8

Excises

Ben J.M. Terra

> Excise—A hateful tax levied upon commodities, and adjudged not by the common judges of property, but wretches hired by those to whom excise is paid.
>
> —*Samuel Johnson*

I. Introduction

A. Nature of Excise Taxes

According to the late H.C. Simons, an American professor of public finance, the only cogent defense of excises rests on Calvinist premises. Calvinism, according to Simons, divides mankind into the elect and those who are obviously damned for their next life. The elect noticed that the damned consumed large quantities of certain goods and liquors, providing an obvious reason for the elect to tax these goods and liquors. This taxation would properly prepare the damned for their fate while at the same time carrying what would otherwise be tax burdens for the elect. This explanation of excises, definitely not meant as a joke, can easily be refuted. The more southward one travels in Europe the less the Calvinist influence, but the larger the number of different specific taxes.[1]

[1]It is precisely this distinction among the member states of the European Union (EU) in relying on various excises that made a unanimous decision on harmonization so difficult. The instruction of art. 99 of the EEC Treaty to the Commission to examine, among other issues, how excise duties can be harmonized only resulted in a few directives on tobacco and many proposals for directives that have not been adopted. It took until the completion of the internal market (1992) to harmonize the excises within the EU, although it is admitted that it is based on a new concept of "general and flexible harmonization" or on the "least common denominator." *See* E. Stubbe, *Die Harmonisierung der besonderen Verbrauchssteuern in der Europäischen Gemeinschaft*, Zeitschrift für Zölle und Verbrauchssteuern 170 (1993).

The harmonization of the excises in the EU is based on three sets of rules: (1) one directive (92/12 of March 23, 1992, O.J. (L 76) 1, as amended) on the general arrangements for products subject to excise duty and the holding, movement, and monitoring of such products, known as the "horizontal directive," (2) three directives on the harmonization of the structures of the excises that are the subject of the general arrangements procedure, namely, mineral oils, alcohol and alcoholic beverages, and manufactured tobacco, and (3) four directives on the approximation of rates of duties applicable to the above-mentioned excises, referred to as the "Directives on rates." *See* Ben Terra & Peter Wattel, European Tax Law 145–46 (1993).

Value-added tax, as discussed in chapter 6, refers to a technique (the so-called credit of input tax based on the invoice method) of levying a turnover tax. The VAT is a general indirect tax on consumption. The general character of this tax requires that locally produced goods and imported goods be treated equally; thus, imports are equally subject to VAT.[2] The levy of VAT on importation of goods is not discriminatory (like import duties) but compensatory. VAT on importation is characterized by its *equivalent nature*. The indirect character of VAT is exemplified by the fact that VAT is remitted on exportation in accordance with the rules of the General Agreement on Tariffs and Trade (GATT). VAT is a general, as opposed to specific, tax on consumption. Excises are examples of specific taxes. The levy of excises on importation is equally characterized by its equivalent nature. Excises on importation are meant to compensate for the internal levy on identical or similar goods. The indirect character of excises is exemplified by the fact that excises are remitted on exportation in accordance with the GATT rules.[3]

Although sometimes applied to services, excise taxes are generally imposed on the sale of specifically listed goods. Import duties and VAT are based on the value of the goods concerned (ad valorem duties). Although a strong argument can be made in favor of charging excises on an ad valorem basis,[4] many excises are levied as specific duties; that is, they are imposed at a specific monetary charge per unit sold, for example, based on weight, quantity, or alcohol content, or in combination with ad valorem duties.

Because of their generally simple nature, excise tax statutes normally lack the technical complexity and need for great detail associated with, for example, income tax laws. Although excise taxes are administered by fiscal authorities, both their administration and their special problems are similar to those encountered in customs duties. The computation of the amount of tax owed is relatively simple. Typical problems involve classification and definition of goods subject to excise, questions about who is responsible for collecting the tax and when it is to be collected, how to treat leasing, and technical issues such as withdrawal from warehouse, how to deal with exempt purchasers or uses, how to handle returns, lost or damaged merchandise, exporter's refunds and issues related to effective dates, such as how to treat floor stocks at the time of the imposition, termination, or change in rate of a tax. An excise tax statute should provide as much guidance as possible with respect to these issues.

B. Terminology

The term "excise" has a historic connotation. As early as the Han dynasty (207 B.C.–A.D. 220) excises were levied on tea, liquor, fish, and reeds used for

[2]Since January 1, 1993, the taxable event of importation between member states of the EU no longer occurs.

[3]*See* discussion *infra* sec. I(C).

[4]*See infra* sec. I(D).

fuel and thatching.[5] Cnossen refers to a study according to which the word excise derives from the Middle Dutch *exijs*, which might be a modification of the old French *assise* meaning session, settlement, or assessment.[6] We submit that the word excise could also be derived from the Latin *excisere*: to carve, to cut out, referring to the carvings on a stick intended for measuring quantities of beer or liquor.

More important is the definition of excises. According to Cnossen, "broadly speaking, the distinguishing features of excise taxation are selectivity in coverage, discrimination in intent, and some form of quantitative measurement in determining the tax liability."[7] Cnossen's classification of excise systems is still useful:

> 1. *Limited excise systems* comprise at least the traditional excise goods: tobacco products, alcoholic beverages, and petroleum products as well as motor vehicles and various forms of entertainment. . . . However, all in all, the coverage of limited systems would not exceed 10–15 commodity groups, with closely related products (various petroleum products, or sugar and saccharine, for instance) being treated as one excisable item. 2. *Intermediate excise systems* consist of between 15 and 30 commodity groups. . . . 3. *Extended excise systems* comprise more than 30 commodity groups spanning almost the whole range of production activities in a particular country.[8]

This chapter is restricted to limited excise systems in the belief that it is preferable to limit excises to a few principal groups of products and to remove vexatious minor excises and regressive excises in favor of a general tax on consumption. A further restriction is that we will focus on the traditional excise goods, such as tobacco products, alcoholic beverages, and petroleum products. Under the subject "others," we discuss some design issues of other excises in general terms.

C. Territoriality

As with the VAT,[9] the two conflicting principles on which the territorial scope of excises can be based are the origin principle and the destination principle. Most countries have adopted the latter for both VAT and excises, resulting in so-called border tax adjustments. The issue of border tax adjustments reemerges with a certain regularity in discussions on world trade. Border tax adjustment refers to the treatment of taxes under the rules of the GATT, now

[5]*See* Sijbren Cnossen, Excise Systems 1 (1977).

[6]*See id.* at 160, ch. 1, n.1.

[7]*Id.* at 7. Certain narrowly based taxes are sometimes called excise taxes, even though they do not fall within traditional categories of excises. *See, e.g.*, USA IRC §§ 4940–48 (excise taxes imposed on tax-exempt organizations). These are beyond the scope of this chapter.

[8]Cnossen, *supra* note 5, at 13.

[9]*See supra* ch. 6.

embedded in the World Trade Organization (WTO). The provisions on the international treatment of internal taxes in the GATT are interpreted to mean that border tax adjustments are permitted for indirect taxes, but not for direct taxes.

Border tax adjustments are a surcharge on imports, which must not exceed the internal taxes or other internal charges levied on similar domestic products, and a refund of duties and taxes upon exportation in amounts not exceeding those that have accrued. Taxation on importation and remission of taxes or duties on exportation are also called "tax frontiers," "tax boundaries," or "tax barriers."

The application of border tax adjustments is voluntary, rather than mandatory. The Contracting Parties to the GATT may impose compensatory taxes on imports and may exempt, or remit, taxes on exports, but they are not required to do so.

In the 1960s, a proposal was made to modify the GATT rules by eliminating border tax adjustments altogether, under the assumption that adjustments result in unfavorable trade patterns. During the Tokyo Round (one of the major multilateral negotiations held under auspices of the GATT), the proposal to eliminate border tax adjustments was, however, rejected and the existing practices confirmed.

The concepts regarding subsidies and border tax adjustments are embodied in the GATT. However, there is no unified GATT provision dealing exclusively with border taxes. Besides article VI, dealing with antidumping and countervailing duties, the only GATT articles concerning border tax adjustments are article II on tariff concessions, article III on internal taxation on imports, and article XVI, adopted in 1955, on the border tax adjustments on exports.

Articles II and III govern border tax adjustments on imports. Article II prohibits import charges other than those provided in the GATT, but excludes from this prohibition the levy on imported products of "a charge equivalent to an internal tax imposed, consistently with Article III in respect of like domestic products." Article III provides that internal taxes shall not be applied to protect domestic production. Discrimination is also forbidden: imported products shall "not be subject, directly or indirectly, to internal taxes or internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products."[10]

D. Method of Charging

The two main methods of charging are specific rates, based on quantity, and ad valorem rates, based on value. Which is better is controversial, and may differ depending on the product and the details of implementation of the

[10]General Agreement on Tariffs and Trade, art. III(2).

charging method. Conventional policy generally advocates that all excises be levied on an ad valorem basis rather than on a specific basis, because this protects the base of the tax from inflation. This is particularly important in countries with high rates of inflation. "Nevertheless, the real value of revenues may be maintained under a specific-rate excise tax if there are regular adjustments of the rate to reflect inflation."[11] It may be argued that with periodic adjustments for inflation, revenues under a specific-rate system will still lag during the periods between adjustments[12] but that the lag can be mitigated by introducing "automatic" adjustments of the specific rates when inflation reaches a certain threshold. Without such automatic adjustment, there could be political pressures to cancel or postpone increases, based on the argument that the tax increases will just make inflation worse.[13]

"An additional reason for [advocating] ad valorem rates is that they are fairer for the less prosperous, whose economy brands under a specific rate would bear the same tax as the luxury brands of the affluent."[14] This argument is most relevant for excises that are imposed on luxury goods for the purpose of introducing progressivity to the system. For goods such as alcoholic beverages, specific rates, for example, based on the unit of alcoholic content (or a combination of specific and ad valorem rates) make more sense given the purpose of the tax.[15] The most compelling reason for recommending specific rates is based on the difficulties of determining the taxable value related to the stage of production or distribution where excise should be levied. The problem can be dealt with under a system of ad valorem rates by providing a presumptive minimum valuation for certain products.

There are two distinct types of excise taxes. Manufacturer's excise taxes are imposed on the producer or importer of a taxable good and included in the price paid for that good by the ultimate purchaser. Retail excise taxes, in contrast, are imposed at the point of sale to the ultimate purchaser. Although recent work in the applied theory of optimal taxation suggests that indirect taxes, including excises, should be imposed as close to the final sale as possible because of the potential for excises to have unexpected distributional and efficiency effects when imposed on intermediate goods,[16] the small number of

[11]William J. McCarten & Janet Stotsky, *Excise Taxes*, *in* Tax Policy Handbook 100, 102 (Parthasarathi Shome ed., 1995).

[12]*See* Ward M. Hussey & Donald C. Lubick, Basic World Tax Code and Commentary: 1996 Edition 306 (1995).

[13]*See id.*

[14]*Id.*

[15]*See* Leif Mutén, *Some Comments on the Basic World Tax Code*, 7 Tax Notes 179, 184 (1993). A study conducted for the European Commission, reported in the Commission Report on the rates of duty laid down in the various rates directives on the approximation of excises (July 1995), shows that "excise duty affects consumption of the different alcoholic beverages through their sensitivity of their specific price" and that "excise duty can also affect the market share of different categories of alcoholic beverage because of competition through prices."

[16]*See* McCarten & Stotsky, *supra* note 11.

taxpayers affected by a tax imposed at the manufacturer's level may involve an administrative advantage that outweighs the suggested advantages of levying as close to the final sale as possible. Because of problems of control, most excises in developing and transition countries take the form of manufacturer's taxes. However, under an ad valorem tax, the taxable value is presumably the price actually paid or payable. At the manufacturer's level, certain costs such as transportation, storage, or even part of the profit can be transferred to the next stage. This type of circumvention requires complex legislation dealing with such matters as what should be included in the value, and special rules for transactions with related parties. Thus, specific taxes may be better than ad valorem rates if tax administrative capacities are limited so that undervaluation of domestic goods or imports is a common problem. Under a specific-rate excise tax, disputes over valuation do not arise. The choice of manufacturer's taxes requires a more frequent use of specific taxes. Furthermore, ad valorem taxes at the manufacturer's level would be either excessive or related to a final consumption price that is not always known, unless it is fixed, as may be the case with tobacco.[17] This chapter will therefore assume the manufacturer's tax and a frequent use of specific taxes in the general discussion without, however, recommending what approach should be taken in specific cases.

E. Principle of Nondiscrimination

The GATT practices as discussed in section C are based on the principle of nondiscrimination between domestically produced and imported products. If an excise does not apply equally to both domestic production and imports, then, to maintain a given degree of protection, a given excise tax rate change will require a corresponding change in the tax rate on imports. In India, for example, changes are made simultaneously in excises and in levies on imports. In Latin America and the EU, excises typically apply to both imports and domestically produced commodities. Within the EU, the principle of nondiscrimination requires an identical excise on locally produced products and products produced in other member states. The identical treatment applies not only to identical goods but also to similar goods; as applied to the latter, this principle has resulted in an extensive body of case law of the European Court of Justice.

II. General Design Issues

It is advisable to limit excises to a few principal groups of products and to remove vexatious minor excises and regressive excises in favor of a general tax on consumption. In contrast to a general tax on consumption, for which a single set of rules suffices, each distinct principal group of excised products re-

[17] *See* discussion *infra* sec. III(C).

quires specific legislation with specific design issues.[18] It is nonetheless advisable to lay down in a single statute the arrangements common to all products subject to excise duties and to set out in specific subdivisions or separate laws the particular provisions relating to the structures and rates of duty on the distinguished products subject to excise duty. The statute should contain at least the following items: general provisions, taxable event, movement of goods, payment of the duty, reimbursement, and exemptions. The most important design issues are discussed below.

In this discussion, we draw heavily on the EU directive in this area, known as the horizontal directive.[19] This directive sets forth principles that member states must follow in drafting their excise tax laws. The discussion is not, however, a commentary on the horizontal directive, nor do we analyze the many provisions that relate to the treatment of transactions within the EU. Rather, we view the directive as setting forth useful guidelines and definitions that countries designing excise tax laws should take into account, even though not all the aspects of the directive will be relevant outside the EU.

A. General Provisions

A statute laying down provisions common to all products subject to excise duties usually starts with the *scope* of the statute itself. Particular provisions relating to the structures and rates of duty on the distinguished products can be set out separately.

The general provisions should define the *territorial application* of excises, in general, the territory of the country. For constitutional or other reasons (remoteness, autonomy, degree of development, etc.), certain parts of the territory may have to be excluded. It is highly recommended that the territorial scope of the tax be defined in the same manner as for VAT, so that there is a uniformity of application of the two taxes.

The *products subject to excise duties* should be mentioned. For example, "this statute applies to mineral oils, alcohol and alcoholic beverages, manufactured tobacco, and others as defined in articles [-], hereinafter referred to as excise products."[20] Here, or in the provisions containing rules for specific products, the items subject to tax will have to be defined.

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[18] *See infra* sec. III.

[19] *See supra* note 1. We also draw on Terra & Wattel, *supra* note 1, at ch. 7.

[20] Although it is advisable to limit excises to a few principal groups of products, the division of fiscal powers within a state, [con]federation, or economic union may allow for separate local excises. It is recommended that, in addition to VAT, the above-mentioned products be made subject to other (specific) indirect taxes only if determination of the tax base, the calculation, chargeability, and other aspects comply with the tax rules applicable to excise duties, based on the horizontal statute. If levels other than the central government retain the right to maintain or even introduce taxes on other products and services (provided that these taxes cannot be characterized as turnover taxes, i.e., a VAT), obviously it should be provided that these taxes may not give rise to border-crossing formalities in the trade within the state, [con]federation, or economic union.

It is recommended that the *definition* of the items subject to tax refer to the customs tariff, based on the harmonized system (HS),[21] a single harmonized method of classifying goods for customs, statistical, and trade purposes, that has been adopted by all the major trading nations, including the United States, the EU, and Japan. The advantage of using this approach is, in addition to the comparability of trade statistics, the use of a uniform "language" in international trade based on a systematic classification that avoids linguistic differences. In light of the destination principle,[22] the classification based on the HS may prevent disputes.

Finally, the general rules should provide which *definitions*, such as those for tax warehouse, suspension arrangement, and authorized warehousekeeper, apply for the purposes of the statute.[23] The definitions that may be required are discussed in the sections below, under the subject to which they pertain.

B. Taxable Event and Chargeability

The statute should provide for the taxable event, namely, that excise products are subject to excise duty at the time of their *production* within, or *importation* into, the territory of the country (as defined under the general provisions). A distinction should be made between the taxable event and the chargeability of the tax. "Taxable event" means the occurrence by virtue of which the legal conditions necessary for the tax to become chargeable are fulfilled, that is, production or importation. The tax becomes chargeable when the tax authority becomes entitled under the law at a given moment to claim the tax from a person liable to pay.[24]

Although production techniques may be different depending on the product subject to excise duty, the definition of the chargeability (see below) does not in principle require a definition of production. If for certain prod-

[21]*See* Customs Cooperation Council, The Harmonized Commodity Description and Coding System (1984).

[22]*See supra* sec. I(C).

[23]The following definitions may apply:

> (a) authorized warehousekeeper: a natural or legal person authorized by the competent authorities . . . to produce, process, hold, receive, and dispatch products subject to excise duty in the course of his business, excise duty being suspended under tax-warehousing arrangement;
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> (b) tax warehouse: a place where goods subject to excise duty are produced, processed, held, received, or dispatched under duty-suspension arrangements by an authorized warehousekeeper in the course of his business, subject to certain conditions laid down by the competent authorities . . . ; [and]
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> (c) suspension arrangement: a tax arrangement applied to the production, processing, holding, and movement of products, excise duty being suspended.

Council Directive 92/12, *supra* note 1, art. 4.

[24]Notwithstanding that the time of payment may be deferred, for example, upon importation based on monthly payments.

ucts a definition is deemed to be necessary, it is better covered in the specific provisions dealing with the structure and rates of duty on the product in question.

Importation is to be defined as the entry of a product subject to excise duty into the territory of the country. The entry from territories excluded from the territory of the country for excise purposes under the general provisions also gives rise to the taxable event of importation.[25] This all-encompassing definition needs some refinement based on the customs legislation in force. Generally, customs legislation provides for a variety of approved treatments or uses of goods, such as placing goods in a free zone or free warehouse, re-exporting the goods from the territory to a third territory, or even the destruction of goods or their abandonment to the state. If the goods do not undergo such treatment or use, they must be declared to customs, in which declaration, depending on the national customs legislation, a variety of procedures are again possible, such as transit, customs warehousing, inward processing, processing under customs control, or release for free circulation.[26] The definition of the taxable event should make clear when the excise duty is deemed to be suspended and when the importation is deemed to take place.

Notwithstanding a clear-cut definition of the taxable event (i.e., production or importation), the occurrence of the event should not necessarily result in chargeability of the tax. The excise duty becomes chargeable at the time of *release for consumption* or when shortages are recorded (the meaning of these terms is discussed below).[27] The conditions of chargeability and the rate of excise duty to be adopted should be those in force on the date on which duty becomes chargeable at the place where release for consumption takes place or shortages are recorded. This requires some further explanation.

From both the state's and a producer's point of view, an immediate collection of duties in all circumstances would have a perverse effect. Produced goods may be exported, thus not requiring collection of tax or, if collected, resulting in refunds. For a product like wine, which may require time (to ripen) between production and consumption, taxation at the moment of production would result in an excessive burden. Therefore, produced or imported excise products may be held in a so-called tax warehouse without excise duty becoming chargeable (or may be placed under a customs-approved treatment or use).[28] This is called the

[25]*See supra* sec. II(A). An additional complication could be that the excluded territories form part of the customs territory of the country. Special mechanisms have to be created in order to monitor the entry from the excluded territory into the excise (and VAT) territory without interference by customs officials.

[26]*See* B.J.M. Terra, Community Customs Law (1995).

[27]*See* Council Directive 92/12, *supra* note 1, art. 6.

[28]*See supra* note 25. Therefore, the statute should stipulate that the production, processing, and holding of products subject to excise duty, where the duty has not been paid, are required to take place in a tax warehouse.

"suspension arrangement." Any departure from this arrangement, that is, a release for consumption, results in chargeability of the duty.[29]

Release for consumption may be defined as

- any departure, including irregular departure (i.e., without fulfilling the required formalities), from a suspension arrangement;
- any manufacture, including irregular manufacture,[30] of excise products outside a suspension arrangement; or
- any importation, including irregular importation, where excise products have not been placed under a suspension arrangement.[31]

It should be borne in mind that the taxation of excise products is based on the destination principle;[32] hence, the suspension arrangement makes it possible to postpone taxation until the products reach the country of destination.[33]

As mentioned above, the excise duty becomes chargeable at the time of release for consumption or when shortages are recorded. With regard to *shortages*, the statute should provide that authorized warehousekeepers shall be exempt from duty for losses occurring under suspension arrangements that are attributable to fortuitous events or force majeure (but not theft) and established by the competent authorities. They shall also be exempt, under suspension arrangements, from losses inherent to the nature of the products during

[29]Excise products coming from or going to third countries or territories where the excises are not levied can be placed under a customs procedure, for example, exportation. In these circumstances, with the exception of the procedure of release for free circulation or consumption, the excise duties on the goods are deemed to be suspended. When goods leave the customs procedure, they are deemed to have been released for consumption.

[30]As mentioned in note 28, it should be required that production, processing, and holding of products subject to excise duty, where the latter has not been paid, take place in a tax warehouse. The provision that manufacturing outside a suspension regime is treated as release for consumption triggers the taxable event and makes the tax become chargeable at the moment of manufacturing.

[31]Council Directive 92/12, *supra* note 1, art. 6.

[32]*See supra* sec. I(C).

[33]Only with regard to products acquired by private individuals for their own use and transported by them does the principle apply that excise duty is charged in the state in which the products are acquired. Sometimes, the acquisition is exempt and an exemption may be granted up to a threshold upon importation. Between the member states of the EU with regard to products acquired by private individuals for their own use and transported by them excise duty is charged in the state in which the products are acquired. Of course "own use" has its limitations. The horizontal directive specifies that excise duty becomes chargeable when products released for consumption in a member state are held for commercial purposes in another member state. Council Directive 92/12, *supra* note 1, art. 9(1). The directive provides for so-called minimum guide levels, below which quantities are not treated as held for commercial purposes, for example 800 cigarettes, 90 liters of wine, including 60 liters of sparkling wines. *Id.* art. 9(2). For mineral oil, the guide level is based on the form of transportation. Atypical transport, that is, other than in tanks of vehicles or in appropriate reserve fuel canisters, results in taxation in the member state of consumption. *Id.* art. 9(3).

production and processing, storage, and transport. The statute should lay down the conditions under which these exemptions are granted.

The statute should specify that the duty on shortages other than the losses referred to above must be levied on the basis of the rates applicable at the time the losses, duly established by the competent authorities, occurred or, if necessary, at the time the shortage was recorded. Furthermore, the statute should provide that the production, processing, and holding of products subject to excise duty must take place in a tax warehouse.

With regard to the *authorization* to operate a tax warehouse and the obligations of an authorized warehousekeeper, the statute should provide that the opening and operation of tax warehouses is subject to authorization from the competent authorities and that an authorized warehousekeeper shall be required to

- provide a guarantee to cover movement and, if necessary, to cover production, processing, and holding;
- keep, for each warehouse, accounts of stock and product movements;
- produce the products whenever so required; and
- consent to all monitoring and stock checks.[34]

C. Movement of Goods

Any departure (including irregular departure, i.e., without fulfilling the required formalities) from a suspension arrangement results in the chargeability of the excise duty. This is not always a desired result, because goods may have to move between places of production (or in general tax warehouses) or to a place or destination that will not result in the chargeability of the duty (e.g., exportation). The statute should prescribe that the movement of excise products under suspension arrangements must take place between tax warehouses or a tax warehouse and the customs office from where the products leave the territory. All such movements must be covered by the "accompanying document" (administrative or commercial). Under certain circumstances, even the movement of excise products already released for consumption (i.e., goods not, or no longer, covered by the suspension arrangements) may be covered by an accompanying document. The consignee of the movement of excise products under suspension arrangements may only be an authorized warehousekeeper. The authorized warehousekeeper[35] must return a copy of the accompanying administrative document, duly annotated, to the consignor of discharge, that is, to the authorized warehousekeeper who dispatched the goods. In this case, the authorized warehousekeeper is discharged from the duty-suspension arrangement.

[34]Council Directive 92/12, *supra* note 1, art. 13.

[35]Or the customs office where the products leave the territory.

The products are subject to excise duty upon arrival at the consignee unless they have been placed under a suspension arrangement or have been exported.

With regard to the provision *from whom the duty is due* when goods are moved between authorized warehousekeepers, a broad provision is suggested; for example, depending on all the circumstances, the duty shall be due from the person making the delivery or holding the products intended for delivery or from the person receiving the products for use.[36]

Notwithstanding the possible use of computerized procedures, all products subject to excise duty moving under duty-suspension arrangements must be accompanied by a document drawn up by the consignor. This document may be either an administrative document or a commercial document. To identify the goods and conduct checks, the packages should be numbered and the products described using the document referred to above. The consignor should seal each container when the authorities recognize the means of transport as suitable for sealing; otherwise, the consignor should seal the packages. Where an irregularity or offense has been committed in the course of a movement involving the chargeability of excise duty, the excise duty should be collected from the natural or legal person who guaranteed payment of the excise duties, without prejudice to the bringing of criminal proceedings.

D. Payment of the Duty

As mentioned above in cases of movement of goods, the duty is due from the person making the delivery, the person holding the products intended for delivery, or the person receiving the products. The law should also specify who must pay the excise duty when it becomes chargeable at the time of release for consumption or when shortages are recorded. However, authorized warehousekeepers are exempt from losses occurring under suspension arrangements that are attributable to fortuitous events, force majeure, and losses inherent to the nature of the products during production, processing, storage, and transport.[37]

As mentioned earlier, the movement of excise products under suspension arrangements must be covered by an accompanying document drawn up by the authorized warehousekeeper, who must provide a guarantee. A guarantee that is jointly and severally binding on the warehousekeeper and the transporter may also be required. If the copy of the accompanying document to be returned to the consignor does not reach him or her, the consignor is not dis-

[36] *See, e.g.*, Council Directive 92/12, *supra* note 1, art. 7(3). Or from a body governed by public law. *Id.*

[37] *Id.* art. 14.

charged from liability for the duty. The excise duty becomes due from the person(s) who guaranteed payment.[38]

E. Reimbursement

In appropriate cases, products subject to excise duty that have been released for consumption may, at the request of a trader in the course of his or her business, be eligible for reimbursement of excise duty by the tax authorities when the products are not intended for consumption in the state.[39]

In applying this provision, before the goods are dispatched, the consignor must request reimbursement from the competent authorities of the state and provide proof that the excise duty has been paid.

F. Exemptions

Products subject to excise duty should be exempted from payment of excise duty where they are intended

- for delivery in the context of diplomatic or consular relations;
- for international organizations recognized as such by the public authorities, . . . and by members of such organizations, within the limits and under the conditions laid down by the international conventions establishing such organizations or by headquarters agreements; . . .
- for consumption under an agreement concluded with other countries or international organizations provided that such an agreement is allowed or authorized with regard to exemption from VAT.[40]

"Eligibility for exemption may be granted in accordance with a procedure for reimbursing excise duties."[41]

States may exempt products supplied by tax-free shops that are carried away in the personal luggage of travelers leaving the country by air or by sea.[42]

Products supplied on board an aircraft or ship during the international passenger service are to be treated in the same way as products supplied by tax-free shops.

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[38]"States may require that products released for consumption in their territory carry tax markings or national identification marks used for fiscal purposes." *Id.* art. 21(1). Any state that requires the use of tax marking or national identification marks as set out above is required to make them available to authorized warehousekeepers of other states. *Id.* art. 21(2). However, each state may require that fiscal marks be made available to a tax representative authorized by the tax authority of that state. *Id.* Without prejudice to any provisions, they may, to ensure that this provision is implemented properly and to prevent fraud, evasion, or abuse, specify that states should ensure that these marks or markings do not hinder the movement of products subject to excise duty. *See id.*

[39]*See id.* art. 22(1).

[40]*Id.* art. 23(1). Presumably the reference to "members" of international organizations is to officials of such organizations, members usually being countries.

[41]*Id.*

[42]*See id.* art. 28(1).

III. Issues in Designing Specific Taxes

A. Mineral Oils

As mentioned in the introduction, one of the typical problems in drafting an excise statute is the classification and definition of goods subject to excise. In order to cover both national descriptions and the descriptions used internationally, the special provisions on the structure of excise duties on mineral oils should provide for a definition of (types of) mineral oil, referring to the codes of the customs tariff, based on the HS.[43] To avoid any form of substitution for those mineral oils for which no level of duty is specified, the statute should stipulate that mineral oil will be subject to excise duty if intended for use, offered for sale, or used as heating fuel or motor fuel. Also, any product not listed as a "mineral oil" must be taxed at the rate for the equivalent mineral oil when offered for sale or used as motor fuel or for heating purposes.

Notwithstanding the general preference for ad valorem duties, mineral oils are often subjected to specific duties. If consumer prices are not fixed, ad valorem prices at the production level could easily result in a shift of profit to later stages. Ad valorem duties levied at the retail level would result in too large a number of taxpayers. The special provisions could, therefore, provide that mineral oils be made subject to a specific duty calculated per 1,000 liters of product, for example, at a temperature of 15° Celsius; heavy fuels should be calculated per 1,000 kilograms.

In addition to the chargeable event, as defined in the horizontal statute, the specific provisions on mineral oils should specify that excise duty becomes due when (certain) products are used for such purposes as heating oil or motor fuel, which products are made subject to excise duty as mentioned above. Furthermore, it should be provided that excise duty becomes due when the conditions for exempt use or use at a reduced rate are no longer fulfilled. With regard to these exemptions or reduced rates, the law should provide for a list of activities, for example, mineral oils supplied for use as fuel for the purpose of air travel other than private pleasure flying, mineral oils used for the process of producing electricity, and so on. Care should be taken to minimize exemptions and to minimize the situations where an exempt product could be converted to a nonexempt use.

The statute must prescribe the rates that apply. As an example, Directive 92/82/EEC provides for the following rates[44] (calculated in European currency units (ECUs) per 1,000 liters of product at a temperature of 15° Celsius; heavy fuels are calculated per 1,000 kilograms): ECU 337 on leaded petrol, ECU 287

[43] *See supra* note 21.

[44] In contrast to the system as envisaged by the Commission with regard to the approximation of excise duties, the directive does not provide for a final rate that all member states must eventually reach. The directive merely prescribes minimum rates, which are applicable to only 7 of the 13 types of mineral oil mentioned in the structures directive.

on unleaded petrol, ECU 18 on heating gas oil, ECU 13 on heavy fuel, and ECU 100 on liquid petroleum gas and methane.[45]

B. Alcohol and Alcoholic Beverages

It seems self-evident that a modern excise on alcohol and alcoholic products should be based on the pure alcohol content of a product. History and tradition, however, make it virtually impossible to come to such a straightforward approach. Therefore, the special provisions on alcohol and alcoholic beverages may as well be built on the historic distinctions made between beer, wine, fermented beverages other than wine and beer, intermediate products, and ethyl alcohol. The special provisions on alcohol and alcoholic beverages are discussed below, based on this distinction.

To solve the problem of classification and definition, with regard to *beer*, the special provisions should provide that the object of taxation is beer covered by HS code 2203 or a mixture of beer with nonalcoholic drinks falling within HS code 2206, both with an alcohol strength more than 0.5 percent vol. The duty is based on the hectoliter/degrees Plato or hectoliter/degrees of actual alcoholic strength by volume. The rates should be fixed. As an example, Directive 92/84/EEC fixes the rate at ECU 0.748 per hectoliter/degree Plato or ECU 1.87 per hectoliter/degree alcohol of finished product.[46]

The statute may exempt from excise duty beer produced by a private individual, provided that the beer is consumed by the producer or by members of his or her family or guests and provided that no sale is involved. If sales are involved, consideration could be given to applying a threshold, set in the same manner as for the VAT, below which no excise duty is due.

With regard to *wine*,[47] a distinction could be made between "still wine" and "sparkling wine."[48] Still wine (falling within HS codes 2204 and 2205) has an alcoholic strength of between 1.2 and 15 percent vol or between 15 and 18 percent vol. In both cases, the alcohol must be entirely of fermented origin.[49] This distinction could be made to allow for a higher duty on wine that has a strength of between 15 percent and 18 percent vol. Sparkling wine has an al-

[45]Council Directive 92/82, arts. 3–7, O.J. (L 316) 19, 19–20.

[46]Council Directive 92/84 art. 6, 1992 O.J. (L 316) 29, 30.

[47]It may be considered to exempt small wine producers from the requirements of operating a tax warehouse and from the other requirements relating to movement and monitoring. *See supra* secs. II(B), (C). Where these small producers themselves move their products within the territory, they should be required to inform the relevant authorities and comply with the requirements for an accompanying document. "Small wine producers" could be understood to mean persons producing on average less than 1,000 hectoliters of wine a year. If such an exemption is introduced, the tax authorities should be informed by the consignee of wine deliveries received by means of the accompanying document referred to above.

[48]Council Directive 92/83 art. 8, 1992 O.J. (L 316) 21, 23.

[49]*Id.* art. 8(1).

coholic strength of between 1.2 percent and 15 percent vol and is mainly distinguished by the use of "mushroom stoppers."[50]

The excise duty should be fixed by reference to the number of hectoliters of finished product; in principle, the same duty should be applied to all still and sparkling wines, although it is not necessary that the duty on still and sparkling wines be the same.

An exemption for private production may be granted under the same conditions as for the production of beer.

Furthermore, the specific statute could make a distinction between "other still fermented beverages" and "other sparkling fermented beverages," referring to the relevant HS codes and actual alcohol strengths, the details of which are not discussed here.[51] The provisions for the establishment of the duty on these fermented beverages other than wine and beer are identical to those on wine. If this choice is made, the statute should provide that, for the application of the horizontal statute, references to wine are deemed to apply to the products referred to above.

Intermediate products are to be defined on a residual basis, that is, falling within HS codes 2204, 2205, and 2206 and having an actual alcoholic strength of between 1.2 percent and 22 percent vol, but not covered by the definition of beer, wine, or other fermented beverages.[52] The duty on intermediate products is also to be based on the number of hectoliters of finished products. Consideration could be given to applying a single reduced rate to intermediate products with a strength not exceeding 15 percent vol under certain conditions.[53]

Ethyl alcohol covers all products of HS codes 2204, 2205, and 2206 (see the products mentioned directly above) whose alcohol strength exceeds 22 percent vol, products whose alcohol strength exceeds 1.2 percent vol that fall within HS codes 2207 and 2208 (even when they form part of a product mentioned in other chapters of the HS), and potable spirits containing the above-mentioned products, whether in solution or not.[54] The excise duty may be fixed per hectoliter of pure alcohol at 20° Celsius.[55]

C. Tobacco

It is sufficient to provide an all-embracing definition of tobacco products, (as distinct from the other products, no reference need be made to the HS code), namely, cigarettes, cigars, cigarillos, smoking tobacco, snuff, and chew-

[50] *Id.* art. 8(2).
[51] *See id.* art. 12.
[52] *Id.* art. 17(1).
[53] *See id.* art. 18(3).
[54] *Id.* art. 20.
[55] *Id.* art. 21.

ing tobacco. Because rolls of tobacco for making one's own cigarettes must be taxed as cigarettes, smoking tobacco may be distinguished between "fine-cut tobacco for the rolling of cigarettes" and "other smoking tobacco." Cigarettes are defined as "(a) rolls of tobacco capable of being smoked as they are and which are not cigars or cigarillos . . . ; (b) rolls of tobacco which by simple non-industrial handling are inserted in cigarette-paper tubes; or (c) rolls of tobacco which by simple non-industrial handling are wrapped in cigarette paper."[56]

Furthermore, the statute should provide for exemptions or refunds, for example, for manufactured tobacco that is destroyed or reworked by the producer.[57] The following definition of a manufacturer could be given: a natural or legal person who converts tobacco into manufactured products prepared for retail sale. With regard to the rates, we present the EU example. A manufacturer is free to determine the maximum retail selling price for each of the products for each of the member states in which the products in question are to be released for consumption. Consumption taxes on cigarettes comprise

- a specific excise duty per unit of the product,
- a proportional excise duty calculated on the basis of the maximum retail selling price, and
- a VAT proportional to the selling price.[58]

The member states must apply an overall minimum excise duty (specific duty plus ad valorem duty excluding VAT) the incidence of which must be 57 percent of the retail selling price (inclusive of all taxes) for cigarettes of the price category most in demand.[59] With regard to the taxes on manufactured tobacco other than cigarettes, the member states are free to apply either an ad valorem duty calculated on the basis of the maximum retail selling price, or a specific duty by quantity, or a combination of both provided that the overall excise duty is at least equivalent to

- 5 percent of the retail selling price inclusive of all taxes, or ECU 7 per 1,000 items or per kilogram for cigars or cigarillos;
- 30 percent of the retail selling price inclusive of all taxes, or ECU 20 per kilogram for fine-cut smoking tobacco; or
- 20 percent of the retail selling price inclusive of all taxes, or ECU 15 per kilogram for other smoking tobaccos.[60]

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[56]Council Directive 79/32, art. 3(1), 1979 O.J. (L 10) 8, 9 as amended by Council Directive 92/78, art. 2, 1992 O.J. (L 316) 5, 6.

[57]Council Directive 72/464, art. 6a, 1972 O.J. (L 301) 1 as amended by Council Directive 92/78, art. 1, 1992 O.J. (L 316) 5, 6.

[58]Council Directive 92/79 art. 1(2), 1992 O.J. (L 316) 8, 8.

[59]*Id.* art. 2.

[60]Council Directive 92/80 art. 3(1), 1992 O.J. (L 316) 10, 10.

D. Others

As discussed earlier, it is advisable to limit excises to a few principal groups of products and to refrain from minor excises in favor of a general tax on consumption. Specific taxes, for example, on matches, lighters, playing cards, sugar, chocolate, nonalcoholic drinks, and carbonated drinks, should be relegated to the realm of curiosities. If any consideration is given to taxing other products, as mentioned in the sections above, or services, it is recommended that the advantages (revenue) be weighed against the disadvantages, such as discrimination, substitution, and administrative costs.

In various countries a tax on motor vehicles is applied, which for revenue and arguably[61] environmental purposes is treated differently from VAT, although legislation for the two is similar. Some specific design issues of a motor vehicle tax are the definition, for example, motorcars and other vehicles (HS code 8703), buses (code 8702), and trucks (code 8704); the taxable event, meaning the importation or, for domestically produced items, the sale by the producer (i.e., the person who manufactures, produces, assembles, or rebuilds a motor vehicle) or use of the vehicle by the producer before any sale, which is treated as a sale.

No excise is to be imposed on the transfer between authorized warehousekeepers and upon exportation.

Special attention should be given to exemptions that are advocated for social reasons or to avoid intermediate costs on export goods. (For this reason, HS code 8701—applying to tractors—is not included in the definition, nor is code 8705, which covers vehicles, such as mobile cranes, road sweepers, etc.) It is worth considering granting an exemption (based on a refund, or a deduction in the framework of the VAT legislation) for commercial and public vehicles (such as cabs, police cars, buses, and trucks). The fact that these motor vehicles are subject to the motor vehicle excise prevents purchases of such vehicles to be used, without or after adjustments, as passenger cars; the latter results under the definition of production in a taxable event.

Considering the extensive range of prices—not necessarily related to specific aspects, such as weight or engine capacity of the vehicles—and the resulting regressivity of specific taxes, an ad valorem tax is preferred. The tax for imported and locally produced vehicles should be based on the current average retail price in the principal markets of the country.[62] Special attention should be paid to the exemptions on importation, for example, for used household effects. Exempt importation of used motor vehicles, for both VAT and excise purposes, should be allowed only under restricted conditions.

[61] The Danish example shows that too high a tax on motor vehicles results in a polluting old national fleet of cars, requiring tax facilities to replace old cars for less-polluting new vehicles.

[62] The so-called accessories create a problem; if imported separately or sold separately, they escape taxation. HS code 8708 provides a good starting point for the articles to be subjected to the excise on motor vehicles.