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EQUALIZATION OF EXCISE BURDEN ON STRONG ALCOHOLIC BEVERAGES A PREREQUISITE FOR JOINING THE EU

Five years after the explanatory and bilateral screening, Negotiating Chapter 16, which refers to taxation, has not been open for negotiations. According to the 2016 and 2017 EC reports, the key problem standing in the way of opening the chapter is the unequal excise burden on domestic and imported coffee and strong alcoholic beverages. The amendments to the Excise Law, introduced in 2018, eliminated fiscal discrimination in terms of the excise tax that need to be paid on imported and domestic coffee products, but missed the opportunity to equalize the tax treatment of strong alcoholic beverages. The amendments to the law last year did not solve this problem either, and this year Chapter 16 will most likely remain closed for negotiations. Therefore, the basic recommendation of this policy brief concerns the Ministry of Finance, which should initiate amendments to the Law on excises in order to equalize the excise burden on different types of strong alcoholic beverages.

INTRODUCTION

EU legislation relating to Chapter 16 covers indirect taxes to the extent possible, primarily value added tax (VAT) and excise tax. Excise tax represents a specific type of consumption tax, which additionally taxes certain categories of products such as energy, tobacco products and alcoholic beverages. An explanatory, analytical review of the harmonization of the legislation of the Republic of Serbia with the *acquis communautaire* for Negotiating Chapter 16 was held in October 2014, and a bilateral screening in March 2015. The report of the European Commission (EC), issued in July 2016, assessed that the Republic of Serbia is not sufficiently ready for negotiations, i.e., for opening the chapter. The main obstacle is the different tax, or tax treatment of coffee and strong alcoholic beverages. This violates Article 37 of the Stabilization and Association Agreement, which explicitly prohibits fiscal discrimination. According to the Excise Tax Law of 2016, the excise tax on coffee was calculated and paid only upon import, and not after its release on the market¹, so that

coffee importers were at a disadvantage compared to domestic producers. In addition, the Law stipulates that the excise tax on strong alcoholic beverages (spirits) is calculated and paid according to the category in which the spirit is classified and not according to the percentage of alcohol contained in a certain beverage. Specifically, **the excise tax on fruit brandy, grape brandy, wine and other fruit brandies with the addition of plant extracts is 134.6 dinars per liter², and 343.7 dinars is paid per liter for brandy made from grain and other agricultural raw materials.** In practice, this means that importers of this category of products (e.g. different types of whiskey) are in an unequal position in relation to domestic producers (traditional brandies, for example). Therefore, the only reason why this important economic chapter hasn't been opened for negotiations is the inconsistency of Serbian tax legislation with EU regulations, in terms of the excise tax charged on spirits.

Therefore, in its annual report, the European Commission was of the view that moderate progress has been made in this area. Even the successful implementation of the Tax Administration Transformation Program, which significantly improved the procedure for the collection of public revenues, did not affect the assessment or enable an affirmative answer to be given about the start of negotiations.

At the end of 2019, the Excise Tax Law was amended again, but without changes in the area of excise tax on strong alcoholic beverages. While this policy brief was published mid-2019, it is quite certain that, Chapter 16 will retain the status of a "closed chapter" in 2020. Even if the Excise Tax Law is amended before the end of the year, which has been the practice so far, the EC can approve the opening of the chapter in 2021 at the earliest.

1. The basic rule in the EU is that excise tax is calculated and paid once a particular product is placed on the market or once it leaves excise warehouse. The same rule is provided under our Law on Excise Tax (coffee products and strong alcoholic beverages are exempted until 2018).

2. <https://www.paragraf.rs/propisi/zakon-o-akcizama.html>

CURRENT REGULATIONS, NECESSITY OF ADDITIONAL HARMONIZATION WITH EU RULES

Excise duties in the EU are regulated by the Council Directive of 2008 (2008/118 /EC³, hereinafter the Directive), which, inter alia, prescribes minimum excise duties, while member states have the possibility to prescribe excise duties that exceed the minimum. According to the current Directive, excise duty is calculated per unit of measure (kilogram, (hectare) liter, per 1000 cigarettes, etc.) and member states are obliged to tax:

- alcoholic products (all alcoholic beverages);
- tobacco products (cigarettes, cigars, cigarillos, cut tobacco and other tobacco products) and
- energy products used for heating and transport (petrol, kerosene, gas oils, liquid petroleum gas, natural gas, coal, coke and electricity).

In addition, member states are given the right to impose excise duties on other goods in line with their objectives and priorities.

The system of excise taxation in the Republic of Serbia is regulated by the Excise Tax Law⁴. In the Republic of Serbia, excise tax is levied on four large groups of goods:

- alcoholic beverages;
- tobacco products (including e-cigarette refills);
- energy sources (oil derivatives, biofuels, bioliquids and electricity⁵);
- coffee.

In Serbia, as in the EU, there are two types of excise duties - specific excise tax, which is determined in nominal value - per unit of measure (kg, l, pack of cigarettes) and ad valorem excise tax, determined as a certain percentage of retail price of excise goods (33% retail price on cigarettes and 7.5% on electricity for final consumption).

In terms of the amount and structure of excise rates, Serbia is, to a significant extent, in line with EU directives. However, the expectation is that the Republic of Serbia will have harmonized all its regulations in the field of taxation with EU rules and directives by the time when the chapter is closed. Directives related to consumption taxes (VAT and excises) require a higher degree of harmonization of regulations, while direct taxes (taxes on labor and capital) require a significantly lower degree of harmonization. Harmonization of taxation in the EU, in addition to legislative harmoni-

zation with directives, also includes administrative and technical issues, which refer to the existence of appropriate capacities for the exchange of information and data, coordination of activities, improvement of software solutions, etc.

In the process of joining the EU, certain, additional changes will be necessary; they refer to the manner of defining in the Law (excise duties on spirits and electricity), and the amount (excise duties on cigarettes). With respect to taxation of energy, by the time Serbia joins the EU, it will have introduced excise duties on energy sources such as natural gas, coal and coke, and replaced the ad valorem excise tax on electricity (7.5%) with a specific excise tax, that is, prescribed in nominal amount. In terms of excise duties on tobacco products, at the time of EU accession, excise duties on cigarettes in Serbia will increase, because they are in absolute terms (observed in EUR / 1000 cigarettes) lower than the minimum excise duty prescribed by the EC.

EXCISE DUTIES ON SPIRITS IN THE EU

The Directive⁶ provides for a minimum excise duty per hectolitre of pure alcohol in the amount of 550 euros, or about 650 RSD per liter of alcohol. Only a few EU countries have prescribed excise duty that is slightly higher than the minimum⁷ while most countries have an excise tax of about 1,000 EUR per hectolitre of pure alcohol (also prescribed by the Directive as a minimum) - Austria, Italy, Luxembourg, Slovakia. Other EU countries apply an amount that is significantly above the minimum excise tax⁸, which has affected retail prices of strong alcoholic beverages.

A comparative overview of the amount of the minimum excise duty, in the case of strong alcoholic beverages (40% alcohol, 0.7 l package) in the EU is shown in the table.

EU minimum excise duty, per hectolitre of pure alcohol (EUR)	550	1.000
Per liter of pure alcohol (EUR) ⁹	5,5	10
Per liter of beverage containing about 40%	2,2	4
Per 0.7 l bottle and about 40% alcohol (EUR)	2,2	2,8
Per bottle of 0.7 l and about 40% alcohol (RSD)	182	330

3. <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32008L0118&from=GA>

4. <https://www.paragraf.rs/propisi/zakon-o-akcizama.html>

5. Mid-2015, final consumption of electricity was taxed by excise tax

6. https://ec.europa.eu/taxation_customs/business/excise-duties-alcohol-tobacco-energy/excise-duties-alcohol_en

7. Bulgaria- EUR 562.4, France – EUR 537.6, Croatia- EUR 715.1, Romania- EUR745.3

8. Finland (EUR 4,880), Sweden (EUR 4,781.3) and Ireland (EUR 4,257) have provided for excise tax that is significantly above the minimum

9. 1% of ethyl alcohol would be around RSD 6.5

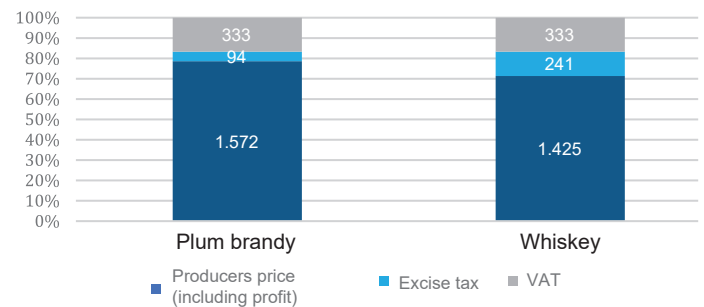
EXCISE DUTIES ON STRONG ALCOHOLIC BEVERAGES IN SERBIA

In Serbia, the excise tax is determined according to the type of alcoholic beverage, regardless of the percentage of alcohol in a specific type of beverage. In order for the EC to open a negotiating chapter, it is necessary to change the way of indicating or calculating excise duties, so that their amount is determined by the percentage of alcohol contained in a certain spirit. According to the law currently in effect, **the excise tax on fruit brandies (e.g. plums) is 134.6 dinars per liter, while the excise tax on grain brandies (e.g. whiskey) is 343.7 dinars per liter.**

The different tax treatment of domestic and imported spirits in Serbia is best illustrated by the chart showing the retail price composition of two types of spirits in accordance with the applicable amounts of excise duties. Two types of strong alcoholic beverages (both in a package of 0.7 l), plum brandy and whiskey (strong alcoholic beverage made from grain) were observed. Both products have a similar percentage of alcohol (over 40%) and a retail price of around 2,000 RSD. Although the same amount of VAT (333 RSD) is paid on both products, because the retail price is the same, the amount of excise duty differs significantly and in that sense it burdens whiskey more. Excise tax on plum brandy is paid in the amount of 94 RSD (5% of the price) and whiskey 241 RSD (12% of the price), i.e., excise and VAT make a little more than a fifth of the price of domestic brandy, but close to 30% of the price of imported whiskey. In other words, the amount of excise duty in the above example of plum brandy and whiskey should be the same or very similar (due to a small difference in% alcohol) for both products.

Given the amount of the minimum excise duty prescribed by the EU, **our proposal is to equalize the excise burden of strong alcoholic beverages by prescribing the same excise duty for all types of drinks (fruit brandy and grain brandy), equal to the minimum in the EU.** In other words, the excise tax should be 650 RSD per liter of pure alcohol, or 6.5 RSD per percent of alcohol, which means that the excise tax in the presented example of whiskey and plum brandy (40% alcohol, 0.7 liter package) would be about 180 RSD. This would eliminate fiscal discrimination between domestic producers and importers of these products. Therefore, in this policy brief, a comparative overview of the minimum excise tax is given, on the basis of which a proposal was made for equalization of the excise burden on domestic and imported spirits.

Retail price composition of spirits



Source: Excise Tax Law, calculation of authors according to applicable tax rates and retail prices

On the other hand, the EU Directive prescribes the possibility of applying lower excise duties on spirits produced by small distilleries. Namely, “small distilleries”, according to the Directive, are those persons who annually produce up to 10 hectoliters (1,000 l) of pure alcohol and who are completely economically and legally independent from other producers. For small distilleries, it is stipulated that the excise duty cannot be lower than 50% of the excise duty prescribed by the national legislation in a certain member state. Below is an overview of standard and reduced excise duties for small producers in EU countries¹⁰. In as many as 7 countries, the excise tax is exactly 50% of the regular, prescribed excise tax, while in Spain, for example, it is close to 88%, in Germany 56% and in Austria it is 54%.

Unlike the EU, Serbian legislation does not recognize the so-called small distilleries, considering that according to the Excise Tax Law, all producers of strong alcoholic beverages that are placed on the market are liable to excise duty, regardless of the quantity produced.

It is necessary to amend the Excise Tax Law in order to harmonise with EU rules and open the Negotiation Chapter.

10. https://ec.europa.eu/taxation_customs/business/excise-duties-alcohol-tobacco-energy/excise-duties-alcohol_en

Member State	Excise duty per hectolitre (EUR)	Excise duty per hectolitre (EUR), for "small distilleries"
Bulgaria	562,9247	281,2148
Croatia	715,1435	357,5718
Spain	958,94	839,15
Slovakia	1.080	540
Austria	1.200	648
Germany	1.303	730
Slovenia	1.320	660
Portugal	1.386,93	693,47
Denmark	2.009,2425	1.004,6213
Latvia	2.025	1.012,5

According to the Law on Strong Alcoholic Beverages, the production of strong alcoholic beverages can be performed by a legal entity and an entrepreneur entered into the Register of Producers of Strong Alcoholic Beverages, which is maintained by the ministry responsible for agricultural affairs.

In the EU, the minimum excise tax is prescribed according to the percentage of alcohol contained in the beverage, and in domestic legislation, the amount of excise tax depends on the category of beverage.

CONCLUSION AND RECOMMENDATIONS

As already mentioned, the Republic of Serbia has harmonized part of the regulations with the EU in the field of taxation (amendment of the Excise Tax Law in 2018). However, the first and only condition for starting negotiations with the EC is the elimination of fiscal discrimination in terms of the level of excise duties on strong alcoholic beverages. As long as producers of spirits made from fruit pay 60% less than producers of grain spirits, the EC will not approve the opening of

the chapter and further accession negotiations. Taking into account the existing legislative framework and the requirements of the EC arising from the Directive, the key recommendations are:

1. **that the amount of excise duty levied on spirits be calculated according to the % of alcohol and not according to the type of drink.** The proposed amendment to the Excise Tax Law would finally eliminate the de facto different treatment of domestic and imported spirits and the EC would approve the opening of a negotiating chapter;
2. **that the amount of excise duty on strong alcoholic beverages be equal to the minimum in the EU.** In accordance with the above example, this would mean that the excise tax per liter of beverages containing about 40% alcohol should be 260 RSD, instead of the current 134.6 RSD for fruit brandy, or 343.7 RSD for grain brandy. In addition, the amount of excise duty on strong alcoholic beverages for the so-called "small distilleries" could be prescribed as at least 50% of excise duty, or about 130 RSD per liter of alcohol.
3. **to introduce the category of "small producers" by the Law on Strong Alcoholic Beverages.** The amendment to the law should set a limit on the production and sale of alcoholic beverages, below which a natural or legal person could be classified as a "small producer".



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11. <https://www.paragraf.rs/propisi/zakon-o-jakim-alkoholnim-picima.html>