

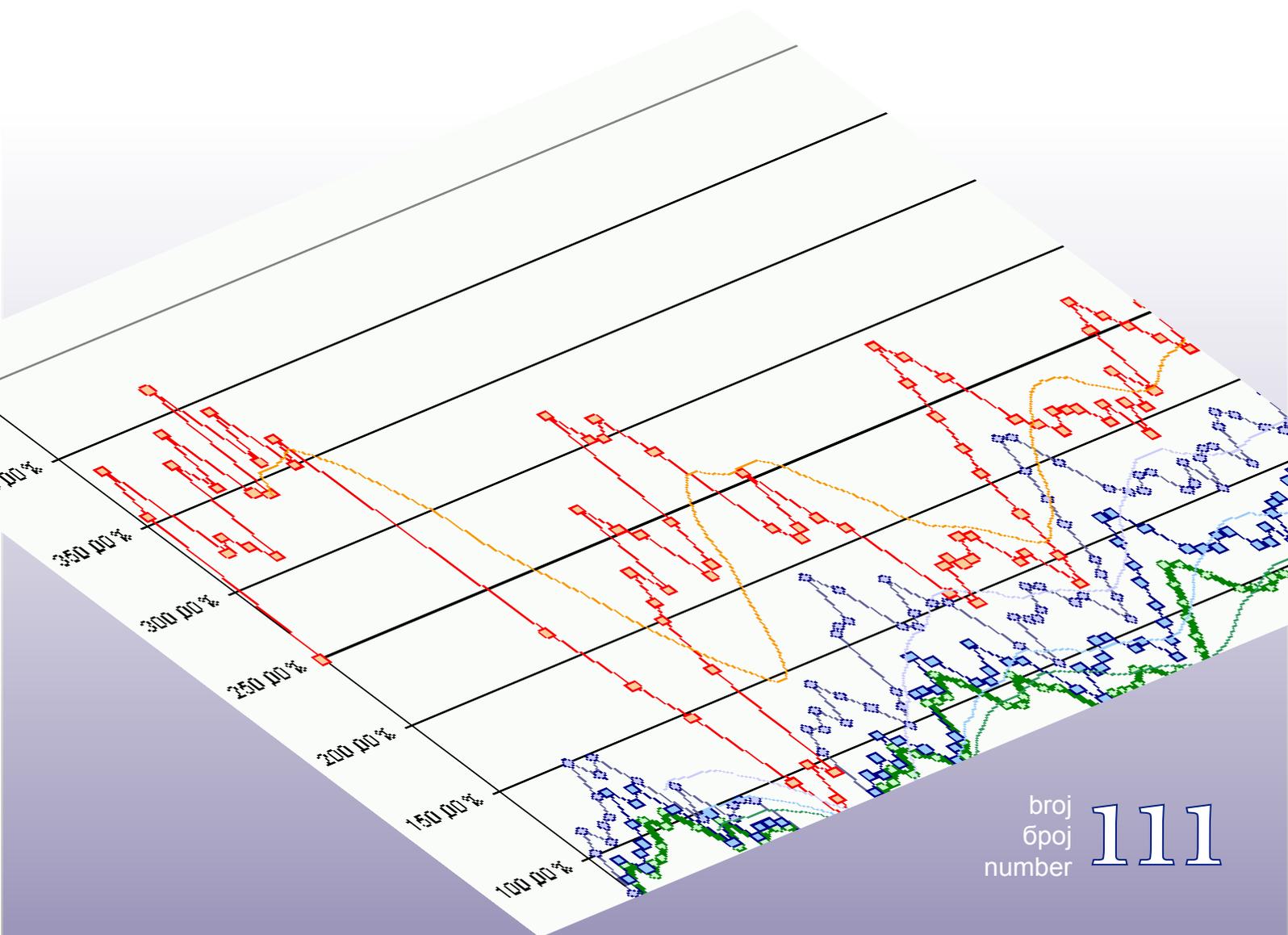
Bosna i Hercegovina
Odjeljenje za makroekonomsku analizu
Upravnog odbora Uprave za indirektno-
neizravno oporezivanje



Босна и Херцеговина
Одјељење за макроекономску анализу
Управног одбора Управе за indirektno-
опорезивање

Macroeconomic Unit of the Governing Board of the Indirect Tax Authority

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With this issue

According to the preliminary cash flow report on the Single Account, the ITA collected in September 566,4 million KM of gross revenues from indirect taxes or 46 million KM more than in the same month of 2013. Since refunds increased by 31,6% or by 27,9 million KM, the net collection amounted 450,1 million KM. That is 18 million KM more than in September 2013, or by 4,2% (Chart 1). At the level of January - September it was collected 4,575 billion KM of gross revenues. There has been a strong growth in refunds of 116,7 million KM or 15,8%. Finally, the net collection within the specified period increased by 92,1 million KM or by 2,5% compared to the same period in 2013, which means that the revised projections of the Unit from June 2014 have been exceeded.

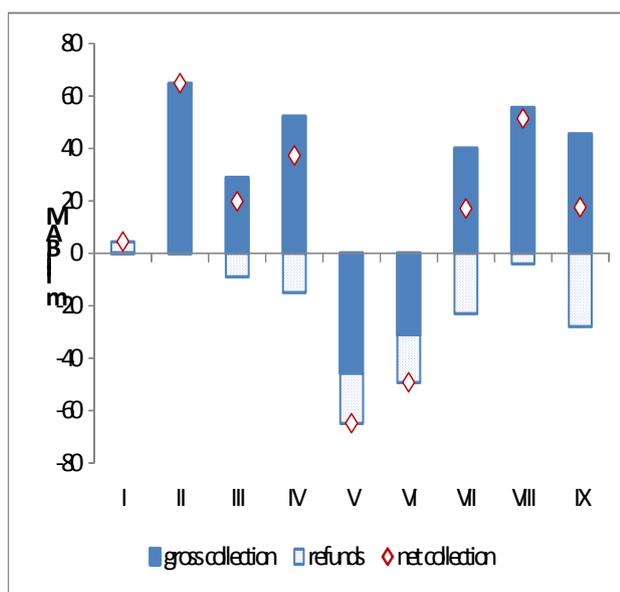


Chart 1

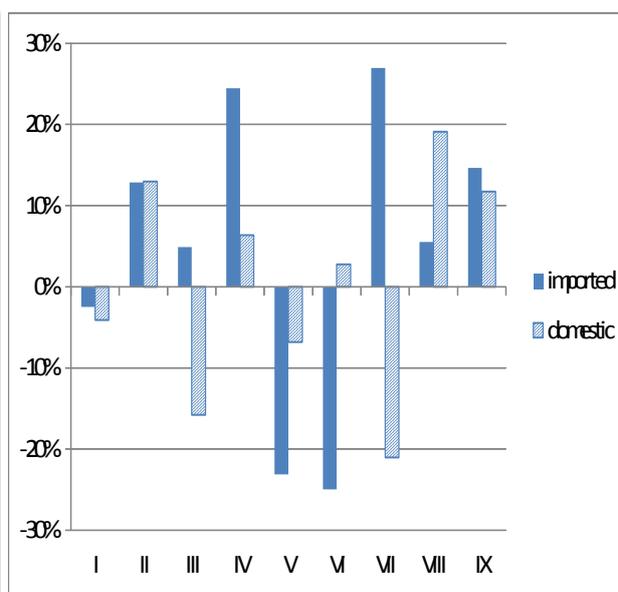


Chart 2

The main generators of revenue growth in September were excise taxes on tobacco, and excises and road fees on imports of oil derivatives. The response of the taxpayers and consumers to changes of the Law on Excise Duties brought the growth of excise duties on imported tobacco of 37,7% and of 11,8% on domestic. As the differentiated rates of excise duties on beer, which have been introduced by the changes of the Law on Excise Duties, apply only as of 1st September 2014, it is still too early for reliable conclusions about the effects. Based on the preliminary report it may be concluded that the first month of the application of differentiated rates brought a drop in revenues from excise taxes on domestic beer and a strong growth in revenues from excise taxes on imported beer, so the revenues from excise tax as a whole increased by 6% (Chart 2).

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Head of Unit

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Differentiated taxation of beer in B&H in the light of EU law and practice

(Author: Dinka Antić, PhD)

On the occasion of the establishment of a common market in 1993, the European Union allowed Member States to introduce differentiated rates of excise duties on beer for independent small breweries in order to allow the survival of the local brewing and retain jobs and population in rural areas, and to ensure balanced regional development within Member States. B&H has introduced differentiated rates of excise duties on beer by the amendments to the Law on Excise Duties in B&H as of 1 September. The introduction of differentiated rates of excise duties on beer raises questions about the possible economic and fiscal implications from the standpoint of taxpayers and fiscal authorities in B&H.

INTRODUCTION: TAX RELIEF IN THEORY AND PRACTICE

Modern tax systems include various tax benefits that are granted to certain categories of taxpayers. Tax benefits are also called tax reliefs. Tax relief is "a generic term to describe all methods used to reduce or refer burden of taxation without regard to the particular way it is accomplished"¹. Selectivity in taxation, which is in the basis of tax relief, in the field of business entity taxation may certain business entities put in a privileged position in the market in relation to competitors. If the scale of tax reliefs includes a broader range of goods and branches, then the market deviations are greater, since consumers are not directed towards the most efficient branches but towards branches that have favorable tax position. Distortion of the market situation sends the wrong signals to investors about the profitability and efficiency of certain branches which can hinder the efficiency of capital allocation. The negative consequence of tax relief is the emergence of unfair competition by favoring some economic agents and discriminating others in the market.

EU Member States, in order to ensure proper functioning of the single market in the EU, strictly limit all tax measures, including tax reliefs which endanger market mechanisms and certain groups of taxpayers put in a more favorable position. In 1997 the EU has adopted the Code of conduct for business taxation², that specifies the rules of taxation that are contrary to the principles of free movement of goods, services, capital and persons and to the principles of market competition within the EU. In 1998 it is published a detailed list of measures taken by the States that lead to harmful competition. The document, prepared by the OECD, offered a list of countermeasures that seek to oppose tax measures that threaten competition, threaten economic and financial decision-making and derogate the tax base (revenue) of the States³.

Due to negative implications developed EU countries and the OECD advocate the abolition or drastic reduction of tax reliefs. In tax systems only tax reliefs being introduced in order to stimulate research and development (R&D – *Research & Development*)⁴, preservation of the environment and reliefs for Start-Ups that encourage job creation and economic growth are retained. The global financial and economic crisis has once again put into focus the efficiency of tax systems.

¹ IBFD, "International Tax Glossary", 5th Edition, Amsterdam, 2005. p. 408.

² Council of European Union, Code of conduct for business taxation, 1 December 1997, OJ C 2, 6.1.1998.

³ More in: OECD, Harmful Tax Competition, An Emerging Global Issue, 1998.

⁴ OECD, "Tax Incentives for Research and Development: Trends and Issues", 2002.

The new tax strategy of the EU until 2020 and strategies of the IMF⁵ and OECD Member States⁶, supported by analyses from the study of Nobel Prize winner James Mirrlees⁷, are based on the expansion of the tax base and on the reduction of tax rates. The approach in designing the tax system that includes a broader tax base and lower rates would enable the realization of a number of advantages that are the characteristics of an ideal tax system. Systems with a broad base and low rates are more equitable because they do not include tax reliefs. The economic position of business entities in the market does not depend on tax preferences but on preferences of customers and the effectiveness of internal economy. Abolition of tax reliefs provided fair competition and full functioning of market mechanisms in the allocation of capital and other resources. Tax systems without reliefs are easier for tax authorities and taxpayers, requiring less time and resources in compliance with the tax laws, administration and tax control. By expanding the tax base, taxes encompass a wider range of taxpayers, which increases collected revenues from taxes. On the other hand, lower rates de-motivate taxpayers to seek ways to avoid paying taxes, because the "cost" of tax evasion can often exceed the amount of tax liability. The ultimate effect of the new direction of taxation is reducing the gray economy and increase in revenues with less "tax effort".

POLICY OF DIFFERENTIATED EXCISE DUTIES ON BEER IN THE EU

Legal framework of the EU

The minimum rates of excise duties for beer in the EU are laid down in 1984 and have not been changed so far, regardless of the increase in inflation. Depending on policy of Member States the minimum excise duty for Member States determining the excise duty according to the degree of alcohol is 1,87 EUR /hl/ % alcohol, and for Member States that use the Plato scale it is 0,748 EUR /hl/ ° Plato⁸.

EU Member States may apply reduced rates of excise duty, which may be differentiated depending on the annual production of breweries, to beer brewed by independent small breweries within the following limits:

- The reduced rates can be introduced only for breweries producing less than 200,000 hl of beer per year;
- The reduced rates shall not be less than 50% of the standard rate of excise duty of the Member State;
- The reduced rates may be introduced only for beer with alcohol content not exceeding 2,8% vol.⁹.

Member States may confine the application of this Article to products containing a mixture of beer with non-alcoholic drinks falling within CN code 2206. Under conditions which will ensure the proper application of exemptions, Member States may exempt from excise duty beer produced by private individuals and consumed by the producer, members of his family, provided that no sale is involved.

⁵ IMF World Economic and Financial Surveys, Fiscal Exit: From Strategy to Implementation, Fiscal Monitor, Washington, November 2010, pp. 73-84.

⁶ OECD, "OECD's Current Tax Agenda", June 2010., OECD, "Tax policy reform and fiscal consolidation", Tax Policy Brief , December 2010.

⁷ Mirrlees J., „Reforming the tax system for the 21st century – Tax by Design”, i "Dimensions of Tax Design", preliminary edition, Institute for Fiscal Studies, London, UK, November 2010.

⁸ Council Directive 92/84/EEC of 19 October 1992 on the approximation of the rates of excise duties on alcohol and alcoholic beverages, OJ L 316, 31.10.1992.

⁹ Council Directive 92/83/EEC of 19 October 1992 on the harmonization of the structures of excise duties on alcohol and alcoholic beverages (OJ L 316, 31.10.1992, p. 21)

In terms of the provisions of the Directive the term "independent small brewery" shall mean a brewery which is legally and economically independent of any other brewery which uses premises situated physically apart from those of any other brewery and does not operate under license. In case of cooperation between two or more small breweries and if their combined annual production does not exceed 200,000 hectoliters, such breweries may be treated as a single independent small brewery.

Member States are required to ensure equal application of reduced rates to beer delivered into their territory from independent small breweries situated in other Member State.

Compared to the general provisions of taxation of beer applied to all Member States only single derogation so far has been approved in favor of Portugal. In June 2008 the EU Council has approved to Portugal an increase in the maximum threshold for the introduction of a reduced rate of excise duty on 300,000 hl and only on beer produced and consumed exclusively in the region of Madeira¹⁰. This measure was introduced in order to maintain the domestic production of indigenous beer in Madeira. Reduction of excise duty should have to compensate the extra costs of domestic production of beer in dislocated, difficult for production and inaccessible areas of the island group in the region of Madeira. Deadline of the application of mentioned derogation was 31 December 2013, so there are currently no active derogations of uniform rules of differentiated taxation of beer.

Definition of „independent brewery“

The option of introducing differentiated rates of excise duty on beer is only available for independent breweries by the Directive 92/83/EEC. Directive lays down the basic criteria that must be met by the brewery in order to be included in the scheme of reduced rates of excise duty. The preamble to the Directive states that it is important to determine common definitions for all the excise products concerned in order to ensure the proper functioning of the EU internal market. In the case of taxation of independent small breweries it is necessary to adopt common solutions permitting Member States to apply the option of differentiated taxation of beer. However, it was also necessary to ensure that Member States which apply reduced rates of excise duty must not cause distortion of competition by national regulations within the internal market of the EU. Independence can be interpreted as physical, in terms of premises, legal, in terms of ownership, and economic independence, in terms of management and operations. Still, criteria listed in the Directive were not precise enough to take into account the different situations in which Member States found themselves when approving the application of reduced rates of excise duty. In some States the problem escalated to such an extent that disputes between fiscal authorities and breweries came to national courts and then to the European Court of Justice. Case C-83/08¹¹, related to Germany, attracted a lot of attention in the EU, so, in addition to the European Commission, governments of Greece and Portugal have also included in the debate.

Analysis¹² of the legal framework showed that brewers who want to join the scheme of reduced rates of excise duty should fulfill two conditions. The first is quantitative and refers to the annual volume of the production of beer which should be less than the maximum amount of 200,000 hl of beer prescribed by the Directive, while the other one is qualitative as it relates to the independence of the brewery from other breweries. Qualitative criteria are necessary in order to

¹⁰ Council Decision of 3 June 2008 authorizing Portugal to apply a reduced rate of excise duty on locally produced beer in the autonomous region of Madeira (2008/417/EC).

¹¹ Reference for a preliminary ruling from the Thüringer Finanzgericht (Germany), lodged on 25 February 2008 — Glückauf Brauerei GmbH v Hauptzollamt Erfurt, OJ C 128, 24.5.2008.

¹² Excerpt from the opinion of the attorney general of the Court.

avoid misuses where benefits from reduced rates by different legal arrangements between allegedly independent breweries *de facto* are achieved by large breweries. In comparison with the large breweries, that use economic and financial advantages of the company's size, small breweries are less effective due to higher costs of production, distribution and financing, that put them in a weaker competitive position in the market. In this regard, favorable excise taxation is considered to be a mechanism for creating equal opportunities for small breweries in the beer market. Reduced rates of excise duty are also introduced to small breweries in order to keep jobs and population in rural areas of Member States and to achieve equal regional development of the EU. Tax reliefs, if granted to big breweries, could, due to their large capacity, lead to market distortion of the Member States and the Union as a whole. In other words, the intention of the EU is to support the survival of small breweries whose capacity is insufficient for their favorable fiscal position to cause distortions in the market. In order to ensure this, a maximum threshold of annual production is prescribed as well as the condition that the brewery is independent legally and economically from other breweries, not only in terms of ownership structure and economic relations but also regarding the production structure, premises and facilities. In addition, it is necessary that independent small brewery produces its own brand, not under the license of other brewery. In this way it ensures the preservation of local indigenous brands of beer in certain regions of Member States.

In the view of the Commission the concept of economic independence of breweries refers to the capacity of the brewery to make its business decisions independently. Thereat, autonomous participation of breweries in the market cannot be considered as the evidence of independence of the brewery because it may be the result of an agreement with the parent company – large brewery in order to avoid competition among brands that produce smaller breweries in its ranks. The judgment¹³ of the Court, which becomes *case law* for all Member States, implies that legal and economic criteria should be used in order to assess the independence of breweries. The legal criteria imply that there are no structural links in terms of share in the ownership and voting rights, and economic that there are no economic links, in terms of management and business connections, that lead to the influence of the management of one brewery on the business decisions of another.

EXCISE POLICY OF EU MEMBER STATES

In terms of implementing the provisions of Directive 92/83/EEC, which allow differentiated taxation of beer under certain conditions, EU Member States apply different approaches. Out of 28 EU Member States, only 6 of them taxed beer at a single rate of excise duty, while other Member States have differentiated rates of excise duty. Given that Directive provides only framework standards, Member States apply various modalities of taxation and differentiation of excise duty rates.

Most States use the criterion of production volume for the differentiation of excise duty. Under the Directive Member States that use the criterion of production volume must apply the prescribed maximum threshold of beer production which may be subject to reduced rates of excise duty amounting to 200,000 hl. A number of EU Member States have taken the maximum allowable threshold from the Directive, while the other Member States with differentiated rates of excise duty on beer prescribed lower threshold of production. According to the situation on 1 July 2014 the minimum threshold of production for the application of differentiate rates is prescribed by Estonia (3,000 hl), followed by Hungary (8,000 hl), Latvia (10,000 hl), Ireland (20,000 hl),

¹³ Court judgment, OJ C 141, 20 June 2009.

Germany (40,000 hl), Austria (50,000 hl), Great Britain (60,000 hl) and, finally, Finland (100,000 hl)¹⁴. Three Member States, Netherlands, Portugal and Spain, do not have a single standard excise duty, but use the scale with 4 to 5 levels of sugar in beer (° Plato), but in Netherlands small breweries pay 92,5% of standard excise duty, depending on scale, and in Portugal 50%. Ireland is specific for using the threshold of production for differentiation of excise duty but tax relief is not applied over the lower rate, but through refund of 50% of paid excise duty only for those breweries that produce less than 20,000 hl of beer per year.

Box 1: The scales of beer taxation in the EU on the basis of production volume

Member States	threshold 1 (hl)	threshold 2 (hl)	threshold 3 (hl)	threshold 4 (hl)	threshold 5 (hl)
Luxemburg	50,000	200,000			
Austria	12,500	25,000	37,500	50,000	
Finland	2,000	30,000	55,000	100,000	
Belgium	12,500	25,000	50,000	75,000	200,000
Czech Republic	10,000	50,000	100,000	150,000	200,000
Germany	5,000	10,000	20,000	40,000	
France	10,000	50,000	200,000		
Poland	20,000	70,000	150,000	200,000	

Source: Report of the European Commission, 1 July 2014.

In some States production threshold for the application of a reduced rate of excise duty is unique, while in other Member States several levels of production with different rates of excise duty (scale of rates) are prescribed. Box 1 gives an overview of prescribed production thresholds for the application of differentiated rates of excise duty on beer in EU Member States.

According to Directive Member States are obliged to ensure the equal application of reduced rates on beer which is in their territory delivered by independent small breweries situated in other Member State. For the purpose of applying this provision, Member States have at their disposal the EMSC mechanism (Excise Movement and Control System) which includes electronic monitoring and control the movement of excise products under suspension within the EU¹⁵, as well as the electronic system of mandatory exchange of data on excise taxpayers, holders of excise warehouses and excise products which allows the participation of inspectors from the tax administration of one State in controls in another State¹⁶.

EU POLICY AND PRACTICE IN THE CASE OF GREAT BRITAIN

For possible introduction of differentiated rates of excise duty on beer in B&H it is useful to analyze the motives for the introduction, legal framework and practice of large EU Member States such as Great Britain which in total beer production in the EU participates with 13% and in total revenues from excise duties on beer in the EU with 40%¹⁷. Such discrepancy of production and revenues collected indicates a high rate of taxation of beer in Great Britain.

¹⁴ Source: European Commission, 1 July 2014.

¹⁵ System is mandatory for all Member States from 1 January 2011.

¹⁶ System, which entered into force on 1 July 2005, is established by the Regulation 2073/2004 (Council Regulation No 2073/2004 of 16 November 2004 on administrative cooperation in the field of excise duties).

¹⁷ Source: SIBA, the Society of Independent Brewers.

Differentiated taxation in Great Britain was initiated in early 2002. Fiscal authorities strove to achieve microeconomic and macroeconomic goals by progressive taxation of beer. Given the lower profitability of small companies, which was reflected in a worse market position, it was necessary to bring small local breweries in equal position with tax relief in regional and national market. Strengthening small breweries should contribute to breaking the monopoly of a few big breweries and provide the necessary dynamism and higher level of innovation necessary for the development of the beer industry and market in line with growing preferences of consumers in terms of new products, variety of supplies and better quality. At the macroeconomic level tax reliefs for small breweries should contribute to maintaining jobs in smaller local communities, reducing regional disparities in development, strengthening competition in the market, reducing sales prices and increasing the export of beer¹⁸.

Box 2: Formulas for calculating reduced rates of excise duty on beer in Great Britain

i. Annual production to 5,000 hl

Reduced rate of excise duty = GP * 50% SST

ii. Annual production 5,000 – 30,000 hl

$$\text{Reduced rate of excise duty} = \frac{\text{GP} - 2,500}{\text{GP}} * \text{SST}$$

iii. Annual production 30,000 – 60,000 hl

$$\text{Reduced rate of excise duty} = \frac{\text{GP} - (2,500 - 8,33\% * \text{GP}_1)}{\text{GP}} * \text{SST}$$

Legend:

GP = annual production (hl)

GP₁ = annual production (hl) over the threshold of 30,000 hl

SST = standard rate of excise duty

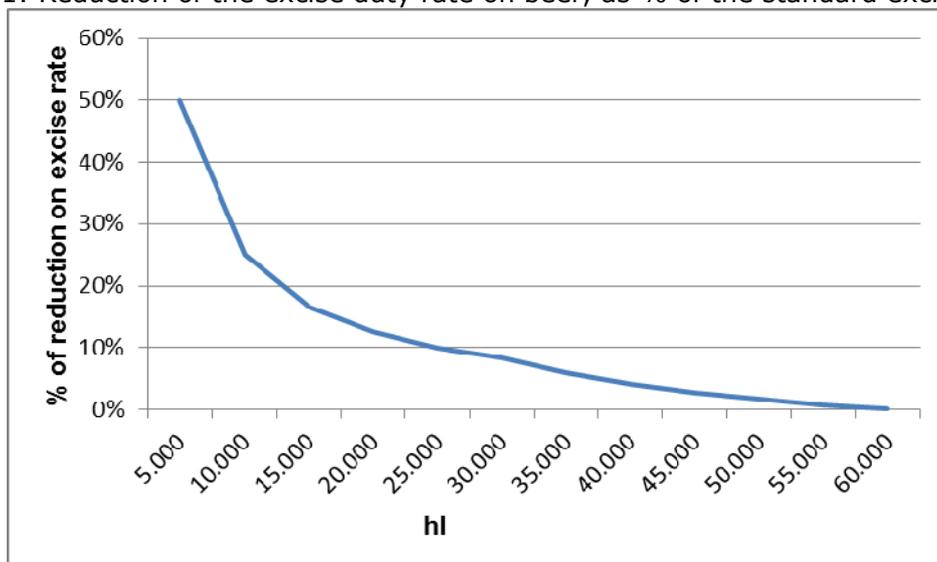
Source: HM Revenue & Customs, Notice 226 Beer Duty, April 2014.

Differentiated taxation of beer was introduced on 1 June 2002. At the beginning breweries that were producing less than 30,000 hectoliters per year could enjoy tax relief in the form of 50% of the standard excise duty on beer, with the full reduced excise duty (50%) applied to the first 5,000 hectoliters. Breweries that produce between 5,000 and 30,000 hl could apply lower rates of excise duty to be charged in proportion to the level of production. From 1 June 2004 the upper threshold of production that is subject to tax relief is increased to 60,000, with the relief that reduces as the production rises to 60,000 hl (see Box 2).

Although formulas for calculating reduced rates of excise duty are complex, it can be concluded that mentioned approach provides the achievement of the primary objective to help small breweries. Tax relief does not apply linearly, but digressively meaning that as the production rises, especially over 30,000 hl, relief rapidly decreases to zero level in the production of 60,000 hl (Chart 1).

¹⁸ More: HM Revenue & Customs, <http://customs.hmrc.gov.uk>

Chart 1: Reduction of the excise duty rate on beer, as % of the standard excise duty



Source: Author's calculation; HM Revenue & Customs

It is also interesting to analyze the legal framework for the excise taxation on beer in Great Britain in the light of the dilemmas Member States had related to the application of the definition of "independent small brewery". Legislation¹⁹ in Great Britain defines the term "beer produced by small brewery" including the beer produced by breweries in Great Britain or abroad, except the beer produced under the license from other brewery.

If two or more breweries have collaboration, they form a group in terms of excise taxation, and to assess whether the group meets the criteria for the application of reduced rates, a total production of the group is taken. This is necessary in order to avoid that a group of breweries achieve the same tax reliefs as it would be the case if there is no correlation between small breweries that form the group. In case that one brewery, which is associated with other breweries in the group, has more than 50% of production under license, the entire group is excluded from the scheme of reduced rates.

In order to qualify for the tax relief, in addition to satisfying the quantitative limitations of production of 60,000 hl, a small brewery must prove that it is a single brewery that is not associated with other breweries. Brewery is considered to be the associated brewery if produces beer in one or more breweries in the calendar year or is in connection with any person who produces beer in another brewery.

The concept of associated company is laid down in details in the Income and Corporation Taxes Act 1988. The association exists in the following cases:

- If persons are associated with marriage or kinship;
- If there is a partnership between persons;
- If there is a mutual association between companies and with persons who control them (for example if the person has direct or indirect control over company's affairs);

¹⁹ Source: HM Revenue & Customs, Notice 226 Beer Duty, April 2014, <http://customs.hmrc.gov.uk>.

- If the companies are linked through shareholders (individuals or companies) who control the company, either on their behalf or together with persons associated with shareholders;
- If the association occurred as a result of controls of associated persons (for example if a husband controls company x and wife company y then it is considered that companies x and y are associated).

The introduction of differentiated rates of excise duty for independent small breweries brought the strong positive effects so it can be concluded that the objectives of the government are met. In the past twelve years of the application of lower rates of excise duty the number of small breweries has grown from 235 to 723²⁰, representing 65% of the total number of breweries in Britain²¹. Today, small breweries in Great Britain employ 5,500 full-time workers. Only in 2013 900 new jobs have been created, although with the process of investing in modern equipment it is expected a slower growth in employment²². It is estimated that every job in a small brewery generates 21 jobs in the chain of supply and distribution²³. Small breweries have also made progress in diversifying the product range so today they offer even 3,000 permanent local brands and approximately 4,000 special and seasonal brands²⁴. These results are even more impressive if we take into account two considerations. In the period 2002-2012 excise duties on beer increased from 11,89 GBP to 19,12 GBP, while the VAT rate was increased from 17,5% to 20%. An increase in taxes had a negative impact on prices and consumption not only of big but of small breweries as well. On the other hand, the global economic crisis led to a drop in consumer's spending. However, although the total beer production in Britain has been reduced by 22%, small breweries recorded a growth of 37% in the period 2009-2013²⁵. Continuous growth in number and production of small breweries indicates to fact that the excise policy towards small breweries represented an effective protection, but also a preventive measure, which in time of global economic crisis significantly helped their survival, and today, in time of recovery, provides security for investment and innovation.

POLICY AND TRENDS IN TAXATION OF BEER IN B&H

Until the reform of indirect taxation the policy of taxation of beer, administration and allocation of revenues from excise duties were under the jurisdiction of the Entities and Brcko District. Initially the Entity policy of taxation of beer meant to differentiate rates on domestic and imported beer. On the domestic beer in the Federation of B&H (FB&H) excise duty was paid in the amount of 20 DEM / hl, and on imported 30 DEM / hl. The excise rate on domestic beer in the Republic of Srpska (RS) was lower and amounted to 0,15 DEM/l, while the excise rate on imported beer was identical to the rate in the FB&H. Discrimination of imported beer in FB&H was completed in 1999 and in RS in 2000 when a single rate of 0,20 KM/l was adopted. Brcko District, after obtaining the fiscal autonomy, introduced an identical rate of excise duty on beer in 2002. The reform of indirect taxation in the segment of beer taxation brought only changes in the administration and distribution of revenues, while the rate of excise duty of 0,20 KM/l retained until the last amendments to the Excise Duty Law in B&H.

²⁰ Source: SIBA, the Society of Independent Brewers, Beer Report 2014.

²¹ More: Ernst&Young, „The Contribution made by Beer to the European Economy“, EU Report - December 2013.

²² Ibid.

²³ Source: SIBA, the Society of Independent Brewers, Local Beer British Brewing Report 2012.

²⁴ Ibid.

²⁵ Source: SIBA, the Society of Independent Brewers, Beer Report 2014.

Data on the collection of excise duty in the period show the revenue growth that lasted until the global economic crisis (Chart 2). The lowest level of collected revenue was recorded in 2011, when it was collected 14,1% less revenue than in 2008. After a slight increase in revenue collected in 2012 from 4%, in 2013 there was again a drop in revenue (Chart 3) which continued throughout 2014.

Chart 2 Trends in the collection of excise duty on beer (2006-2013)

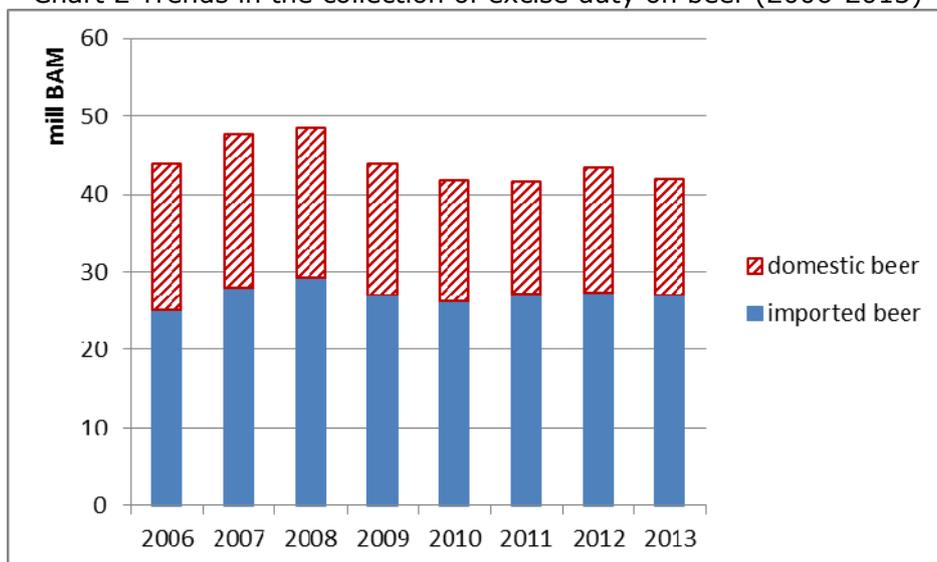
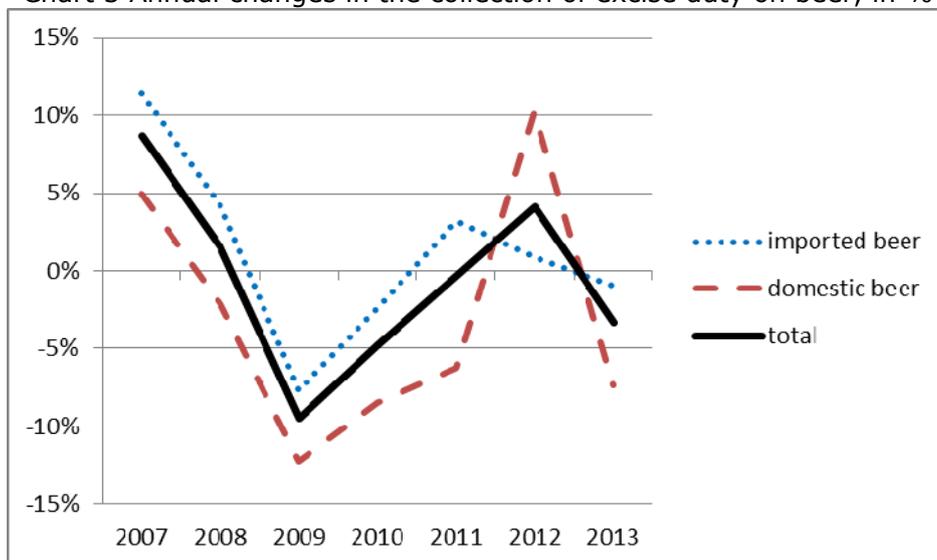


Chart 3 Annual changes in the collection of excise duty on beer, in %

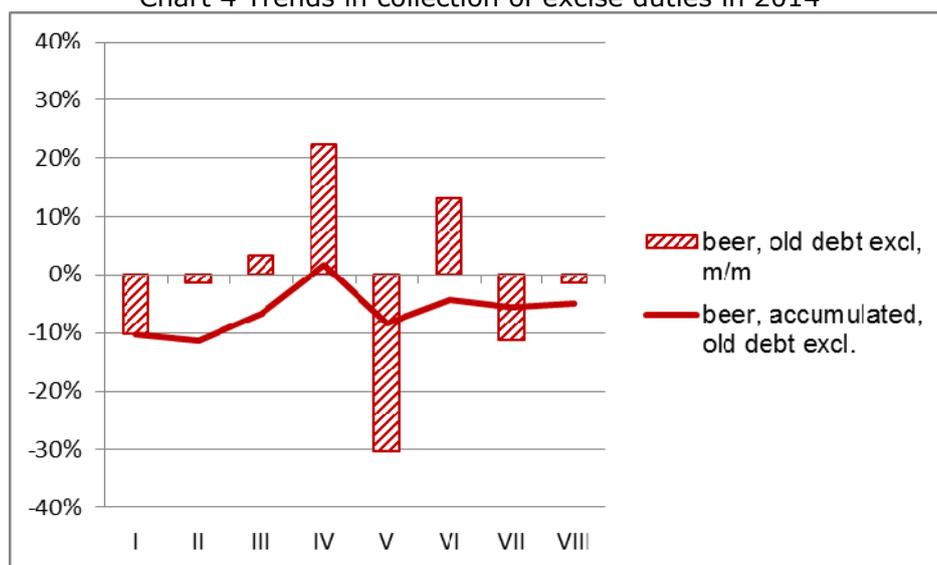


Strong monthly fluctuations marked the collection of revenue from excise duties on beer in 2014 (Chart 4). In addition, earlier this year a significant amount of debt on the basis of excise duty was collected. The total collection of current excise duties and debt is by 14,2% higher than the collection of excise duties on beer in 2013. Due to a one-off effect, excluding the collection of old

debts from the total collection of excise duties, a negative growth of 4,7% occurred instead of the positive trend.

Analysis of trends in collection of excise duties on beer indicates a continuous contraction of the market, which is now for 14% smaller than in 2008. Another important phenomenon is steadily decreasing share of domestic beer, even in such a reduced market. Compared to 2006 the share of domestic beer is reduced from 7 p.p. While the drop of the market of imported beer in the period 2009-2013 compared to 2008 amounted to maximum 10%, a quarter of market was lost with domestic beer per year (Chart 5).

Chart 4 Trends in collection of excise duties in 2014



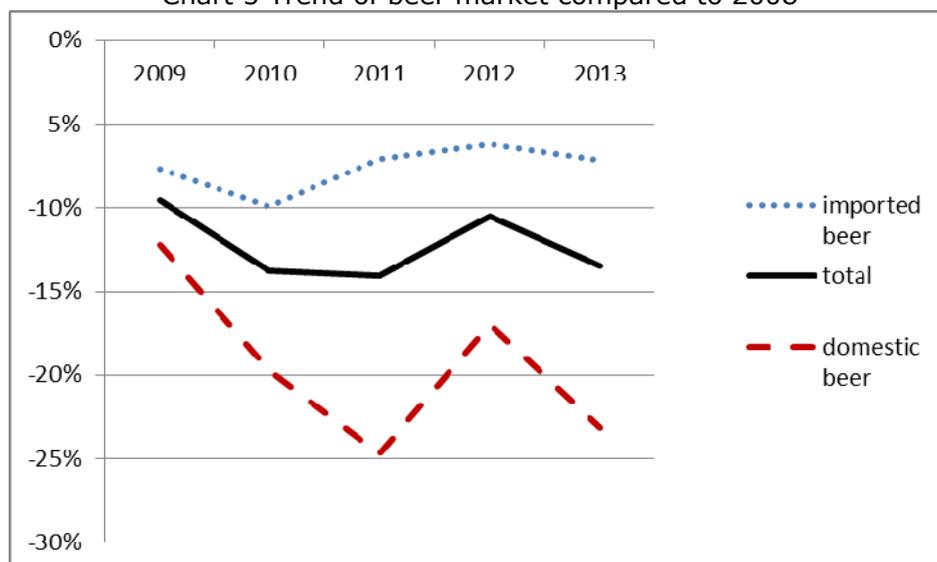
As of 1 September, B&H introduced differentiated rate of excise duties on beer by amending the Law on Excise Duties. The current single rate of 0,20 KM/l was increased to 0,25 KM/l, and a lower rate of 0,20 KM/l was introduced. Since the beer is taxed by the specific excise duty, in time the rate of excise duty is subject to the loss of real value due to inflation. To prevent erosion of revenue many countries periodically change rates of specific excise duty or incorporate automatic indexation in laws²⁶. Starting from the statistics of retail prices in B&H in the period 2006-2013²⁷ the cumulative price increase amounted to 24,8%. Given that the increase of standard rate of excise duty on beer amounts 25% it can be concluded that the increase in the standard excise duty annuls the effect of inflation in the previous period. By amendments to the Law the method of determination of excise duty rate has not been complied with the EU standards so it is still expressed in monetary units per liter of beer. Therefore, collection of revenue from excise duties depends solely on the amount of beer consumption, while in the EU it depends also on the level of alcohol or sugar (° Plato) contained in beer.

²⁶ See the Law on Excise Duties in Serbia

²⁷ Data from the Agency for Statistics of B&H, www.bhas.ba

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Chart 5 Trend of beer market compared to 2008



Amendments to the Law provide that the right to tax relief can be achieved by breweries with an average beer production in the previous three years less than 400,000 hl, as well as importers of beer, provided that the beer is purchased by the manufacturers whose average production in the last three years was less than 400,000 hl. In addition to the threshold of production as a criterion for the application of reduced rates, amendments to the Law do not provide for the application of the criterion of independent breweries, as prescribed by the EU Directives.

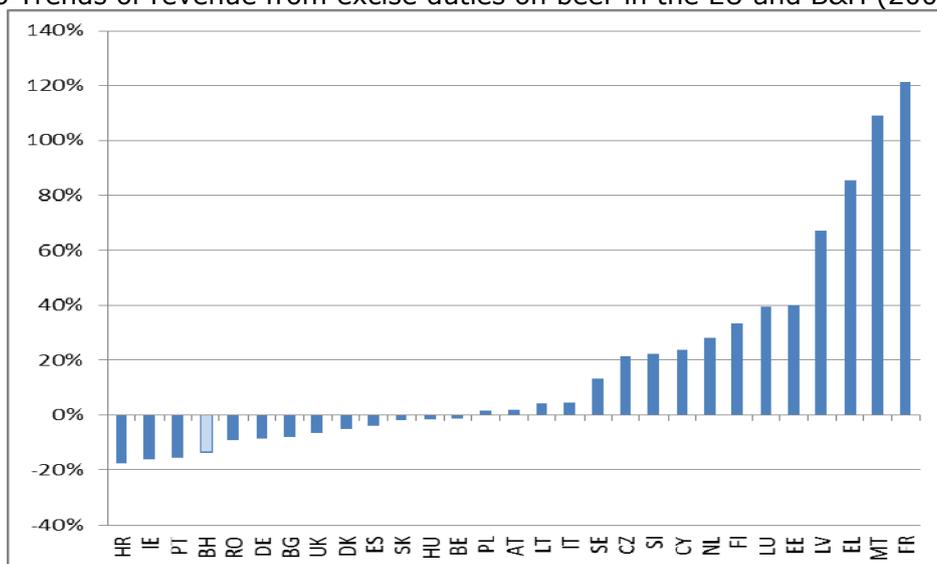
B&H vs EU

Data on collection of revenue from excise duties on beer in EU Member States show divergent trends. When compared to the collection of excise duties in 2013 with 2008 it can be concluded that 16 Member States achieved growth, moving up to a maximum of 120% in France (Chart 6). Other States recorded a decrease moving up to -17% in Croatia. Comparing the collection of revenue in a given period in B&H it can be seen that B&H is at the top of countries in terms of negative effects in the collection of excise duties on beer.

Chart 7 shows that the majority of EU Member States have a far higher rate of excise duty than B&H. Only four countries have a lower rate of excise duty, which is only slightly higher than the EU minimum excise duty. With the increasing the standard excise duty (in the Chart B&H (1)) B&H has shifted its position for only one place in the scale.

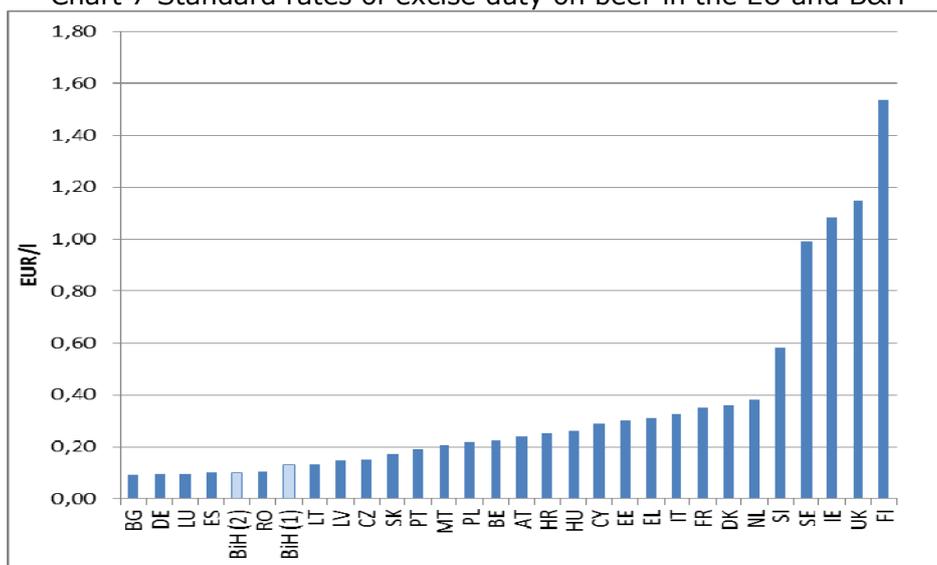
Comparing with the minimum excise duty in the EU for 1 liter of beer, new standard excise duty in B&H increased by 37% and decreased by 9%. On the other hand, excise duties in B&H after the increase are lower than the excise duty on beer in Croatia, standard rate by 52% and reduced by 62%.

Chart 6 Trends of revenue from excise duties on beer in the EU and B&H (2008-2013)



Source: European Commission, 1 July 2014., data for Romania (2008-2012), other Member States (2008-2013); Ministry of Finance of Croatia (data for 2008); Author's calculation.

Chart 7 Standard rates of excise duty on beer in the EU and B&H



Source: European Commission, 1 July 2014.; Law on Excise Duties in B&H, 1 September 2014.; Author's calculation.
Note: rates are calculated for beer with 4,8% alcohol / 12° Plato and expressed in EUR per 1 liter.

INSTEAD OF CONCLUSION: LESSONS FOR B&H

EU standards in any area represent a framework to which Member States should adhere. But the aggravating circumstances to set common standards represent the heterogeneity of the EU in terms of the size of Member States, level of economic and social development, historical heritage and tradition, the standard of living and habits of citizens, etc. For example, standards for the classification of companies into small, medium and large cannot be the same in Germany or Malta.

Similar situation is with the standards for differentiated taxation of beer. The maximum threshold of production is set at 200,000 hl to be high enough to cover small breweries in large States. However, practice shows that large Member States such as Germany and Great Britain opted for much lower limits of production to truly cover small breweries. Such practice indicates the objectives of excise policies in these Member States. Lower excise duties on beer are not considered as protective measure, but as fiscal reliefs by which broader developmental, regional and social objectives could be achieved, in terms of ensuring even development within the country and reducing the pressure of migrations to urban areas and big cities. Example of Great Britain suggests that the fiscal relief is not linear for all independent breweries whose production is below the prescribed threshold, but digressive, stimulating only micro breweries. In addition, the precise definition of the term "legal and economic independence" by the judgments of the European Court of Justice and national regulations of Great Britain maximally narrows the space for possible abuses by major breweries. Great Britain is an example that well advised and targeted fiscal measures can be effective if they are accompanied by precise rules that will exclude or keep to a minimum the occurrence of abuses.

The introduction of differentiated excise duties on beer in B&H in the current situation can have a favorable effect on a few local breweries, given that the level of production is below the prescribed threshold. In given circumstances, when all local companies together cover only 35% of the market in B&H, which is below allowed threshold of concentration, business strategies of the domestic beer industry should be directed towards the increase in the market share. Internal growth for the company would include investments in additional capacities of existing owners or the entry of new investors, and external one the merger of companies (mergers and acquisitions). The increase in capacity leads to the realization of the positive effects of volume and size economies. Concentration of domestic production may represent a certain strategic option that can ensure greater efficiency of internal economy, lower prices and higher sales. However, in the near future, breweries that are close to the mentioned threshold for the application of the reduced rate of excise duty could face the problem of further increasing production capacity over the threshold for the application of lower excise duty. Thus, the fiscal measure, which in given moment of company's business, enables favorable position in the market, can easily be turned into a limiting factor for the growth of the company, closing a company for investments and business expansion („lock-in effect"), at first leading it to the stagnation and then to the decline related to the competition.

Bearing in mind that with the latest amendments to the Law on Excise Duties B&H increased the standard rate of excise duty and introduced a lower rate, a question of fiscal effects of this measure is raised. Introducing the scale of excise duty rates may provide an incentive to increase smuggling and tax evasions so in addition to excise duties, revenues from VAT may also be lost. In addition, a differentiation of rates produces additional compliance costs for taxpayers in relation to proving the volume of production required for the realization of reliefs. Additional costs of administering will burden customs and tax services in connection with the control and verification of documentation for entitlement to reliefs, as well as the monitoring of trends of beer production in the country and from the supplier importer. Given the limited capacity of customs and tax services, more complex controls of taxing beer will lead to shifting the focus of inspectors from other taxpayers who bring most of revenues from indirect taxes. Since the excise duties on beer represent only 0,9% of indirect taxes, additional tax effort of taxpayers and fiscal authorities will probably exceed the additional revenues from differentiated excise duty rates²⁸.

²⁸ According to recent estimates of the ITA GB Macroeconomic Analysis Unit additional revenue from excise duties on beer are estimated at 6-7 mil KM per year. More: Revised projections of revenue from indirect taxes, MAU bulletin No. 108/109, July/August 2014, www.oma.uino.gov.ba.

Consolidated reports

Table 1. (Consolidated report: B&H institutions, entities, SA)

Consolidated report includes

- revenues from indirect taxes collected by the Indirect Tax Authority on the Single Account,
- transfers from the ITA Single Account,
- revenues and expenditures of the institutions of Bosnia and Herzegovina,
- revenues and expenditures of the budget of the Federation of Bosnia and Herzegovina,
- revenues and expenditures of the budget of the Republika Srpska.*

Report doesn't include unadjusted revenues collected on ITA SA.

**Includes: (A) Budget of the Republic and extra-budgetary resources recorded in Treasury General Ledger of the RS, (B) total foreign debt for the projects realized through municipalities and companies, and (C) Budget users who have their own bank accounts (including some foreign project implementation units established by ministries)*

Preliminary report: B&H Institutions, entities and SA, I-VIII 2014

(in million KM)	I	II	III	IV	V	VI	VII	VIII	Total
Revenue	441,3	457,7	544,0	582,4	470,7	507,3	581,1	516,6	4.101,1
Taxes	414,6	411,3	426,0	459,4	410,3	422,8	481,8	503,8	3.530,0
Direct taxes	23,5	27,5	56,6	42,8	25,0	25,9	30,6	24,4	256,2
Taxes on income, profits and capital gains	22,8	26,6	55,6	41,7	24,0	24,7	29,1	23,1	247,7
Taxes on property	0,7	0,8	1,0	1,1	1,0	1,2	1,5	1,3	8,6
Indirect taxes (net)	391,0	383,8	369,2	415,3	385,2	396,5	451,2	478,9	3.271,1
VAT	245,3	257,5	240,3	251,8	245,7	238,9	277,1	312,1	2.068,8
Excises	109,5	86,3	86,6	115,6	99,6	112,6	126,0	117,2	853,3
Road fee	22,2	20,6	20,2	27,1	20,9	24,3	26,6	29,1	191,2
Customs	12,8	18,3	20,7	19,3	17,4	18,8	19,8	18,9	146,0
Other indirect taxes	1,1	1,1	1,4	1,4	1,7	1,8	1,7	1,6	11,8
Other taxes	0,1	0,0	0,2	1,4	0,1	0,4	0,0	0,4	2,7
Social security contributions	0,0	0,0	0,0	0,0	0,0	0,7	8,0	6,3	14,9
Grants	1,7	0,4	7,9	0,2	0,5	12,8	0,9	5,8	30,2
Foreign grants	1,7	0,4	7,8	0,2	0,5	12,6	0,9	5,6	29,8
Transfers	0,0	0,0	0,1	0,0	0,0	0,1	0,0	0,2	0,4
Other (non-tax) revenue	25,0	46,0	110,1	122,7	59,9	71,1	90,4	0,8	526,0

(in million KM)	I	II	III	IV	V	VI	VII	VIII	Total
Expenditure	416,4	449,2	421,2	445,6	439,4	437,4	532,1	600,6	3.741,8
Expense	414,4	435,5	416,5	437,4	428,1	436,0	519,8	553,9	3.641,6
Compensation of employees	124,7	126,6	130,5	128,1	129,5	132,1	136,5	126,1	1.034,0
Use of goods and services	12,9	30,8	30,9	27,3	22,5	32,5	28,5	21,7	207,1
Social benefits	52,5	54,1	65,3	53,6	53,5	55,5	60,5	63,9	458,9
Interest	5,9	10,4	17,3	9,4	19,8	20,0	7,1	9,1	99,0
Interest payments to non-residents	2,4	7,9	10,1	5,9	12,5	9,1	4,4	5,7	58,1
Interest payments to residents	3,4	2,5	7,2	3,5	7,3	10,9	2,7	3,4	40,9
Subsidies	2,1	6,5	5,1	8,4	10,9	17,8	19,2	33,0	102,9
Grants, transfers (including transfers from SA**)	211,1	200,7	161,9	207,5	185,6	169,1	256,8	281,6	1.674,2
Other expense	5,2	6,4	5,6	3,1	6,3	8,9	11,3	18,7	65,5
Net acquisition of nonfinancial assets	2,0	13,6	4,6	8,2	11,4	1,5	12,3	46,6	100,2
Acquisition of nonfinancial assets	2,2	14,2	5,0	8,9	11,6	2,8	18,0	47,9	110,5
Disposal of nonfinancial assets	0,1	0,6	0,4	0,8	0,2	1,3	5,7	1,2	10,4
Gross/Net operating balance (revenue minus expense)	26,9	22,2	127,5	145,0	42,6	71,4	61,3	-37,4	459,5
Net lending /borrowing (revenue minus expenditures)	24,9	8,5	122,9	136,8	31,2	69,9	49,1	-84,0	359,3

** transfers from SA include unconsolidated transfers to BD, cantons, municipalities and road funds

Table 1