

## ANALYSIS OF ETHYL ALCOHOL EXCISE EXEMPTION ACCORDING TO EXCISE LAW

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### ABSTRACT:

*Ethyl alcohol or EA is one of the types of excisable goods stipulated in the current Indonesian Excise Law. Excise revenue from ethyl alcohol is very small when compared to total state revenue from the excise sector. This occurs because in Indonesia, ethyl alcohol is a separate entity as an excisable goods which differs from alcoholic beverages or MMEA. Excisable goods which are in Indonesia referred to as ethyl alcohol in other countries are better known as spirits. Spirits or what is often referred to as "alcohol" with certain conditions "whether denatured or not", will get excise exemption facilities if it is to be used not as a beverage. The main objective of this qualitative research is to clarify the position of ethyl alcohol as an excisable goods, although the definition of ethyl alcohol in the Excise Law often overlaps with spirits as MMEA. The inclusion of ethyl alcohol as an excisable good is primarily not for state revenue, but as an instrument for controlling these goods, so that they are not misused to produce alcoholic beverages. The study results also suggest redefining all excisable goods in the form of alcoholic products in future amendments to the Excise Law.*

**Keywords:** *ethyl alcohol, spirits, excise, excise exemption, alcohol products*

## 1. INTRODUCTION

According to Law No. 11 of 1995 on Excise which was later amended by Law No. 39 of 2007, ethyl alcohol or ethanol is one of the goods subject to excise. However, when compared to the two other excisable goods, namely tobacco products and beverages containing ethyl alcohol, excise revenue from this commodity is relatively small in value. This small state revenue from ethanol is since most of these commodities receive excise-free facilities, either through unimposing of the excise or the excise-exemption.

In many countries, the excise tax on alcohol products is generally divided into three categories, namely beer which is a malt fermented alcoholic beverage, fermented alcoholic beverages other than beer (for example wine, sake, cider, etc.), and other alcohol products such as distilled alcohol from fermentation products and ethyl alcohol obtained from chemical synthesis. On the other hand, Indonesia only divides the excise tax on alcohol products into two categories, namely “ethyl alcohol or ethanol, regardless of the materials used and the manufacturing process” and “beverages including concentrates containing ethyl alcohol in whatever strength regardless of the materials used and the manufacturing process”. Beverages containing ethyl alcohol in Indonesian are often abbreviated as MMEA while ethyl alcohol is abbreviated as EA.

The current regulation of excise on alcohol products is a substitute for the previous rules, which are based on the two legacy ordinances of the Dutch East Indies, namely the *1931 Beer Excise Ordinance* and the *1898 Distilled Alcohol Excise Ordinance*. If we re-read these two ordinances, we will know that the excise regulations in these two sources are already in line with best practice in many countries.

The transformation process of classifying excisable goods in the form of alcohol products from the old ordinance to the new Excise Law which only divides alcohol products into two, namely EA and MMEA, often causes unclear parameters for distilled products "when the distilled product is called MMEA and when it is included in the EA category". This lack of clarity has an impact on the implementing regulations for the Excise Law, including regulations that manage excise exemptions in the form of a Regulation of the Minister of Finance and a Regulation of the Director-General of Customs and Excise.

The purpose of this paper is to provide a critical analysis of several regulations concerning the exemption of ethyl alcohol excise which is contained in the articles in the

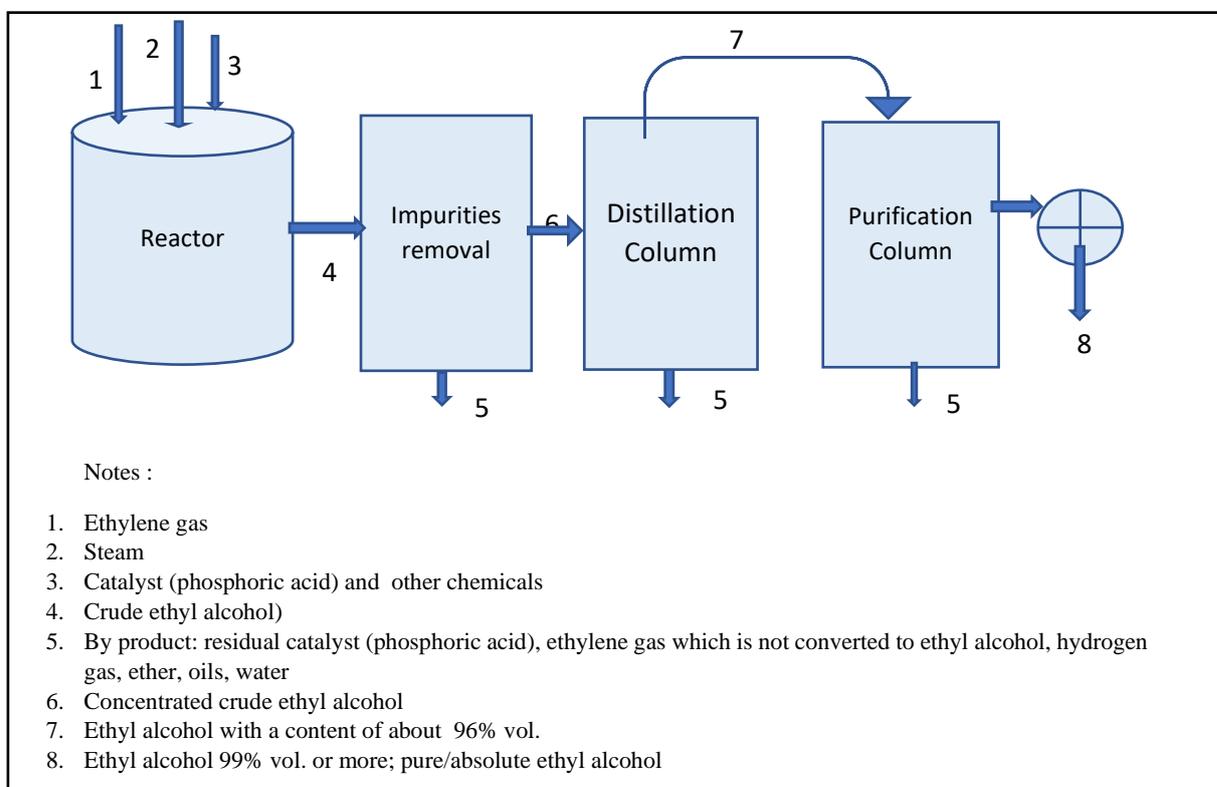
Excise Law and Regulation of the Minister of Finance (PMK) and the Regulation of the Director General of Customs and Excise (Perdirjen Bea Cukai). The results of the analysis are expected to be used as a reference for decision-makers in the preparation of excise exemption regulations for the short term (PMK and Perdirjen Bea Cukai) and the long term (amendments to the Excise Law).

## 2. LITERATURE REVIEW

### 2.1 Ethyl Alcohol

The definition of ethyl alcohol or ethanol according to the Encyclopedia Britannica (2021) is a member of a class of organic compounds that are given the general name alcohols and its molecular formula is  $C_2H_5OH$ . Ethyl alcohol can be obtained from the distillation process of fermented products whose raw materials come from agricultural commodities such as sugar cane, cassava, corn, etc., or through chemical synthesis such as hydration of ethylene gas. How to produce ethyl alcohol in outline can be seen in Figure 1 and Figure 2 below (simplification of the flowsheet by the author).

Figure 1. Simplified flow sheet for the manufacture of ethyl alcohol from ethylene gas

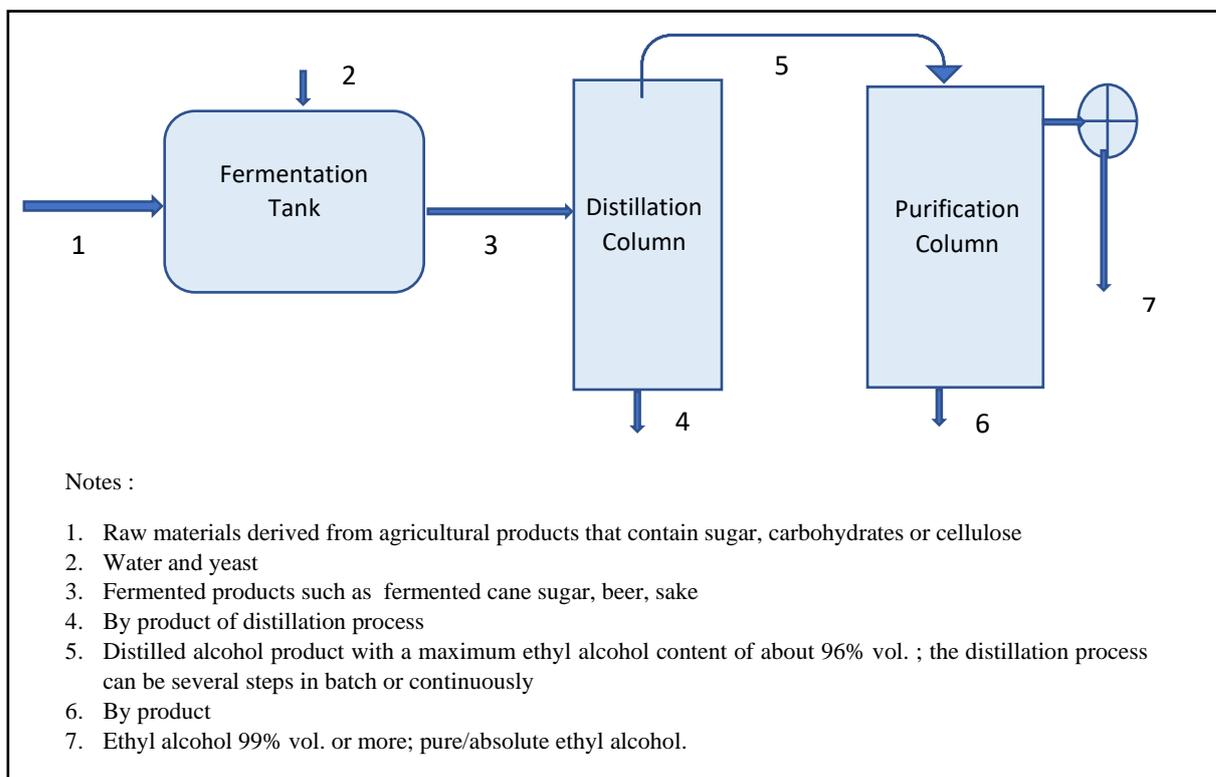


Source: Compiled by author form Equistar (2003).

In accordance with Figure 1, ethyl alcohol obtained from this process in crude form, or which has undergone a process of removing impurities is non-food grade ethyl alcohol so that it cannot be used as a ready-to-drink product or used as raw material or auxiliary material for making alcoholic beverages. Considering that this type of ethyl alcohol is not suitable for drinking directly or as raw material for alcoholic drinks, the status/classification of this item as an EA type of excisable goods is clear.

The classification of goods according to the Harmonized System (HS) of ethyl alcohol of this type "resulting from chemical synthesis" is included in heading 2207 if it has an alcoholic strength by volume of 80% vol. or higher and at heading 2208 if it has an alcoholic strength by volume of less than 80% vol.

Figure 2. Simplified flow sheet for the manufacture of alcoholic beverages and ethyl alcohol from agricultural products



Source: Compiled by author form various sources.

In accordance with Figure 2, the main stages of the manufacturing process are fermentation using yeast and continued by distillation and finally passes the purification process if needed. The results of this fermentation process are usually in the form of fermented alcoholic beverages, for example, beer is derived from fermented barley/malt, wine comes from the fermentation of grapes, sake comes from fermented rice, etc. The

fermented alcoholic drinks contain protein and some congeners “as secondary constituents”. These congeners are unique to each raw material and are usually composed of higher alcohols, esters, aldehydes, acids, etc.

If we distill these fermented products, we will get distilled alcoholic beverages or *spirits*. Some examples of these types of beverages are whiskey from beer distillation, brandy from the distillation of wine, and *ciu* “traditional alcoholic drink in Indonesia” derived from sugar cane molasses distillation product.

If the distillation process continues until the secondary constituents are almost completely removed, *neutral spirits* will be obtained. The limit on the ethyl alcohol content in neutral spirits differs in some countries but is usually 95% vol. or 190 proof. Since the mixture of ethyl alcohol and water has azeotropic properties, the maximum content of ethyl alcohol obtained by this distillation is only about 96% vol. To obtain pure ethyl alcohol, we need another process after distillation. One example is through the process of adsorption using molecular sieves.

The results illustrated in Figure 2 can be either alcoholic beverages or other alcoholic products. Alcoholic beverages and ethyl alcohol are included in Chapter 22 HS which are divided into 6 headings starting from heading 22.03 to heading 22.08. The first four headings, “22.03 to 22.06”, are headings for various types of alcoholic beverages obtained from the fermentation process while the last two headings, “22.07 and 22.08”, are for alcoholic products obtained from the distillation or other purification process whether used as alcoholic beverages or not.

Heading 22.07 is for ethyl alcohol of an alcoholic strength by volume of 80% vol. or higher; ethyl alcohol and other spirits, denature, of any strength. When we interpret this heading, we conclude that this heading is intended for ethyl alcohol which is not suitable for drinking due to the alcohol content is too high” not suitable for drinking directly” or has been denatured.

Heading 22.08 is for undenatured ethyl alcohol of an alcoholic strength by volume of less than 80% vol. and spirits, liqueurs, and other spirituous beverages. If we interpret this heading, then we conclude that this heading contains alcoholic drinks obtained from the distillation process of fermented products and ethyl alcohol which is not a beverage with an alcohol content below 80% vol. This heading also allows accommodating all kinds of ethyl alcohol products with levels of alcohol content less than 80% vol. that is

not suitable for drinking “does not mean denatured ethyl alcohol” or undenatured ethyl alcohol used as raw material and/or auxiliary material in making alcoholic beverages.

## **2.2 Denatured Ethanol**

In Encyclopedia of Food and Health (Bekatorou, 2016), the term 'denatured alcohol' refers to alcohol products adulterated with toxic and/or bad tasting additives (e.g., methanol, benzene, pyridine, castor oil, gasoline, isopropyl alcohol, and acetone), making it unsuitable for human consumption. The most common additive used is methanol (5–10%), giving rise to the term 'methylated spirits.'

The uses of denatured alcohol are very diverse, such as disinfectants, camping stove fuel, pest control, woodworking, etc. Ethanol that will be used not for consumption as a beverage or raw material for beverages will usually be granted excise duty by mixing it with other ingredients approved by the customs and excise authorities.

## **2.3 Ethanol excise exemption in some countries.**

To obtain exemption from excise on ethanol, it can be pursued by denaturing the ethanol with certain ingredients. The materials used must be approved by the government authority. The following is an example of several ethyl alcohol excise exemptions, which include the denaturation of ethanol in three selected countries, namely: Canada, the United States, and the United Kingdom. The reason for choosing these three countries is because they already have comprehensive rules when compared to regulations in developing countries.

### **2.3.1 Canada**

The Canadian Excise Law (Excise Act, 2001) states that denatured alcohol (DA) and specially denatured alcohol (SDA) are made by mixing spirits with denaturants with the aim that these spirits cannot be drunk, usually used for various industrial purposes. The law also mandates to control/supervise the production of denatured alcohol, there is even strict supervision over the ownership, supply, import, and disposal of specially denatured alcohol.

Furthermore, spirits is defined as any material or substance containing more than 0.5% absolute ethyl alcohol by volume, excluding wine, beer, vinegar, DA, SDA, fuel oil, or other residues produced as a result of the distillation process or other formulations

that approved. Any product that contains or is made from beer, vinegar, DA, SDA, fuel oil, or other residue produced (as a result of the distillation process or approved formulations) that cannot be consumed as a beverage is also exempted from the definition of spirits.

The formulation of DA and SDA submitted by the manufacturer/factory must be approved by the Government. Examples of denaturants for making DA and SDA are methyl alcohol, toluene, ethyl acetate, naphtha solvent, isopropyl alcohol, acetone, formaldehyde solution, chloroform, iodine, and pine tar.

### **2.3.2 The United States**

The Alcohol and Tobacco Tax and Trade Bureau (TTB) “under the US Department of Treasury” classifies denatured alcohol into three categories: *completely denatured alcohol*, *specially denatured alcohol*, and *specially denatured rum*. The definition of *alcohol* according to Written Comments on Certain Tariff and Trade, Volume 99, Issue 11, September 16, 1985, is “*the spirits known as ethyl alcohol, ethanol, or spirits of wine, from whatever source or by whatever process produced*”. The term does not include such spirits as whiskey, brandy, rum, gin, or vodka. While *rum* is defined as *any spirits produced from sugar cane products and distilled at less than 190 proof in such manner that the spirits possess the taste, aroma, and characteristics generally attributed to rum*.

Completely denatured alcohol (CDA) is alcohol that must be completely denatured only according to the prescribed formula (alcohol plus denaturants and/or odorants or perfumes materials). Denaturants used may be added a little odorant, rust inhibitor, or dye. Any such additions must be done only with the approval of the TTB officer in charge. The request for approval must be submitted to the TTB officer in charge.

Odor or fragrance ingredients may be added to denaturants permitted for CDA in an amount of not more than 1 part up to 250, by weight. However, the addition may not decrease the denaturation value or change the chemical or physical constants outside the specified limits for these denaturants as stipulated by regulations, except for odors. The factory owner of distilled spirits who uses the denaturant that has added the odor or fragrance must inform the TTB officer who handles it, in writing, about the name and nature of the odor or fragrance ingredients used.

Example of a CDA formula: for every 100 gallons of ethyl alcohol not less than 195 proof (97.5% vol) is mixed/destroyed with as much as 2.0 gallons of unleaded gasoline, rubber hydrocarbon solvent, kerosene, deodorized kerosene, alkylate, ethyl tertiary butyl ether, high octane denaturant blend, methyl tertiary butyl ether, naphtha, natural gasoline, raffinate, or a combination thereof; or as much as 5.0 gallons of toluene.

***The drawback on taxpaid distilled spirits used in manufacturing non-beverage products***

The provisions in this section apply to the manufacture of drugs, medicinal preparations, food products, flavourings, flavouring extracts, and perfumes that are not suitable for beverage use and are made from distilled alcohol/distilled spirits for which the tax/excise has been paid. The regulations cover the following topics: how to obtain tax/excise drawbacks on distilled alcohol used in the manufacture of non-beverage products; and guarantees, claims, formulas and samples, losses, and records that must be kept in connection with the manufacture of non-beverage products.

***Tax-free alcohol***

Tax-free alcohol is undenatured alcohol that is used for non-drink purposes in scientific research and drug use by educational organizations, hospitals, laboratories, etc. The use of tax-free alcohol needs to be regulated to prevent illegal diversion to the use of taxable beverages.

**2.3.3 United Kingdom**

Denatured alcohol in the UK is grouped into 3 (three) categories namely: (a) *Completely Denatured Alcohol (CDA)*, (b) *Industrial Denatured Alcohol (IDA)*, and (c) *Trade Specific Denatured Alcohol (TSDA)*. CDA must be prepared according to the following formulation: with every 90 parts by volume of the alcohol mixture 9.5 parts by volume of wood naphtha or its substitutes and 0.5 parts by volume of crude pyridine/crude pyridine, and to the resulting mixture the mineral naphtha (petroleum) is added in the proportion of 3.75 liters for every 1000 liters of the mixture and synthetic organic dye (methyl violet) in the proportion of 1.5 grams for every 1000 liters of the mixture.

Besides, CDAs that have been made in EU member countries, following the CDA formula of that member country, must be received in the UK without tax. The CDA

formulations approved for all member states are specified in Commission Regulation (EC) No. 3199/9.

Before July 1, 2013, the CDA formulation included methyl violet dye. Recording of dyes is no longer mandatory in CDA-prescribed formulations. However, some users may still want to include a purple dye. The purple dye can be added if needed and the mixture will still be treated as CDA. Also, denatured alcohol, which is not a CDA, which has been prepared in EU country according to the formulation of that member country and has been added to products that are not for human consumption, must be received in the UK without excise.

IDA is a denatured class of alcohol designed for industrial use. Consists of 95 parts by volume of alcohol and 5 parts by volume of wood naphtha, or a substitute for wood naphtha. The TSDA formulation is a denatured type of alcohol approved to meet specific trade requirements. There are currently 12 approved TSDA formulations, all with different specific uses.

***Ethyl Alcohol for medical and scientific purposes***

Ethyl alcohol for medical use as well as for scientific use (for example for laboratory analysis, school/university learning purposes) is also exempt from excise. The excise exemption here does not include ethyl alcohol used for washing equipment (e.g., laboratory equipment). To get an exemption from excise for this washing activity, denatured ethyl alcohol must be used.

***Ethyl Alcohol/spirits for manufacturing use.***

For manufacturing purposes, there is no definite list of permitted uses and will be considered in each case based on the benefits. In general, spirits will be exempt for: the manufacture of a related product or process in which the distilled alcohol/spirits acts as a catalyst, or where the distilled alcohol is converted into other substances; spirits for the manufacture of ethyl esters and ethyl ether; spirits is involved in the manufacturing process where denatured alcohol (DA or SDA) is shown to be incompatible or detrimental to the process. To obtain excise exemption, of course, the producer must be able to prove that the use of denatured alcohol is inappropriate because it has an adverse effect in certain processes so that the authorities are confident in providing an exemption for the alcohol used. Each case of an application for exemption will be examined based on its merits, and

if the excise exemption is granted, strict controls on the storage of the duty-free spirits and record-keeping requirements are imposed.

*Ethyl alcohol used as an auxiliary ingredient in the food industry, flavoring essence, perfumery, or toilet preparation or perfume.*

In principle, spirits for the food industry, essence, toilet preparation, and perfume are not exempted from excise, except for the manufacture of vinegar.

#### **2.4 Ethyl alcohol excise duty exemption under the Distilled Alcohol Excise Ordinance**

##### **Stbl. No. 90, 27 February 1898 and its amendments.**

Under article 5 of the Ordinance and Government Regulations governing it, distilled alcohol that is granted duty-free facilities includes:

- a. denatured distilled alcohol that is unfit for drinking;
- b. distilled alcohol for scientific purposes;
- c. distilled alcohol which is used as auxiliary material or raw material to make products that will be designated in government regulations (other than goods in letter d);
- d. methyl alcohol, fusel oil, amyl alcohol, butyl alcohol, and propyl alcohol determined to be used as raw materials or auxiliary materials for handicraft companies as mixing materials for other goods.

Denatured distilled alcohol that is unfit for drinking includes methylated spirits (*brand spiritus*) which are made by mixing distilled alcohol with a minimum content of 85% by volume with methanol in a certain ratio (determined by the Minister of Finance) or by other means stipulated by the Minister of Finance. Distilled alcohol used solely for scientific purposes may be exempt from excise if it has a content of at least eighty-five percent by volume. The excise exemption granted is personal and non-transferable.

Exemption from excise on refined alcohol is also granted for refined alcohol which is intended as an auxiliary or raw material for the manufacture of final products such as vinegar, glycerin soap or translucent soap, iodine or bromium preparations, sulfur ether, ether chlorine, confectionery, vitamin preparations, etc.

## 2.5 Exemption from Excise on Ethyl Alcohol According to the Excise Law and its Regulations.<sup>1</sup>

The giving of excise free refers to two articles in the Law, namely article 8 (Unimposing of the Excise) and article 9 (Exemption from Excise). The granting of excise free on ethyl alcohol for the first type is with the facility of unimposing of the excise referring to Article 8 paragraph (2) letter d which states that the excise is also not imposed on Excisable Goods if the goods are to be used as raw or auxiliary materials for manufacturing the finished Excisable Goods. This paragraph is usually used for ethyl alcohol/EA (e.g. EA with 96% by volume) to be used as MMEA (for example Vodka with EA content of 42% by volume). Both EA and MMEA are excisable goods.

The second type of ethyl alcohol excise free is based on the Exemption from Excise facility which refers to article 9. Some of the paragraphs in this article that are widely used are:

- Article 9 paragraph (1) letter a which state that exemption from excise may be granted for Excisable Goods that are used as raw or auxiliary materials for manufacturing finished goods not subject to excise;
- Article 9 paragraph (1) letter b which states exemption from excise may be granted for Excisable Goods that are required for research and scientific development;
- Article 9 paragraph (2) letter a which states exemption from excise may also be granted for certain Excisable Goods, namely completely denatured ethyl alcohol that is unfit for drinking. In the explanation of this paragraph, it is stated " Completely denatured ethyl alcohol that is unfit for drinking" means ethyl alcohol, which is denatured by using certain denaturants, it is known as "brand spiritus".

## 2.6 Data of Unimposing of the Excise on Ethyl Alcohol (EA) and Exemption from Excise on Ethyl Alcohol (EA)

Following is a table of data on unimposing of the excise facilities (Table 1) and data on facilities for exemption of excise on EA (Table 2). Unimposing of the excise

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<sup>1</sup> To make it easier for the reader to interpret the terminology in the Indonesian Excise Law and the regulations under it in the form of the Minister of Finance Regulation and the Regulation of the Director General of Customs and Excise, the author translates *mencampur/dicampur* with "denature/denatured" and *merusak/dirusak* with "denature completely/completely denatured". These two terms are used for excise exemption on ethyl alcohol.

facilities are provided for EAs to be used as raw materials or auxiliary materials in the manufacture of final goods which are excisable goods, while the excise exemption facility for EA is granted if EA will be used as raw materials or auxiliary materials in the manufacture of final goods, not an excisable item.

Table 1. Unimposing of the excise on EA 2018-2020 (in liters)

Year	For tobacco products	For alcoholic beverages
2018	3,883,903	19,377,970
2019	3,106,531	21,585,386
2020	3,611,084	24,892,518

Source: Director General of Customs and Excise, Ministry of Finance.

Table 2. Excise exemption on EA 2018-2020 (in liters)

Year	Non denatured ethyl alcohol	Completely denatured ethyl alcohol for Brand Spiritus	Others denatured ethyl alcohol : SDA-BIT6, SDA-IPA5, SDA EAC 2 and denatured EA for fuel oil	Non denatured ethyl alcohol for foodstuff (essence, flavouring, cooking wine, etc)
2018	33,733,459	2,116,265	68,727,578	4,721,040
2019	35,631,661	3,514,970	65,819,963	5,706,160
2020	43,168,110	3,479,670	175,475,655	5,476,231

Source: Director General of Customs and Excise, Ministry of Finance.

### 3. RESEARCH METHODS

The research method used is a qualitative by descriptive-interpretive approaches through several stages, i.e.:

1. The current condition, which aims to map the current condition as a baseline. The data required is secondary data obtained from literature studies and other sources such as data obtained from the Directorate General of Customs and Excise (DGCE).
2. Identification of objectives and needs with the aim of knowing the aims and objectives of the proposed regulation under existing conditions, without having to violate existing laws and regulations.
3. Benchmarking, looking at practices in other countries where spirits/ethanol are positioned as excisable goods and how to obtain ethanol excise tax exemption.

#### 4. ANALYSIS AND DISCUSSION

##### 4.1 The Definition of Ethyl Alcohol or EA According to Law Number 11 of 1995 Concerning Excise as Amended by Law Number 39 of 2007

As stated by the explanation of article 4 paragraph (1) letter a, *ethyl alcohol or ethanol is defined as a liquid, clear and colorless goods, which is an organic compound with the chemical formula C<sub>2</sub>H<sub>5</sub>OH, which is obtained either by fermentation and/or distillation or by chemical synthesis.* In our opinion, this explanation makes the meaning of ethyl alcohol as an excisable goods more limited than what is meant in the body of the law as stated in article 4 paragraph (1) letter a which states that *excise is imposed on ethyl alcohol or ethanol, regardless of the materials used and the manufacturing process.* This article does not limit the ethyl alcohol content or the color of ethyl alcohol. Regardless of the ethyl alcohol content, color, or method of manufacture, these are excisable goods.

According to Appendix II of Law 12/2011 concerning the Formation of Legislative Regulations, *the explanation* has the function of being the official interpretation of the legislators of certain norms in the body. Therefore, the explanation only contains descriptions of words, phrases, sentences, or equivalent words/foreign terms in the norm which can be accompanied by examples. Explanation as a means of clarifying norms in the body must not confuse the norm in question.

The explanation of the definition of ethyl alcohol, would be more appropriate if we add the sentence in the pure or absolute state after the word ethyl alcohol so that the explanation becomes *ethyl alcohol or ethanol in the pure or absolute state is a liquid, clear and colorless substance, is an organic compound with the formula chemical C<sub>2</sub>H<sub>5</sub>OH, obtained either by fermentation and/or distillation or by chemical synthesis.* This change in definition is necessary if the excise amendment will still use the terminology ethyl alcohol as an excisable goods so that there is no question from the common people "*is a liquid with 90% ethyl alcohol content by volume mixed with a blue substance still including ethyl alcohol?*".

Currently there are two opinions regarding the function of explanation. The first opinion says that the explanation of articles in the Law is legally binding, while the second opinion says that what is binding as a norm (and can be used as a legal basis) is the articles in the body and not the explanation, since the explanation only functions as an official interpretation of the article contained in the body. This second opinion was supported by

Adi Condro Bawono (2012) in his review entitled "*Fungsi Penjelasan dan Lampiran Perundang-Undangan*" in hukumonline.com.

#### 4.2 International Best Practice for The Position of Ethyl Alcohol as An Excisable Goods

Table 3 below is a list of excisable items for alcohol products in three selected countries compared to Indonesia before 1995 and since 1995.

Table 3. Comparison of excisable goods for ethyl alcohol products in three countries with Indonesia

Canada	USA	United Kingdom	Indonesia	
			Before 1995	Since 1995
- Alcohol (spirits, wine, beer)  Note: Wine is a fermented drink from agricultural or plant products.  There is a denatured alcohol regulation by mixing spirits with a legal denaturant (DA, SDA).	-Beverage Alcohol (Beer, Distilled Spirits, Wine, Sake, etc) -Non-beverage alcohol (Alcohol fuel, Industrial Alcohol, Tax-Free Alcohol)  Note : There is a regulation regarding denatured alcohol which is made by mixing spirits / rum with a legal denaturant (SDA, CDA).	-Beverage Alcohol (wine and made wine, beer,cider and perry, spirits, low alcohol beverages)  Note: There are production, distribution, and use of denatured alcohol which is made by mixing dutiable alcohol/spirits with legally defined denaturant (CDA, IDA, TSDA).	- Beer - Distilled Alcohol	-Ethyl Alkohol/EA -Alcoholic beverages/MMEA

Source: Compiled by author form various sources.

From the Table 3, it can be explained, the imposition of excise on alcohol products is generally divided into two types, namely *fermented drinks* (beer, wine, sake, etc.) and *spirits* (alcohol products obtained either from the distillation process of fermentation products or obtained by other means). Where is the position of ethyl alcohol, which in Indonesia is currently one of the clearly stated excisable goods, while at the international level and in Indonesia before 1995 the term ethyl alcohol as excisable goods were not explicitly stated?

The position of ethyl alcohol both in Indonesia and in other countries will be clear if we start discussing the exemption of excise on alcohol products for purposes other than alcoholic beverages such as for industrial purposes as a raw or auxiliary material (alcohol

or ethyl alcohol is not a final product whether alcohol is denatured or not) or for fuel which will be used directly (denatured alcohol/ethyl alcohol as the final product).

*Ethyl alcohol*, which is separately designated as excisable goods in *Indonesia*, is actually the same as *spirits* in *other countries*. On practical level, *spirits* are divided into two, namely *spirits* which are *alcoholic beverages* such as vodka, brandy, whiskey, and *spirits for industrial purposes* (whether they need to be denatured or not), and spirits that are denatured for direct use. Spirits for industrial use or those to be denatured for direct use must have certain specifications and the minimum content of ethyl alcohol is determined (best practice 170 proof or 85% EA content).

The excise tariff for spirits in other countries depends on the ethyl alcohol content "the higher the ethyl alcohol content, the higher the excise rate". Thus, the tariff for spirits with an ethanol content of 96% will be higher than that of spirits for whiskey (alcoholic beverage) with an ethanol content of about 42%. In practice, spirits with ethanol content of 96% never pay off their duties due to excise exemption facilities. Spirits with this kind of condition will mostly be used as raw materials or auxiliary materials in the manufacture of other goods.

In Indonesia, ethyl alcohol at any level, the excise tariff is IDR 20,000 (USD 1.4) per liter, while the tariff for spirits with an ethyl alcohol content above 20% for domestic production is IDR 80,000 (USD 5.6) per liter. This improper determination of excise rates can lead to fraud "for example by paying excise for EA 96%, then diluting it illegally into 42% Vodka". The vagueness in defining ethyl alcohol and the inaccuracy in determining the excise rate for EA brings consequences for fraud which is quite difficult for law enforcement. As an example, there is an individual who buys 400 liters of 96% ethyl alcohol, whose excise has been paid at retail outlets. Retail outlets have a license to trade EA while individuals do not. It is possible that this individual will use ethyl alcohol as raw material for MMEA

The separation of ethyl alcohol (EA) from alcoholic beverages (MMEA) as a separate excisable goods entity, brings a consequence of a separate article in the Excise Law which regulates unimposing of the excise which is different from the excise exemption article, although the essence of these two articles is the same. Ethyl alcohol which will be diluted as MMEA will get unimposing of the excise facility, "not excise exemption facility".

#### 4.3 Exemption of Excise on Ethyl Alcohol According to Law Number 11 of 1995 Concerning Excise as Amended by Law Number 39 of 2007

The exemption of excise on ethyl alcohol which will be discussed here<sup>2</sup> is the exemption of excise which refers to article 9 paragraph (1) letter a and article 9 paragraph (2) letter a. According to article 9 paragraph (1) letter a, exemption from excise may be granted for Excisable Goods that are used as raw or auxiliary materials for manufacturing finished goods not subject to excise. Thus, ethyl alcohol which will be used to make final products such as medicines, foodstuffs, paint thinners, hand sanitizers, etc. will get an exemption from excise.

In implementing this article, in principle, there are two conditions for the treatment of EA. The first condition is that the EA needs to be denatured so it is “*not good for drinking*”. Examples of final products are thinners, disinfectants, paints, etc. The second condition is EA without denaturation as raw materials or supporting materials for making finished goods. The end product can be vitamins, medicines, pharmaceutical products, or other products.

The two conditions above are contained in the Minister of Finance Regulation (PMK) Number 109/PMK.04/2010 concerning Procedures for Excise Exemption which has been amended twice with PMK Number 40/PMK.04/2014 and Number 172/PMK.04/2019 as well as in several the Director General of Customs and Excise Regulation (Perdirjen Bea Cukai). The latest is Perdirjen Bea Cukai Number 17/BC/2018.

According to the latest Perdirjen Bea Cukai, there are currently only four denatured EA formulations, e.g. SDA BIT 6 (Ethyl Alcohol denatured with Bitrex 6 ppm), SDA IPA 5 (Ethyl Alcohol denatured with Isopropyl Alcohol 5%), SDA EAC 2 (Ethyl Alcohol denatured with Ethyl Acetate 2%), and Ethanol denatured Fuel Oil.

If we look at the construction of this paragraph, then we see that the EA treatment that has not been denatured will be the same as the EA treatment that has been denatured, which is still both excisable goods so that the administration, documentation, and

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<sup>2</sup> The term ethyl alcohol is denatured so that it is not suitable or unfit for drinking in international best practice. It is used for both completely denatured alcohol and other denatured alcohol, for example specially denatured alcohol. But in the Indonesian Excise Law, *completely denatured alcohol* that is *unfit for drinking* only mentions goods with the name *brand spiritus*. So that in the minister of finance regulation, which is the implementation rule of the Excise Law, denatured ethyl alcohol which will be used as raw material or auxiliary material for manufacturing finished good is not subject to excise using the term “*denatured ethyl alcohol*” so it is *not good for drinking*”.

supervision processes in transportation to the final product factory are the same. Article 9 paragraph (2) letter a states that exemption from excise may also be granted for certain Excisable Goods, namely *completely denatured ethyl alcohol* that is *unfit for drinking*. In the explanation, this item is limited only to the *brand spiritus*.

Thus the explanation narrows down the norms mentioned in the article. In international practice completely denatured ethyl alcohol is often referred to as methylated spirits and the commodity type is not only *brand spiritus*. In Perdirjen Bea Cukai Number 53/BC/2012, the number brand spiritus formulations is set at only one, so that this Perdirjen Bea Cukai further narrows the meaning of the norms contained in the article of the Law.

### **Case Study**

PT XXY makes a brand spiritus/methylated spirits by denaturing ethyl alcohol with denaturants methanol, methylene blue, and premium gasoline. To make a brand spiritus, the company had obtained prior permission from the local Customs and Excise Service Office. Based on an audit conducted by the Directorate of Audit, DGCE, the company is required to pay its excise and administrative sanctions because the methylated spirits formulation produced by the company is different from the formulation stipulated in the Director General of Customs and Excise Regulation which requires denaturants in the form of methanol, methylene blue, and kerosene. Excise and administrative fines that must be paid more than Rp.115 billion. To get rid of this bill, the company made various efforts, either through an objection process or an appeal to the Tax Court, but they were unsuccessful.

In our point of view, this is something that is not quite right because when applying for the process of making brand spiritus, the company had obtained prior permission from the local Customs and Excise Service Office. In our opinion, the Customs and Excise Service Office considers kerosene and premium an equivalent material because they all come from petroleum products. The only difference between premium and kerosene is their range of boiling point. This will not happen if the Director General Regulation also opens up opportunities for denaturing materials including other petroleum products such as aviation fuel, gasoline, naptha, etc.

The transportation of both denatured and completely denatured alcohol has been strictly regulated, treated the same as the transportation of excisable goods that have not

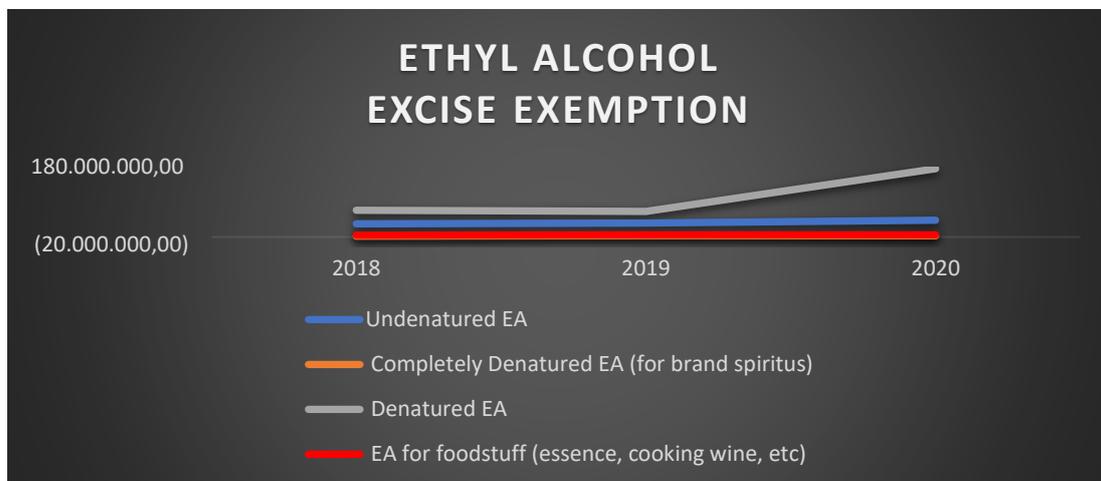
paid excise, even though both are actually no longer suitable for drinking. The reason behind this strict rule is because it is feared that both types of goods can be refined back into ethyl alcohol.

In our opinion, denatured ethyl alcohol and completely denatured alcohol should be excluded from excisable goods, and for transportation it is better to use a different packaging or label than undenatured ethyl alcohol. By excluding these commodities as excisable goods, the administrative burden on DGCE will be significantly reduced. As a comparison, in the Canadian Excise Law, all denatured alcohol has been removed from the definition of spirits because they cannot be drunk directly, even though they can be used as raw materials or auxiliary materials for non-excisable goods.

#### 4.4 Analysis Data Excise Free on EA

Applications for ethyl alcohol excise duty exemption "through a denaturation process using denaturant bitrex (SDA-BIT6)" in 2020 increased very sharply (Figure 3). This can be estimated because 2020 is the year of the Covid-19 pandemic so that the need for alcohol-based hand sanitizers and disinfectants is also increasing sharply.

Figure 3. Volume of Ethyl Alcohol that is exempted from excise based on its intended use



Source: Director General of Customs and Excise, Ministry of Finance.

#### 4.5 Opportunity to Increase Excise Revenue From EA

Compared to other excisable goods, the excise revenue from EA is very small, so that many people think that ethyl alcohol should be excluded as excisable goods. In our point of view, this opinion is misleading because the designation of EA as an excisable goods is mainly not as state revenue, but because these goods must be controlled due to they are easily misused as raw material for alcoholic beverages. Apart from that, there is

an inaccuracy in the division of alcoholic products as excisable goods. We should follow international best practices that what we call as “ethyl alcohol” actually *spirits* in other countries.

The definition of an item subject to excise in our country is sometimes confusing. For alcohol products, DGCE relies too much on other agencies such as the Food and Drug Administration (BPOM) and other technical ministries. For example, DGCE never clearly defined "cooking wine". In many countries cooking wine is subject to excise when the salt and sugar levels have not passed a certain level. In Indonesia, when a product is labeled "Arak Masak " or "Ang Ciu" or "Cooking Wine" from the BPOM, DGCE tends not to impose excise on the product even though the method of making cooking wine and its composition is identical or similar to MMEA. In Indonesia, most of the Ang Ciu is made from fermented rice plus ethyl alcohol without any clear parameters what the minimum salt or sugar content is. Because cooking wine in Indonesia is not considered an excisable item, the producer of cooking wine is granted exemption from excise on EA used as raw or auxiliary material.

In the UK, alcohol/spirits for foodstuff, perfume, toilet preparations are not exempted. Indonesia can imitate the UK to increase excise revenue from ethyl alcohol. In our opinion, ethyl alcohol to be used for foodstuffs should still be subject to excise because we will consume the finished goods for food and this is not against the Indonesian Excise Law. Following is the data on EA excise revenue for the last 3 years and the opportunity for additional excise revenues if the EA for foodstuffs does not get excise exemption (Table 4).

Table 4. Excise revenues on EA 2018–2020 and potential additional revenues

Year	Volume of the EA that pays excise (liter)	Excise Revenues (billion IDR)	Volume of the EA for foodstuffs , excise exemption (liter)	Potential Additional Excise Revenues (billion IDR)
2018	7,059,647	141.1930	4,721,040	94.4208
2019	6,018,425	120.3685	5,706,160	114.1232
2020	11,578,867	231.5774	5,476,231	109.5246

Source: Director General of Customs and Excise, Ministry of Finance.

## 5. CONCLUSION AND SUGGESTIONS

Based on the description and discussion above, we conclude and suggest the following points:

1. The simplification of excisable alcohol products into only two types of goods namely MMEA and EA has the consequence of not being clear in classifying alcohol made from the distillation process: when they are referred to as MMEA and when they are called EA. In future amendments to the Excise Law, we recommend that definitions of alcohol products be explained more clearly by using references to international best practice or the Harmonized System Convention.
2. The number of denatured alcohol and completely denatured alcohol formulations for the purpose of exempting ethyl alcohol excise as stipulated in the Regulation of the Director General of Customs and Excise (Perdirjen Bea Cukai) is currently very limited. The small number of formulations causes narrowing of the meaning of the norms stipulated in the body of the Excise Law. We suggest that the number of formulations needs to be increased so that it will be very beneficial for the development of various kinds of products that require ethyl alcohol as a raw or auxiliary material.
3. Exemption from excise on ethyl alcohol for food products such as cooking wine, essence, and flavoring for foodstuffs should not need to be approved because we will consume these foods and the ethyl alcohol mixed in food products or essence/flavoring is not completely lost. By not exempting the EA excise on foodstuffs, it will increase state revenue in the EA excise sector.

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