper will also pay special attention to the tax treatment of income generated on the basis of factoring business in accordance with the positive legal regulations of the Republic of Serbia.

Keywords: Factoring, reverse factoring, tax treatment, creditor, factor, agreement for the sale of good.
Field: Social science.

1.INTRODUCTION

As a specific financial instrument for business financing, factoring is gaining more and more importance at the macro and micro level. Factoring as a specific parabanking operation is complementary to traditional banking operations (Ђорђевић, 2008, p. 25). For a long time, legal theory and business practice classified factoring as an independent legal transaction without properties of a banking transaction (Зиндовић, 2011, pp. 17-19), with the prevailing view that factoring is an independent banking transaction nowadays. Factoring is the financial service of selling and purchasing existing non-matured or future short-term accounts receivable, arising from agreements on the sale of goods or provision of services, either nationally or abroad (Article 2. par. 1(1), Factoring Law - FLRS, 'Official Gazette of the RS', no. 62/2013).

The increase in the production volume and the impossibility for small and medium-sized enterprises to secure favorable credit lines create the necessary conditions for the development of the factoring market in the Republic of Serbia. The inflow of fresh capital is a 'luxury', for the reason that the right to

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accounts receivable is exercised in a longer period of time of 30-90 days (Kerkovic & Mihajlov, 2012, p. 429) with a high degree of risk of collection of receivables. By applying the factoring mechanism, small and medium-sized enterprises are given the opportunity to access an alternative source of financing. Factoring in export-oriented economies is one of the indispensable financial instruments for financing small and medium-sized enterprises (Borgia, Burgess & Shank 2003, pp. 38-45). The support of monetary, tax and legislative authorities creates a stable basis for the development of factoring business in the Republic of Serbia, primarily because they have an interest in promoting the development of domestic production and exports. Factoring as a business of financing short-term accounts receivable has four functions, specifically: 1) financing the client based on a loan to the assignor or through an advance payment given to the client (advance financing) or based on the sale of accounts receivable to the factor (discount financing); 2) collection of accounts receivable; 3) assumption of risk (security) of accounts receivable collection (del credere function) and 4) service function (bookkeeping, recordkeeping, advisory and other outsourcing services) (Art. 1(2)(b) UNIDROIT Convention on International Factoring).

2. FACTORING AGREEMENT SUBJECT MATTER

The subject matter of a factoring agreement can be any existing non-matured or future, whole or partial, short-term accounts receivable arising from agreements on the sale of goods or provision of services, entered into by and between legal entities and entrepreneurs (Art. 2. par. 1 (2), FLRS). The provision in the factoring agreement, by which the sale of a future accounts receivable is carried out, produces a legal effect at the moment of the origination of the account receivable (Art. 3. par. 1, FLRS). The subject matter of factoring can be an account receivable of a legal entity and entrepreneur arising from an agreement on the sale of goods or provision of services concluded with the beneficiary of funds from the budget of the Republic of Serbia, the budget of an autonomous province or the budget of local self-government units, as well as the beneficiary of funds from mandatory social insurance organizations (Art. 2. par. 2, FLRS). Only receivables that arise between legal entities can be the subject of a factoring agreement. Receivables that arise from the contractual relationship of natural persons cannot be the subject of a factoring agreement, but as such are the subject of an assignment agreement. It is also important that the subject of factoring cannot be an account receivable arising from the sale of goods or the provision of services for personal, family or household needs (Art. 4, par. 2, FLRS). Factoring agreements of one assignor entered into with different factors, the subject matter of which is the sale of the same account receivable, are prohibited, and any such subsequently concluded agreement is null and void (Art. 22, par. 1, FLRS). It is allowed for the assignor to enter into several agreements with different factors, but only on the condition that the subjects of the sale of accounts receivable have a different legal basis. The subject matter of the agreement can be further sold and transferred from one factor to another factor, unless this is expressly prohibited by the factoring agreement (Art. 31, FLRS). The primary agreement (assignor - creditor from the core business and the debtor) or the debtor's general terms and conditions of business may stipulate a ban on the sale of accounts receivable. Regardless of whether the above prohibition is provided for in the primary agreement or in the debtor's general terms of business, it does not produce legal effect, that is, the assignor can sell its accounts receivable to the factor. However, in order for the assignor to be able to sell its accounts receivable to the factor despite the ban, two requirements have to be met: a) that it is in accordance with the law and b) that it is not regulated otherwise by an international agreement (Art. 30, FLRS). The legislator remains vague in terms of what is to be considered an international agreement. Whether it is an international agreement when the parties come from countries that are signatories to the convention or it is an international agreement when only one member is a signatory to the convention or when none of the parties is a signatory to the convention.

3.REVERSE FACTORING

3.1. Concept of reverse factoring

The current economic situation is forcing companies to manage liquidity in a better manner. Supply chain financing can be an attractive way for companies to improve their working capital position. Because it is initiated by a large customer to help its suppliers finance their accounts receivable faster and at a lower interest rate than they would otherwise receive on a regular basis, reverse factoring is also known as supplier factoring (supplier financing), or supply chain factoring. Reverse factoring is an agreement between a factor and a (usually strong) customer-debtor whereby the factor offers each supplier the ability to finance those invoices that are approved for payment. In order to support exporters, which was necessary for the growth of the factoring industry, a reverse factoring system has been developed (Матић, 2014, p. 272). Reverse factoring belongs to the group of Supply chain financing techniques. Supply Chain Finance can be best defined as the use of financing and risk mitigation practices and techniques to optimise the management of the working capital and liquidity invested in supply chain processes and transactions. (Hausemer & Rzepecka & Atanasova & Lechardoy & Michaelsen & Sadlik & Kubovicová, 2020, p. 13).

Reverse factoring is one of the related services, although it is not a legal counterpart to factoring, it is similar in terms of the way it deals with financing, i.e. represents a variation of the basic factoring service. The reverse factoring symbolizes financing of procurement rather than sales, as in the factoring industry, and transfers debt from the core business arising from the supply of products and services from the customer to the factor. As such, it is a special type of factoring that is contracted between the factor and the debtor from the agreement on sale of goods or provision of services in the country and abroad, on the basis of which the factor, by accepting invoices from the debtor, assumes its payment liability to the creditors, and has the right to collect from the debtor within the term of the agreement on sale of goods or provision of services in the country and abroad (Матић, 2014, pp. 268-285; Article 18, FLRS). In case of factoring, the client receives money from the factor at its disposal, however, in reverse factoring, the factor directly settles the debts to the suppliers, and the money that the client set aside to pay its debts to the supplier can be used to improve business. In essence, reverse factoring represents the purchase of other people’s accounts receivable, that is, factoring financing is a way of obtaining funds by selling accounts receivable (Мартиновић & Недовић, 2015, p. 188).

3.2. Peculiarities of reverse factoring

Although it is similar to traditional non-recourse factoring in terms of its characteristics, reverse factoring differs in that it finances the customer’s liabilities to the supplier, and does not purchase its accounts receivable (Касавица, 2014, p. 112). In addition to this difference, reverse factoring has two crucial differences compared to ordinary factoring, specifically: a) first, upon receipt of goods, the customer would approve the invoice, and this approval is a guarantee of payment by the customer, which allows the supplier to obtain funds at a more favorable borrowing rate and b) second, in exchange for the offer of the reverse factoring program, the customer requests an extension of the payment delay to the supplier (Kouvelis & Xu, 2020, p. 20-21). The aim of the procedure is to finance the supplier’s receivables from the financier - the factor, so that the supplier can quickly cash the invoices for what it has sold.

Unlike factoring, reverse factoring involves a financially strong buyer and less reliable suppliers who need a financial platform to fill the liquidity gap that arises over a certain longer credit period. It should be noted that, unlike conventional factoring, the idea does not come from suppliers who would provide the factor with their invoices in exchange for early payment, but the whole process is initiated by the bank’s client. There must be a time delay between the day when the factor provides the client with funds and the day when the debtor pays the factor from the client’s core business for reverse factoring to have a financial effect (there would be no financing service if it were agreed that the factor would make the payment on the day the account receivable is due or on the day of the actual debtor’s payment). Based the submitted documentation that proves the existence, the bank finances the unsettled, overdue, undisputed liabilities of the client (customer) and takes over related accounts receivable from suppliers connected with the client (customer). Reverse factoring is used to finance the settlement of the customer’s debts to the supplier as a result of the sale of goods or services. There is a possibility for the client to settle its liabilities to the supplier much faster and without payment delays, improves its business relationship with the supplier in such a way that it has the possibility to negotiate for better terms of sale of goods and price, and the services it purchases from them. (Gaćeša, 2020, p. 2).

The process of reverse factoring usually involves several steps. First, the buyer-debtor (client) submits a request to the factor for reverse factoring after the seller or the supplier, has sold and delivered the products to it and issued an invoice with deferred payment. The factor assesses the creditworthiness of the client (debtor) and approves the upper limit of financing for the client. As soon as the reverse factoring agreement is entered into, the factor pays the supplier 100% of the agreement value and sends the debtor an invoice for the factoring fee pursuant to the terms of the agreement and the seller’s accepted notification that the debt has been transferred to the new debtor, the factor (client). Extremely creditworthy clients and debtors are dealt with without security measures, and the contracting parties enter into a reverse factoring arrangement without recourse, i.e. security measures (Матић, 2014, p. 274).

The purchase of accounts receivable as per issued invoices is carried out by paying the nominal value of the invoice to the client's account, less the amount of the discount calculated from the date of purchase, until the due date of the invoice, as well as the amount of the fee for processing the request. This is known as the discount redemption principle. The entire nominal amount of the acquired invoices becomes the property of the factor after payment of the invoices. Another way of executing the work involves payment to the client's account of the agreed percentage of approximately 80% of the nominal value of the invoice, less the amount of the estimated fee for processing the request. The rest of the percentage amount up to the full nominal amount of the invoice is contracted as a guarantee fund. The amount of the advance paid to the client plus interest calculated on the amount of the advance paid, from the day of payment of the advance to the due date - after payment of purchased invoices - bill collection, as well as for other contracted commissions and costs, belongs to the factor. The client is responsible for paying the remaining amount up to the full nominal amount of the invoice.

It is the customer's responsibility to provide accurate and irrevocable information regarding their liabilities and to ensure that each supplier participates in the program. The accounts receivable financing is based by the factor on the customer's creditworthiness. As a result, it is not necessary for the client's suppliers to have a good credit rating. However, a good assessment of the client's creditworthiness is important in order to settle accounts receivable appropriately (Klapper, 2006, pp. 3111–3130). Therefore, reverse factoring is a method used in transition countries where the private sector consists of small and undercapitalized enterprises that rely on multinational or foreign buyers seeking local, cheaper suppliers. In the case of factoring, based on the findings of the investigation into the creditworthiness of the client and the debtor, the factor will determine whether it is advantageous for it to contract factoring with or without the right of recourse. The factor has the possibility to demand payment from the client if, upon maturity of the purchased invoices, it is unable to collect its accounts receivable from the main debtor thanks to the right of recourse (Матић, 2014, p. 275).

4. ADVANTAGES OF REVERSE FACTORING

4.1. Advantages for customers

In reverse factoring, the customer improves its relationship with its suppliers, gets preferential prices from them, reduces costs and increases liquidity. Without using its own resources, the customer helps the suppliers. Based on supplier factoring, the customer can establish long-term business relationships with a selected group of suppliers because they benefit from receiving 100% of the invoice value immediately, as opposed to the reduced amount provided by a standard factoring arrangement. The customer, on the other hand, has additional cash and can use it to pay other due liabilities. Costs are reduced because invoice payments are concentrated with one component and not spread over several suppliers (Матић, 2014, 276). As for other benefits, reverse factoring makes it possible to extend the days payable outstanding. This is a consequence of greater negotiating capacity with suppliers, as a result of using a safe financial instrument. Furthermore, working capital requirements are financed by suppliers instead of bank loans, thus improving the balance sheet structure. In fact, defaulting on a regular bank loan appears to be more likely than defaulting on a reverse factoring agreement, as paying the supplier guarantees business continuity and it is easier to restructure the debt. Another advantage is that it reduces payment processing costs, as well as administrative expenses, by imputing the entire management of supplier payments to the bank. (Falcão, 2014, p. 11).

In general, the advantages for the customer are: 1) postponement of the deadline for payment of debts, which results in faster cash flow (when the customer and supplier are notified of the approval of the reverse factoring transaction, the existing invoice or agreement is attached in order to extend the deadline for payment by the customer, which extends the deadline for payment by the supplier. This happens before implementation and before the account receivable is transferred from the supplier to the factor. The fact that the annex has already been decided during the negotiation period and the fact that the supplier is aware that after signing the annex it will receive the money soon and before the original due date affect its decision to agree to the annex (due before the annex). Such 'extended accounts receivable' are then transferred to the factor, and the customer undertakes to pay the factor in accordance with the newly established payment term); 2) increased emphasis on proactivity in working capital management; 3) reduced costs related to payment processing because the payment is made by the factor (bank); 4) the possibility of increasing earnings through receiving an advance rebate in exchange for timely payment to suppliers; 5) improved relations with suppliers while laying the foundation for future negotiations with improved procurement conditions; 6) the image of the company is improved and its suppliers are more loyal because the company is perceived as a company that takes care of the interests of its suppliers; 7) the possibility of using money that has been accumulated to settle supplier accounts, for liquidity or for investment; 8) the customer (client) has no costs because all these costs, including interest and fees, are borne by the supplier and 10) it increases the reliability of links within the supply chain and reduces the probability of operational risk as a result of the presence of an additional controller (bank). Verification of data on invoices, comparison with orders (purchase orders), mutual reconciliation of open accounts payable card (customer) and open accounts receivable (seller), as well as with data from invoices, purchase orders and other sources, what this phrase refers to (Касавица, 2014, pp. 112-114). In addition to the obvious benefits of interest income and fees, a factoring company that uses the mechanism of reverse factoring also has access to new clients with the potential for long-term business. Since it deals directly with large clients as a financier, the factor can deal with suppliers faster and easier than if it went to each client's supplier. In this way, numerous minor hazards are condensed into one, unimportant risk.

4.2. Advantages for suppliers

Reverse factoring enables the supplier to access a loan on more favorable terms, and this is possible only because the bank relies on the stronger credit rating of the customer. If the suppliers decide to take a loan, the length of the accounts receivable period is reduced, as well as the length of the bank loan. Even without an advance payment, it ensures receipt on the due date and avoids losses due to unrecoverable payments, reducing the administrative costs of collection (Falcão, 2014, p. 11).

Reverse factoring produces the following advantages to suppliers: 1) faster conversion of accounts receivable into cash, acceleration of the cash cycle; 2) access to additional financing that may not be available based on a balance sheet review (especially for smaller businesses, which are most affected by the wave of bankruptcies); 3) reduction of financing costs as a result of the dependence of costs on the rating of a strong customer; 4) elimination of risks related to the collection of receivables, in addition to reducing costs related to their management; 5) when a reverse factoring line is created and a positive credit history is established, there is the potential to demand discounting at any time during the transaction; 6) financing technique that does not appear in the balance sheet; 7) more predictable cash flow; 8) increases the reliability of connections within the supply chain and reduces the probability of operational risk as a result of the presence of an additional controller (bank). Verification of data on invoices, comparison with orders (purchase orders), mutual reconciliation of the card of open accounts payable (customer) and open accounts receivable (seller), as well as with data from invoices, purchase orders and other sources, what this phrase refers to (Касавица, 2014, pp 112-114).

Therefore, the advantages of reverse factoring for the supplier are more than clear, if it has weak or problematic finances, it has access to a credit line that converts invoices into new funds without the need for a pledge or other forms of security, then it has access to agreed preferential prices from the customer, reduces costs of managing its receivables and has the privilege of being insured against late payment by customers at no additional cost (Klapper, 2002, 13). The advantages of this instrument are especially important for suppliers, which are smaller and less creditworthy companies. However, strong clients do not necessarily do business only with risky firms. It may be the case that some suppliers also have a good risk profile. In this case, suppliers would most likely take advantage of a more favorable line of credit instead of seeking a bank loan. Therefore, it is important to test the creditworthiness of the supplier (Falcão, 2014, p. 12). With all these advantages for the three parties involved in the reverse factoring arrangement, it is only natural that this instrument increases the business flow, necessary to follow the economic expansion.

4.3. Advantages for banks

As for the advantages of factoring for the bank, reverse factoring builds stronger and more lasting customer relationships. By means of reverse factoring, the bank can expand its business with small businesses, suppliers, without taking on a greater risk. Reverse factoring increases the volume of financial flows by having a centralized organization, and also increases factoring transactions, thanks to advances. In addition, the bank knows exactly where and why the funds are used, unlike loans where the bank cannot track the purpose of lending. All this indicates that reverse factoring is a lower risk financial instrument for the bank, that is, all trade financing techniques, including reverse factoring, are considered an extremely low risk operation (Falcão, 2014, p. 10).

The advantages of reverse factoring for the bank are as follows: 1) the potential for greater profitability as a result of a smaller increase in the amount of required capital compared to traditional lending; 2) gaining new clients as a result of opening the door for the bank to work together with them through the financing of a large number of suppliers of a powerful client; 3) enables the creation of a closer relationship with clients and close cooperation with them in the long term - once established, it becomes a structure that is included in the business models of the participants, who become extremely dependent on it; 4) enables players in the supply chain to build their business more easily, resulting in increased demand for other banking products and 5) raises the potential of additional sub-sectors within the banking industry, such as the asset sector etc. (Касавица, 2014, p. 114).

5. TAX TREATMENT OF FACTORING IN THE LAW OF REPUBLIC OF SERBIA

As the supply of all products and services is subject to value added tax (VAT), the question arises as to the treatment of factoring from the aspect of this tax. Pursuant to the provisions of the applicable law, the subject of VAT taxation is the delivery of goods and the provision of services performed by the taxpayer in the Republic of Serbia for a fee, as part of the performance of its activity, as well as the import of goods into the Republic of Serbia. The provision of services means all transactions and actions within the scope of activities that are not delivery of goods. (Art. 3 and Art. 5, par. 1, Law on Value Added Tax of the Republic of Serbia - LVATRS, Official Gazette of the RS, no.84/04, 86/04, 61/05, 61/07, 93/12, 108/13,6/14, 68/14, 142/14, 5/15, 83/15, 5/16, 108/16, 7/17, 113/17, 13/18, 30/18, 4/19). Factoring is the financial service of selling and purchasing existing non-matured or future short-term accounts receivable, arising from agreements on the sale of goods or provision of services, nationally and abroad. Since VAT is taxed on the provision of services, the provider of the service in question (the factor) should appear as a VAT payer. However, according to the opinion of the Ministry of Finance, no. 011-00-00648/2017-04 dated 31/08/2017, the provisions of the applicable law, which prescribe tax exemption for business operations and intermediation in the transactions with accounts receivable, apply to factoring as well. This exemption applies to all forms of business and intermediation in the transactions with accounts receivable, checks, promissory notes and other similar securities, except for the collection of receivables for other entities (Art. 25 par. 1(6), LVARTS). According to the stated opinion of the Ministry of Finance, factoring is not about collection of receivables for other entities, because the factor collects due receivables in its own name and for its own account, and therefore it is a financial service to which the prescribed tax exemption applies. This means that VAT is not calculated and paid on the factoring fee. Before the passing of the law in 2013, which defined factoring as a financial service for the purchase and sale of an existing non-matured or future short-term accounts receivable, arising from agreements on the sale of goods or provision of services, nationally and abroad, the opinion of the Ministry of Finance no. 413-00-732/2009-04 dated 23/03/2009 was effective. Given that there was still no legal regulation of factoring, according to this opinion, the tax exemption from VAT referred to the fee (amount of commission or the value of the discount with which an account receivable was purchased) for the provision of services provided by the company within the factoring operations. The provision of services included the purchase of accounts receivable from suppliers of goods, that is, service providers before the due date, which meant that the suppliers of goods, that is, service providers transferred the account receivable to the factor - a company. The company was not obliged to calculate and pay VAT, but it did not have the right to deduct the previous tax either. By passing the law regulating factoring for the first time in our legislation, not only progress was made in factoring standardization, but defining it as a financial service enabled more precise application of the provisions of the tax law on its tax exemption. Traditionally, financial services are exempted from the VAT system in most modern countries. In financial theory, this is explained by reasons of a technical nature that the determination of the tax base in financial intermediation transactions is much more difficult. However, the dominant arguments are related to the negative effects of taxation of financial services on the level of the interest rate. Inclusion of financial services in the VAT system leads to an increase in interest rates, and thus, indirectly, it can lead, in the conditions of globalization mobility of financial services, to a serious outflow of capital to those countries that have a more favorable tax treatment of financial services. (Поповић, 1999, p. 819.) The tax law of the European Union follows the trend of excluding financial services from the VAT system. The provisions of Directive 2006/112/EC itemize transactions that are exempt from paying VAT (Art. 135 (1) a) b)-g) Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, Official Journal of the European Union 134/06). Regarding factoring, the judgment of the European Court in the case of MKG-Kraftfahrzeuge-Factoring GmbH (C-305/01) is relevant. According to this judgment, a company that purchases debts, assuming the risk of non-payment by the debtor, and which, in return, charges a commission from its users, performs economic activity in terms of Art. 2 and 4 of Directive 2006/112/EC and is therefore a taxpayer. That economic activity represents, according to the interpretation of this court, debt collection and the sale of claim rights, and the taxpayer has the right to deduct taxes pursuant to Article 17 of that Directive.

The factoring service provider (factor) is not obliged to calculate and pay VAT, but does not have the right to deduct the previous tax, because it is a tax exemption without the right to deduct the previous tax. Previous tax is the tax that was paid in the previous stage of the supply cycle. VAT is paid at each stage of the supply cycle from production to the end user, but only on the value added at that stage. The tax base, that is, the added value, is the difference between the purchase and sale price in the taxation stage. The VAT payment mechanism is such that the taxpayer, when calculating the tax at its stage of supply cycle, deducts the amount of the previous tax from the amount of tax it owes, that is, the amount paid by its predecessors in the supply cycle. The amount paid at the previous stage, which is included in the purchase price, must be documented by the taxpayer through an invoice. In the case of tax exemptions with the right to deduct the previous tax, the taxpayer is exempted from paying VAT, with the fact that it will have the right to a refund of the previously paid tax. This means that the taxpayer will have the right to request a refund of the amount of tax paid at the previous stage of the supply cycle. This compensation, that is, the tax refund, is made by the state from the budget. In this way, the taxpayer will be exempt from the tax paid at the previous stage of the supply cycle, which is included in the purchase price of products or services. Hence, this type of VAT exemption appears to be the most favorable for the taxpayer. Practically, the taxpayer is completely exempted from tax liability. In the case of VAT exemptions without the right to deduct the previous tax, the taxpayer does not calculate and does not pay tax on the supply of goods and services, but at the same time, it does not have the right to claim the deduction of the previous tax that was calculated and paid by the predecessors in the supply cycle, that is, its suppliers. Since the taxpayer of this type of VAT exemption does not calculate the tax, it cannot deduct from the tax the amount of the tax burden that was paid at the previous stage. In fact, it will bear the burden of the previous tax contained in the purchase price of the product. Tax exemptions without the right to tax deduction show a paradox in VAT: 'that the exempted one is actually taxed'. Although by law it is exempt from paying VAT, with this type of exemption, the taxpayer actually bears the tax burden, which it paid through the purchase price of its inputs (Поповић, 1999, p. 808).

As factoring appears as one of the indispensable financial instruments for financing small and medium-sized enterprises, the question arises whether such tax treatment of factoring in R. Serbia provides sufficient tax benefit to these enterprises. In EU member states, there is a large gap between the effective corporate tax burden and the statutory tax rate, and it shows that member states tend to use tax incentives to a large extent to achieve many economic goals (Ђурић-Тодоровић & Ђорђевић & Цакић, 2022, p. 27). The impact of the tax burden on the growth of the economy can be positive, because it ensures the financing of goods and services by the state that enable economic growth, such as education, research and development, infrastructure, etc. (Ранђеловић, 2021, p. 197). Noticing the importance of small and medium-sized enterprises for economic growth, an increasing number of countries have recently begun to apply various forms of tax incentives for them. In addition to others, tax incentives are applied for potential investors, which enables the establishment of a relationship between those economic entities that dispose of large capital and small and medium-sized enterprises that, as a rule, have little, or almost no, capital. In the tax legislation of Serbia, there is also a tax relief for investors (Art. 50. Law on Profit Tax, Official Gazette of RS, no. 25/01, 80/02, 43/03, 84704, 18/10, 101 /11, 119/12, 47/13, 108/13, 68/14, 142/14, 91/15, 112/15, 113/17, 95/18). Creators of tax policy in R. Serbia should consider the possibility of providing a more favorable VAT treatment of factoring in addition to the existing tax incentives. According to the imprecise provisions of the law, as well as according to the opinion of the competent ministry, these services are exempt from paying VAT but without the right to deduct the previous tax. In Ireland, for example, all factoring companies are exempt from VAT with the right to deduct input tax, except those that provide services to other businesses that do not have the right to deduct input tax (for example, if they carry out financial services that are exempt from VAT). Examples of good practice are Finland and Belgium, where the taxation of factoring services depends on the amount and method of determining the factoring fee. If the service provider buys the claim at a fair price and does not charge any special fee to its client, case law considers that this is not a paid service that is subject to taxation.

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