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What Is Expected from New Excise Duty Regulations in Croatia?

Danijela Kuliš

New excise duties on tobacco and unleaded petrol should boost the Croatian central budget by HRK 60 million and 220 million respectively. Compliance with the EU minimum taxation standards and curbing tobacco consumption are good enough reasons to increase the excise duty rates. However, the stated amounts will not contribute significantly to the covering of the current year's budget deficit of HRK 14 billion. Much more revenues for the state budget could be derived through successful smuggling and illicit trade combating, tax debtor identification and the collection of tax arrears.

In view of the proposed state budget revision, the Croatian Government adopted two regulations (NN 102/10) at its session held on August 24, 2010. The Regulation on Excise Duty Rate on Cigarettes and Regulation on Excise Duty Rate on unleaded petrol, to become effective on October, 1 and September, 1 respectively, introduce higher amounts of these duties than those applied so far. The idea is to increase tax revenues and to achieve further harmonisation with the EU *acquis*.

Excise duties on tobacco products in Croatia vs. EU

The Excise Duty Act (OG 83/2009) which entered into force on January 1, 2010, sets out the basic principles of excise taxation in accordance with the European Harmonized System for three commodity groups: energy products and electricity, alcohol and alcoholic beverages and tobacco products.

The new Regulation on Excise Duty Rate on Tobacco Products (OG 102/10) introduces an increase in proportional excise duties from 30% to **33%** of the relevant retail selling price (RSP). Due to this increase, the share of overall excise duty (specific plus proportional excise), currently standing at 50% of RSP, would go up, approximating the minimum rate of 57% required under the European legislation.

A comparison between the amounts of excise duties (Table 1) shows that excise duties on cigarettes are lower in Croatia than in the EU. In accordance with the health and environmental policy requirements, the upward trend in excise tax on cigarettes in the EU, observed over the past few years, is likely to continue, which means that the Croatian legislation will have to follow this trend.

Table 1 The amounts of excise duties on tobacco products

Tobacco product		Excise Duty Act (OG 83/09)	Regulation (OG 102/10)	EU 2010/2011 ¹	EU 2014 ¹
Cigarettes	Specific excise	HRK 180 per 1,000 units	HRK 180 per 1,000 units	EUR 64 per 1,000 units	EUR 90 per 1,000 units
	Proportional excise	30% of RSP	33% of RSP	57% of average RSP	60% ² of average RSP
Cigars		HRK 1,100 per 1,000 units		5% of average RSP or EUR 12 per 1,000 units or kg ³	
Cigarillos		HRK 220 per 1,000 units		5% of average RSP or EUR 12 per 1,000 units or kg	
Tobacco		HRK 92-136 per kg		Fine-cut smoking tobacco ⁴	
				40% of average RSP or EUR 40 per kg	43% of average RSP or EUR 47 per kg
				Other tobacco products	
				22% of average RSP or EUR 22 per kg	22% of average RSP or EUR 22 per kg

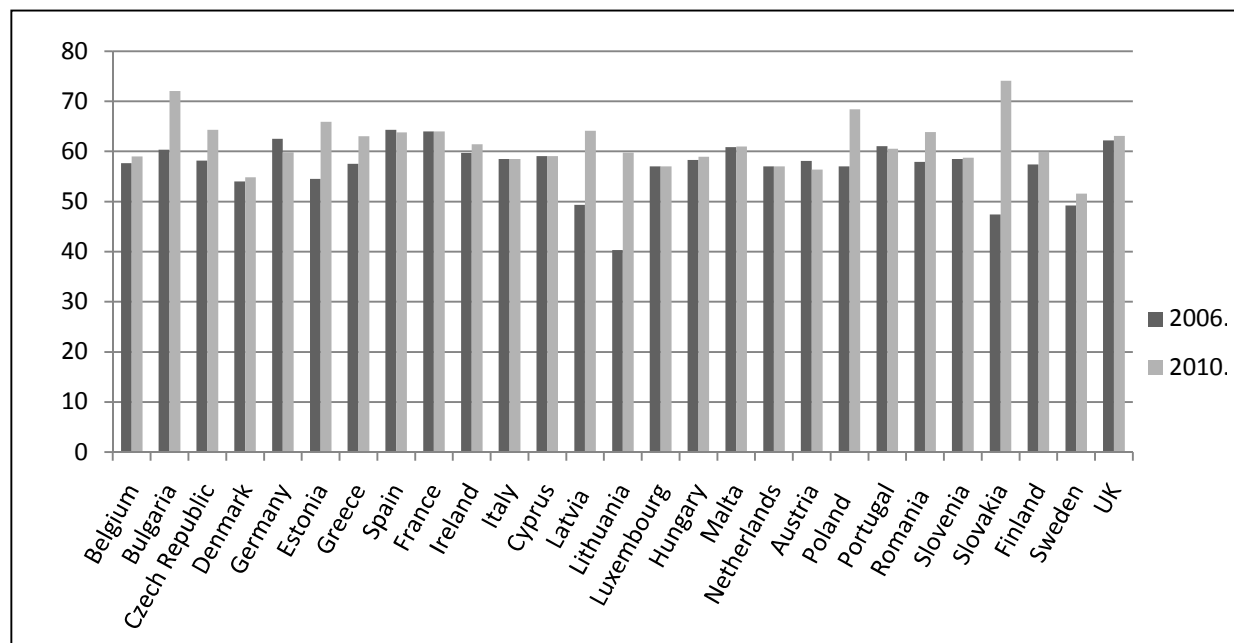
¹ Official Journal of the European Union, 27 February, 2010, L 50/1. Available from: [<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:050:0001:0007:EN:PDF>].

² Countries which have not reached the minimum rate, or have only just reached it (Bulgaria, Greece, Estonia, Lithuania, Latvia, Hungary, Poland and Romania) will be allowed a transitional period until January 1, 2018.

³ As of January 1, 2011.

⁴ In the EU, fine-cut smoking tobacco intended for the rolling of cigarettes is taxed at a rate different from that applied to other tobacco within the same group "Other tobacco products".

Figure 1 Overall minimum excise duty on cigarettes in the EU, as a % of average RSP



Source: European Commission. Available from:

[http://ec.europa.eu/taxation_customs/resources/documents/taxation/excise_duties/tobacco_products/rates/excise_duties-part_III_tobacco-en.pdf](January 2010); [<http://www.douane.gouv.fr/data/file/1432.pdf>] (June 2006)

A comparison in the share of overall minimum excise duty in RSP between EU Member States (Fig. 1) points to an increase in these shares in 2010 relative to 2006, in all the countries, especially those that had joined the EU in 2004. This was due to the application of the "minimum 57%" rule, growth in budget revenue and cigarette consumption control as a measure of health, environmental, social and educational policies.

Excise duty on unleaded motor petrol in Croatia vs. EU

Excise duty on unleaded petrol, tariff codes CN 2710 11 31, 2710 11 41, 2710 11 45 and 2710 11 49 has amounted to HRK **2,850 per 1,000 litres**. Pursuant to the new Regulation, the amount goes up to HRK **3,100 per 1,000 litres**. The minimum prescribed amount of excise duty on lead-free petrol in the EU is EUR 359 per 1,000 litres (HRK 2,613 per 1,000 litres)¹. Only six countries (Bulgaria, Estonia, Cyprus, Latvia, Portugal and Finland) have lower excise duties than Croatia.

The increase in excise duty rates is accounted for by a shortfall in budget revenue and the need to return to the rate applied in 2007, when the revenue outturn was 6% above the plan for 2010.

Table 2 Excise duty revenues in Croatia, 2006-2010, in million HRK

	2006	2007	2008	2009	2010 plan
Tobacco products	2,710	2,944	3,084	3,074	3,017
Unleaded motor petrol	6,314	6,485	6,065	6,046	6,078

Source: Monthly Statistical Review of the Ministry of Finance, No. 171 (2009) and 174 (2010).

Revenues from excise duties on tobacco products dropped by HRK 10 million in 2009 relative to 2008. The possible reasons for this may be reduced consumption, as a result of price-related (higher excise rates and prices) and non-price-related measures (tobacco consumption control regulations, health warning messages and ban on tobacco product advertising). Increasing excise duties normally has two effects: tax revenue growth and a drop in consumption. However, tobacco products are specific as there is no adequate substitute for them, while at the same time they are addictive. Therefore, an increase in their prices does not necessarily lead to a drop in the consumption of tobacco products. Reduced revenues from these duties are also due to tax fraud and tobacco smuggling. During only one action in June 2009, the police seized smuggled cigarettes worth HRK 4 million².

Excise duties on oil derivatives represent the most important excise revenues. In the first three months of 2010, collected excise on oil derivatives accounted for 66% of total collected excise duty revenues, followed by excise duties on tobacco products (22% of the total), which, altogether accounted for about 88% of total excise revenues in the first quarter of 2010.

The question is what will be the impact of higher prices on fuel consumption. Price elasticity, i.e. the impact of price growth on consumption, is higher in the case of fuels than in the case of tobacco products. In the former case, there is a possibility of substitution (e.g. the use of public transport), and the consumption also depends on the share of fuel costs in the total buyer's income (after reaching a certain limit, consumption goes down). Moreover, a rise in fuel prices, resulting in higher transportation costs, can lead to the growth of prices of other products.

¹ Available from:

[http://ec.europa.eu/taxation_customs/resources/documents/taxation/excise_duties/energy_products/rates/excise_duties-part_II_energy_products-en.pdf]

² Available from: [<http://www.seebiz.eu/hr/politika/akcija-memphis-policija-i-uskok-razbili-lanac-krijumcara-cigareta,47918.html>]

Expected effects

Given the trends in excise taxation and the fact that, besides the fiscal effects, account is increasingly being taken of the health and environmental impacts, both the amounts of and revenues from excise duties went up in all EU Member states over the last few years.

The proposal for raising the excise duties is in line with this trend, as well as with the need for harmonisation with the EU regulations. The question is, however, to what extent will the planned revenue increase (by HRK 260 million), even if it comes true, help overcome the state budget deficit of HRK 14 billion. The revenues lost due to the smuggling of and illicit trade in goods subject to excise duties, the identification of tax debtors and collection of tax arrears would certainly make a more substantial contribution to filling the budget gap.