Consumption Tax Trends 2010
VAT/GST and Excise Rates, Trends and Administration Issues

Chapter 1

Taxing Consumption

Consumption taxes

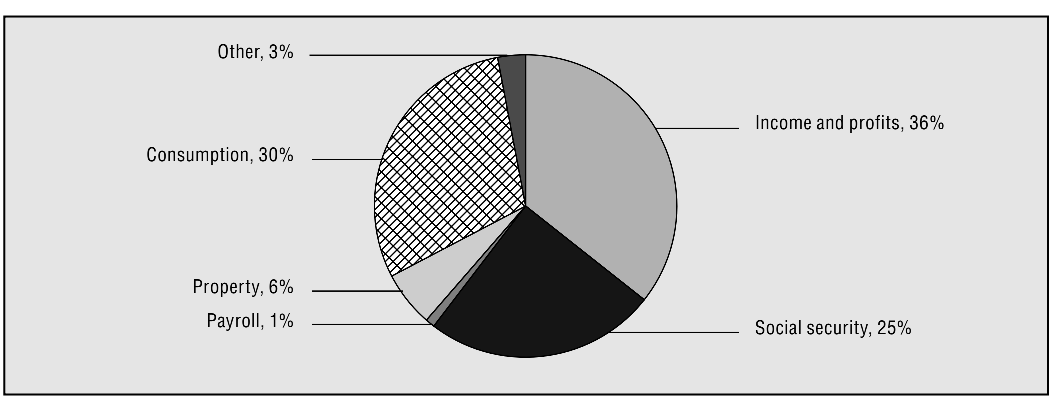
In the OECD classification, "taxes" are confined to compulsory, unrequited payments to general government. They are divided into five broad categories: taxes on income (1000), profits and capital gains (2000); social security contributions (3000); taxes on payroll and workforce; property taxes (4000); and taxes on goods and services (5000) (OECD, *Revenue Statistics 1965-2008*).

In the statistical nomenclature of the OECD, consumption taxes (identified as "Taxes on production, sale, transfer, leasing and delivery of goods and rendering of services") fall mainly into two sub-categories:

- *General taxes (5110)* on consumption. This category includes value added taxes (5111), *i.e.* VAT and its equivalent in several jurisdictions, the Goods and Services Tax (GST),[1] sales taxes (5112), and other general taxes on goods and services (5113).
- *Taxes on specific goods and services (5120),* consisting primarily of excise taxes (5121), customs and import duties (5123) and taxes on specific services (*e.g.* taxes on insurance premiums and financial services).

Looking at the unweighted average of revenue from the five broad categories of taxes as a percentage of overall taxation in the OECD member countries (see Tables 3.2, 3.4 and 3.7), it can be seen that the proportion of consumption taxes is roughly 30%. In 2008, this broke down to one-third for taxes on specific goods and services and two-thirds for general consumption taxes.

Figure 1.1. **Average tax revenue as a percentage of aggregate taxation, by category of tax**



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General consumption taxes

Retail sales taxes

A retail sales tax is a consumption tax charged only once at the last point of sale for products to the final end user. In principle, only consumers are charged the tax; resellers are exempt if they do not act as final end users of the products. To achieve this, business purchasers are normally required to provide the seller with a “resale certificate”, which states that the seller is purchasing an item to resell it. The tax is charged on each item sold to purchasers who do not provide such a certificate. The retail sales tax covers not only retailers, but all businesses dealing directly with final end users.

The basis for taxation is the sale price. Unlike multi-stage cumulative taxes, this system allows the tax burden to be calculated exactly and it does not discriminate between different forms of production or distribution channels.

The United States is the only OECD country within which a retail sales tax is employed as the principal consumption tax. However, the retail sales tax in the United States is not a federal tax. Rather, it is a tax imposed at the state level. Currently, 46 of the 50 States impose retail sales taxes. In addition, over 7 500 local tax jurisdictions impose retail sales taxes in accordance with state law requirements. The local taxes are almost always identical in coverage to the state-level tax, are administered at the state level and amount in substance simply to an increase in the state rate, with the additional revenues distributed to the localities. Retail sales taxes are complemented in every state by functionally identical “use” taxes imposed on goods purchased from out-of-state vendors, because the state has no power to tax out-of-state “sale” and therefore imposes a complementary tax on the in-state “use”.

State or sub-federal retail sales and use taxes in place in the United States are not without their own problems, especially in the context of interstate and international trade. New means of communication have made purchasing goods across state borders without collection of tax even easier than it was before. Supreme Court rulings prohibit states from requiring vendors to collect tax on cross-border sales when they are not physically present in the purchaser’s state. To address this problem, as well as others caused by the lack of harmonisation in state sales and use taxes, a number of states have entered into the Streamlined Sales and Use Tax Agreement (SSUTA available at *www.streamlinedsalestax.org*).This agreement aims at establishing a uniform set of definitions of potentially taxable items that states can choose to tax or not (*e.g.* digital products). The Streamlined member states have also developed a Streamlined Sales Tax Registration System (SSTRS) that enables taxpayers to register voluntarily in order to participate in SSUTA. Voluntary registration requires sellers to collect sales and use taxes in all states into which they make sales, regardless of their physical presence there, and it permits sellers to benefit from increased legal certainty as regards their tax liability. This scheme could become mandatory if the US Congress approves proposed legislation providing congressional consent to SSUTA.

Value added taxes

VAT is the most widespread general consumption tax. The spread of this tax has been the most important development in taxation over the last half-century. Limited to less than ten countries in the late 1960s, it has now been implemented by over 150 countries (see Annex B) where it often accounts for one-fifth of total tax revenue. In addition, 20 of the 33 OECD member countries are members of the European Union[2] and share a common legal framework for VAT. The recognised capacity of VAT to raise revenue in a neutral and transparent manner has drawn all OECD member countries (except the United States) to adopt this broad-based consumption tax. Its neutrality towards cross-border trade has also made it the preferred alternative to customs duties in the context of trade liberalisation.

Although there is a wide diversity in the way VAT systems are implemented, the key features of VAT can be defined as follows:

- It is a tax on consumption, paid, ultimately, by final consumers and collected by businesses.
- The tax is levied on a broad base (as opposed to, *e.g.* excise duties that cover specific products).
- In principle, business should not bear the burden of the tax itself since there are mechanisms in place that allow for a refund of the tax levied on intermediate transactions between businesses.
- The system is based on tax collection in a staged process, with successive taxpayers entitled to deduct input tax on purchases and account for output tax on sales. As the final consumer is unable to recover the tax, the amount of tax actually collected through the staged collection process should be equal to the amount of VAT charged by the last vendor in the supply chain. In practice, VAT can also be described as a transaction tax.

Indirect tax

VAT is often categorised as an *indirect tax*. Although the distinction between direct and indirect taxes is not always clear, a basic distinction can be made between direct taxes as taxes levied "directly" on income and (possibly) wealth while indirect taxes are levied on the expenditures that the income and wealth finance. Sometimes VAT is also categorised as an indirect tax in that the person who is liable to pay the tax (the business) is someone other than the person who actually bears the cost of the tax (the final consumer).

The staged collection process

The value added tax system is based on tax collection in a staged process, with successive taxpayers entitled to deduct input tax on purchases and account for output tax on sales. Each business in the supply chain takes part in the process of controlling and collecting the tax, remitting the proportion of tax corresponding to the margin realised on transactions, or the difference between the VAT paid to suppliers and the VAT charged to customers. It is because of this characteristic that the tax is called "value added tax".

There are two main approaches for operating the staged collection process:

- The ***invoice credit method*** ("transaction based method") under which each trader charges VAT at the specified rate on each sale and passes to the purchaser an invoice showing the amount of tax thus charged. The purchaser, if subject to VAT on his own sales, is in turn able to credit such payment of input tax against the output tax charged on his sales, remitting the balance to the tax authorities and receiving refunds when there are excess credits. This method is based on invoices that could, in principle, be cross-checked to pick up any overstatement of credit entitlement. By linking the tax credit on the purchaser's inputs to the tax paid by the purchaser, the invoice credit method is designed to discourage fraud.

- The ***Subtraction method*** ("entity based method") under which tax is levied directly on an accounts-based measure of value added calculated for each firm by subtracting VAT calculated on allowable purchases from VAT on taxable turnover. This method is less suited to deal with differential rates structures. Of the OECD countries employing VAT, only Japan uses the subtraction method.

In practice, OECD countries with value added taxes impose the tax at all stages and normally allow immediate deduction of taxes on purchases by all but the final consumer. These features give value added taxes their main economic advantage, that of neutrality. The full right to deduction of input tax through the supply chain, with the exception of the final consumer, ensures the neutrality of the tax, whatever the nature of the product, the structure of the distribution chain and the technical means used for its delivery (stores, physical delivery, Internet).

When the right of deduction covers all inputs, the final burden of the tax does not lie on businesses but on consumers. This is not always the case since some non-OECD economies do not grant credits for the tax on purchases of capital goods or do not refund excess credits (any excess of tax paid on inputs over tax chargeable on outputs). In these circumstances some of the tax burden lies on business. It can also be argued that the economic burden of the VAT can lie in variable proportion on business and consumers. Indeed, the effective incidence of VAT, like that of any other tax, is determined not by the formal nature of the tax but by market circumstances, including the elasticity of demand for consumption and the nature of competition between suppliers (Ebrill, Keen, Bodin and Summers, 2001).

There are a number of other ways in which restrictions are imposed in practice on the right to deduct input tax. Some are deliberate and some result from imperfect administration. Deliberate limitations can result from the exemption of a number of activities. In most countries a number of services are exempt from VAT without right to deduct input tax for social (health, education and charities), practical (financial services, insurance) or historical (immovable property, land) reasons (see Chapter 3). Another set of restrictions to the right of deduction relates – or is deemed to relate- to purchases used for the private consumption of employees or clients of the business such as cars and entertainment. It may also happen that restrictions to the right of deduction are imposed on VAT incurred on investment goods or capital assets. This implies that an irrecoverable tax is embedded in the VAT base of final consumption and leads to a form of cumulative tax. Such a system is often called a "production-type VAT". However, most countries operate a "consumption-type VAT" where VAT is normally deductible on all inputs, including fixed assets.

Although VAT systems implemented in most countries are based on common characteristics, there remain many differences in the way they are operated, including between OECD member countries and even between European Union countries whose VAT laws share the same legislative root.

Neutrality

The concept of tax neutrality in VAT has a number of dimensions, including the absence of discrimination in a tax environment that is unbiased and impartial and the elimination of undue tax burdens and disproportionate or inappropriate compliance costs for businesses. Neutrality is one of the principles that help to ensure the collection of the right amount of revenue by governments in the right jurisdiction.

In domestic trade, tax neutrality is achieved by the staged payment system: each (fully taxable) business pays VAT to its providers on its inputs and receives VAT from its customers on its outputs. Input VAT incurred by each business is offset against output VAT so that the "right" amount of tax to be remitted to tax authorities by each business is the net amount or balance of those two. In some cases, the result of the offset gives rise to a refund due by the tax authorities to the business. Examples include businesses that incur more tax on their inputs than is due on their outputs (such as exporters, as their output is free of VAT under the destination principle) and businesses whose purchases are larger than their sales in the same period (such as new or developing businesses or seasonality). As a result of the staged payment system, VAT normally "flows through the business" to tax the supplies to the final consumer. It is important therefore that at each stage, the supplier is entitled to a full right to deduction of input tax, meaning that the tax burden eventually rests with the final consumer rather than the intermediaries in the supply chain.

This ensures that the tax ultimately collected along a particular supply chain is proportional to the amount paid by the final consumer, whatever the nature of the supply, the structure of the distribution chain, the number of transactions or economic operators involved and the technical means used.

Consumption tax

From an economic standpoint, VAT is a tax on final consumption by households. Practically, the tax deduction mechanism ensures that the VAT paid by businesses along the value chain does not bear on them but, ultimately, on final consumers only. Therefore, *as economists understand and use the term, only people consume. Businesses buy and use capital goods, office supplies and the like – but they do not consume them in this sense* (Keen and Hellerstein, 2010). In other words, final consumption is only made by private persons (as well as legal persons and governments when they do not act as businesses).

From a legal and practical standpoint, VAT is essentially a transaction tax. In "real life" things can be consumed in many ways. Some can be consumed fully and immediately (like a taxi ride); some can be bought and fully consumed later (like a sandwich); some can be consumed over a longer period of time (like a desk or a subscription to an online database). However, VAT does not actually tax such material consumption. Its subject is rather the whole of the transactions made across the value chain up to and including the final consumer.

In a VAT context, the term "consumption" covers two complementary elements: on the one hand the business-to-business supplies where businesses use inputs for providing onward supplies and, on the other hand, the purchases made by final consumers. The staged payment system is built in such a way that the tax revenue for governments corresponds to the tax applied to the sale to the final consumer only.

This concept of consumption should not be confused with the term "use and enjoyment" (an expression found in the VAT system of the EU), which is closer to the meaning of the term consumption in "real life" as opposed to the VAT world. In some instances, these two events will take place simultaneously, *e.g.* a meal in a restaurant or access to a fair. In such circumstances, the place of the use and enjoyment may be considered by tax administrations as a proxy to ascertain the appropriate payment of the tax (see the section on the destination principle below), but this does not mean that the use and enjoyment is taxed as such.

VAT in cross-border trade

Destination principle *versus* origin principle. The features of the VAT system allow the tax to keep its neutrality in cross-border trade because the *destination principle* is applied. According to this principle, which is the international norm, exports are exempt with refund of input taxes (that is, "free of VAT"[3]) and imports are taxed on the same basis and with the same rates as local supplies. This implies that the total tax paid in relation to a supply is determined by the rules applicable in the jurisdiction of its consumption and therefore all revenue accrues to the jurisdiction where the supply to the final customer occurs.

Sales tax systems, although they work differently in practice, also set out to tax consumption of goods, and to some extent services, within the jurisdiction of consumption. Exported goods are usually relieved from sales tax to provide a degree of neutrality for cross-border trade. However, in most sales tax systems, businesses do incur some irrecoverable sales tax and, if they subsequently export goods, there will be an element of sales tax embedded in the price.

The destination principle contrasts with the *origin principle*[4] according to which each jurisdiction would levy the VAT on the value created within its own borders. This means that exporting jurisdictions would tax exports on the same basis and at the same rate as local supplies while importing jurisdictions would give a credit against their own VAT for the hypothetical tax that would have been paid at the importing jurisdiction's own rate. Tax paid on a supply would then reflect the pattern of its origins and the aggregate revenue would be distributed in that pattern. This would run counter to one of the core features of VAT: as a tax on consumption, the revenue should accrue to the jurisdiction where the final consumption takes place. Under the origin principle these revenues are shared amongst jurisdictions where value is added. In addition, as a neutral tax the total amount of VAT collected should not be influenced by the economic or geographical structure of the value chain. However, under the origin principle this amount reflects the various rates applicable in countries where value is added.

The application of the destination principle, although it is more consistent with the main VAT principles and is accepted as the international norm, is not without its own difficulties. First, as already noted, the usual way of implementing this principle for VAT involves exemption of exports, which means that goods and services circulate free of tax in cross-border trade. The possibilities of fraud are evident. Second, the way it is actually implemented across countries is different which can, in some instances, lead to double taxation or unintended non-taxation and create uncertainties for both business and tax administrations. This issue is becoming increasingly important as globalisation allows greater development of cross-border trade and economic integration.

Cross-border trade in goods. In the cross-border trade in tangible goods, the destination principle works well because it is underpinned by the filtering role of Customs. Exported goods are free of VAT (and are freed of any residual VAT via successive taxpayers' deductions of input tax), whilst imports are subject to the same VAT as equivalent domestic goods. The VAT on imports is generally collected at the same time as customs duties, although in some countries collection is postponed until declared on the importer's next VAT return. Deduction of the VAT incurred at importation, in the same way as input tax deduction on a domestic supply, ensures neutrality and limits distortion in relation to cross-border trade.

Within the European Union, which abolished internal customs barriers and tax frontiers in 1993, the system of intra-Community delivery (exempt in the goods' country of origin) and intra-Community acquisition (taxed in the country of destination) performs the filtering role that operates in normal imports/export regimes.

However, this system does not always ensure the absence of any distortion. For example, double taxation issues may arise in cross-border trade of second hand goods since the goods that have been taxed once in the jurisdiction of export (logically without right to deduction of input tax by the final consumer) are taxed a second time in the jurisdiction of import. Such double taxation may not be consistent with to the VAT principles. In domestic trade, some jurisdictions have solved the issue by implementing a margin tax scheme but the issue remains for cross-border trade. Double taxation can also arise when goods are bought or imported in a jurisdiction by a foreign taxpayer, which is not established or registered there. This is the case for example when a foreign business requires a local producer to produce washing machines, which are subsequently exported. This production requires the local manufacturing of moulds that remain the property of the foreign business. These moulds are destroyed after production is finished. Since those moulds are never exported from the jurisdiction of production, they are taxed in that jurisdiction but the foreign taxpayer is unable to recover that input tax since it is not registered there, nor is it required to be registered. This tax is then embedded in the basis for taxation in the country where the washing machines are imported. This creates an element of double taxation, which may not be consistent with the VAT principles. To avoid this double taxation, some jurisdictions ensure that mechanisms are in place to allow foreign businesses to recover the tax or to avoid VAT being charged on those transactions (see Chapter 2).

Cross-border trade in services and intangibles. Applying the destination principle to supplies of services and intangible products[5] is more difficult. The nature of services and intangibles is such that there are no customs controls that can confirm their exportation or impose the VAT at importation. According to the staged payment process, the supplier should account for the tax in the jurisdiction where the service or the intangible property is consumed. However, the operation of this principle would be extremely difficult in practice: registration of suppliers in every single jurisdiction where their supplies are consumed would prove extremely burdensome, if not impracticable. In addition, it is often not easy for the supplier to determine where services and intangibles are likely to be consumed, in particular in an increasingly globalised environment.

The solution developed in most jurisdictions consists of identifying the place of consumption by reference to proxies. The nature of those proxies and the way they are used vary widely across jurisdictions since they result from local history and legal frameworks.

The rules of the European Union. From 1 January 2010, new rules have been introduced to ensure that place of taxation rules for VAT on services are adapted to current communication technologies and market developments. According to the VAT Directive (Council Directive 2006/112/EC of 28 November 2006), the place of taxation depends on the status of the customer receiving the service and, for a number of exceptions, on the nature of the service supplied.

The supply of services between businesses (B2B services) is in principle taxed at the customer's place of establishment. However, if those services are provided to a fixed establishment of the taxable person in another place, the place of taxation for those services shall be the place where that fixed establishment is located. It is interesting to note that this rule associates two different approaches: a proxy (customer location) and consumption (service "provided to"). Such an association is probably due to the perceived need to protect against fraud. This rule applies to both intra-EU supplies (between different Member States) and supplies to and from non-EU countries. Services supplied to final consumers (B2C services) are in principle taxed where the supplier is located.

However, several exceptions have been introduced for both B2B and B2C services according to their nature. For example, services connected to immovable property are taxed where the immovable property is located; services relating to cultural, artistic, sporting, scientific, educational, entertainment and similar activities are taxed at the place where those services are physically carried out. Specific exceptions also apply to B2C supplies only, such as electronically supplied services provided by non-EU suppliers: these are taxed at the place where the customer resides or has a permanent address. Television broadcasting and telecommunications services supplied by non-EU suppliers are taxable at the place where the private customer effectively uses and enjoys the service. From 1 January 2015 onwards, B2C telecommunications, broadcasting and electronically supplied services provided by suppliers established in the EU will be taxed at the place where the customer resides or has a permanent address. As a result, EU and non-EU suppliers will then be placed on an equal footing as regards the place of taxation for such services and, hence, the VAT rates applicable.

The rules beyond the European Union. Although the EU model has been adopted by a large number of countries in Europe, it should be borne in mind that other systems are in place. The New Zealand GST (adopted in 1986) for example involves a different approach, based on the residence of the supplier. The place of taxation for supplies made by non-residents is presumed to be outside New Zealand, except when the service is physically performed in New Zealand (by the provider or by someone else) and the recipient is either a final consumer or a registered business who has agreed to have the transaction treated as being made in New Zealand. In contrast, the place of taxation for supplies by residents is presumed to be New Zealand, unless the supply is a zero-rated export of services. As a result, "the broad inclusion of supplies by resident suppliers necessitates fairly extensive zero-rating rules and the list of zero-rated services includes most situations where consumption is likely to take place offshore" (Millar, 2007). These services include international transport and related services; services physically performed outside New Zealand; services supplied to a non-resident who is outside New Zealand at the time the services are performed (provided that it is not reasonably foreseeable that the services will be provided to a person in New Zealand); services directly in connection with land or goods located outside New Zealand and supplies in relation to intellectual property rights for use outside New Zealand. Unlike the EU approach (which determines the place of taxation by reference of the nature of the supply and the status of the customer) the New Zealand approach results from a combination of proxies such as location of the provider; location of the customer; relationship with the tangible world (goods or land); intended use of the supply and physical performance. However, "the

European and New Zealand models use a similar range of proxies for identifying the place of taxation. What differs is the way they combine these proxies, the order of application, and the priority given to each proxy" (Millar, 2007).

In the Australian GST approach, supplies are taxable in Australia when they are "connected with Australia". According to that proxy, supplies of services performed in Australia, provided through an Australian enterprise, or consisting of rights to receive supplies in Australia are considered to be potentially taxable in Australia. To prevent GST applying to services not consumed in Australia, the Australian GST law includes broad, proxy-based zero-ratings ("GST-free") similar to those used in New Zealand. Australia's most significant variation from the New Zealand GST is its extensive application to non-residents, who may be required to remit GST for services performed in Australia, irrespective of whether their customer is a registered business or a final consumer. Similarly, services supplied from Australia to a non-resident cannot be zero-rated if the services are delivered to another person (whether a business or a consumer) in Australia. Further to a report issued in 2009 by the Australian Board of Taxation, the Government has agreed to make amendments to the Australian GST cross-border rules with effect from 1 July 2012. Notably, the rules will be amended to limit the circumstances where supplies of goods, services and intangibles by non-residents will require them to register for GST in Australia.

At first sight, the approach of the EU VAT Directive and those of the tax laws in New Zealand and Australia seem different. The VAT Directive apparently provides "universal" principles for the allocation of the tax base between the member states and with the rest of the world, based on the nature of the supplies and the status of the customer, whereas the tax laws in Australia and New Zealand rely on concrete proxies for connecting supplies with their own jurisdiction. However, in practice, these approaches are not that dissimilar. One of the main objectives of the EU VAT Directive is to provide a legislative framework for avoiding conflicts on the jurisdiction where cross-border supplies are taxed, both within the EU and with third countries. It is up to each Member State to transpose the Directive into its national law in order to obtain the appropriate tax result. The practical implementation of the Directive into national law is often made through the definition of concrete place of taxation proxies, which are quite close in nature to those employed in Australia and New Zealand (place were the supplier and/or the customer are established; place where the goods or land are located; physical performance).

These examples (and there are many others) show that, although all OECD countries (and beyond) attempt to implement the destination principle, the practical approaches for such implementation can be somewhat different, creating areas for potential double taxation, unintended non-taxation and uncertainties for both business and tax administrations. These issues were considered serious enough to require remedies (OECD, 2005) and the OECD's Committee on Fiscal Affairs agreed that work should be undertaken to develop internationally agreed approaches. OECD Guidelines on these issues are currently being developed (see Chapter 2).

Reverse charge. Making exports free of VAT and taxing imports introduce a breach in the staged collection process. In most countries where an invoice credit method is used, tax on services and intangibles provided from abroad are usually collected by the so-called *reverse charge mechanism*. Normally, taxpayers that deliver services in countries where they are not established have to register for VAT purposes and fulfil all VAT obligations in that country. To avoid such administrative burdens on foreign providers, the reverse charge mechanism allows (or sometimes requires) the VAT-registered customer to account for the tax on supplies received from foreign traders. Generally, when the recipient uses the input for VAT taxable outputs, the amount of tax is deductible so that this does not lead to any actual payment to the tax authorities. However, the reverse charge mechanism is not applied in all jurisdictions and, where it is implemented, the rules may differ across countries. The reverse charge mechanism also implies a difference of treatment for sales to domestic and foreign customers and has a cash-flow impact as, when applied, it avoids the customer having to pay the VAT to the supplier before being able to deduct it in its tax return. It is clear that the reverse charge mechanism is not appropriate for business-to-consumer supplies.

Neutrality in cross-border trade. The general principles underpinning neutrality described above also apply to cross-border trade. In principle, the rules applicable to cross-border supplies should not produce a tax advantage for comparable domestic transactions. The application of the destination principle, including the refund or credit of the tax incurred by businesses on exports, ensures there is no unfair competitive advantage afforded to domestic businesses, hence customer choice is not distorted.

However, there are inevitably a number of cases where supplies made to foreign businesses will not be free of tax so that they will incur VAT in a jurisdiction where they are neither established nor registered. Normally, the right to deduction of VAT is exercised by reducing the net tax payable. However, when foreign businesses incur VAT on business expenditures in a jurisdiction where they are not registered (or required to be registered) for VAT, this process cannot be applied. Many countries ensure, at least in theory, that foreign businesses are not discriminated against compared to domestic businesses and they have developed approaches to ensure foreign businesses do not incur irrecoverable VAT, which would not be incurred by domestic businesses. There is no standard approach for applying this principle in practice; these depend on the legal and administrative traditions of each country.

It is also true that tax administrations legitimately impose specific compliance requirements on foreign businesses. Indeed, dealing with foreign businesses with no "legal" presence in a jurisdiction inevitably brings an element of risk and appropriate measures are developed to protect against fraud or avoidance. However, in practice, the compliance burden involved with such specific rules may constitute a form of unjustified discrimination against foreign businesses. The OECD undertook a survey in 2007 of more than 300 businesses in 33 countries (OECD, 2010 a). The outcomes showed that the issue was serious enough to deserve remedies. As a result Guidelines on Neutrality were developed and further work is being done on ways to minimise excess taxation in cross-border trade (see Chapter 2).

Consumption taxes on specific goods and services

In the OECD nomenclature, taxes on specific goods and services (5120) include a range of taxes such as excises, customs and import duties, taxes on exports and taxes on specific services. *Consumption Tax Trends* focuses on excise duties only.

A number of general characteristics differentiate excise duties from value added taxes:

- They are levied on a limited range of products.

- They are not normally liable to tax until the goods enter free circulation, which may be at a late stage in the supply chain.
- Excise charges are generally assessed by reference to the weight, volume, strength or quantity of the product, combined in some cases, with *ad valorem* taxes.

Consequently, and unlike VAT, the excise system is characterised by a small number of taxpayers at the manufacturing or wholesale stage.

As with VAT, excise taxes aim to be neutral internationally. As the tax is normally collected when the goods are released into free circulation, neutrality is often ensured by holding exports under controlled regimes (such as bonded warehouses) and certification of final export (again under controlled conditions) by Customs. Similarly, imported excise goods are levied at importation although frequently the goods enter into controlled tax-free regimes until released into free circulation.

Excise taxes may cover a very wide range of products like salt, sugar, matches, fruit juice or chocolates. However, the range of products subject to excise has declined with the expansion of general consumption taxes. Excise taxes on alcohol, tobacco and hydrocarbon oils continue to raise significant revenues for governments.

There has been a discernible trend in recent decades to ascribe to these taxes characteristics other than simply revenue raising. A number of excise duties have been adjusted with a view to discouraging certain behaviours considered harmful, especially for health reasons. This is particularly the case for excise duties on tobacco and alcohol (so-called "sin taxes") whose rates have been increased in such a way they aim to reduce consumption of these products. The structure of certain excise duties has also gradually changed to encourage more responsible behaviour towards the collective welfare, especially the environment. This is the case for taxes on fuels, cars and other products which produce environmentally harmful emissions.

Such a trend can be regarded as a change in tax policy of governments. Governments have long been conscious that the tax system has an influence on the decisions of firms and individuals. They know the impact of the tax system on employment, business formation and expansion, and consumption patterns and thus have generally tried to raise revenues without distorting consumption patterns or inhibiting investment decisions. Many of the same ideas can be used in the field of environmentally related taxation; however, a goal of environmentally related taxation is to skew consumption and production patterns and reduce the size of the tax base, which is quite different from the goals of most types of taxation (OECD, 2010b). Wider work has been undertaken by the OECD on the impact of taxation on the environment and a full report was issued in 2010 (OECD, 2010b).

Notes

1. For ease of reading, all value added taxes will be referred to as VAT in this chapter.
2. At the time of going to press Estonia, a member state of the EU, was about to become the 34th member of the OECD.
3. "Free of VAT" may be termed zero-rated, exempt with credit, or some other local terminology depending on the jurisdiction. Whatever the description used, the effect should be the same – no VAT is added by the supplier but the supplier is entitled to input tax credits, to the extent that the jurisdiction allows, in respect of such supplies.

4. This should be distinguished from the term used in the EU for a proposed system (but never implemented) in which the VAT would have been collected by the member state of origin and the revenue later channelled to the member state of destination for transactions within the EU.
5. Unlike in the European Union, where there are just two categories of supplies (goods and services) for VAT purposes, some OECD countries have other categories such as intellectual property rights and other intangibles. For ease of reference these are referred to as "intangible products".

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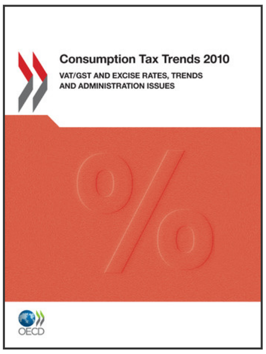

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