

Fuel tax changes

In the 2003–4 Budget, the Government proposed changes to the excise (and customs duty) on some fuels. On 16 December 2003, the Government announced changes to these proposals. This Research Note sets out how the Government now proposes to tax certain fuels.

Background

In March 2001, the Government announced the [Fuel Taxation Inquiry](#). It was established following sharp petrol price rises that coincided with the introduction of the goods and services tax, and decisions related to fuel including the abolition of the indexation of excise rates to changes in the consumer price index.

The Inquiry recommended, among other things, that excise (and customs) duty should apply to all liquid fuels and liquefied and/or compressed natural and petroleum gases, and the rates to apply should be based on the relative energy content of each fuel (except aviation fuels and greases). Table 1 shows what rates would be if they were based on energy content.

Table 1: Excise rates based on the energy content (cents per litre)

Fuel	Rate now	Energy content based excise	Difference
Diesel	38.1	38.1	0.0
Petrol	38.1	33.8	-4.3
LPG	0.0	25.9	25.9
Ethanol	0.0	23.1	23.1

Source: Fuel Taxation Inquiry Report, p. 110. Note: the energy content of a

fuel measured as the ratio of the energy content of diesel. Energy content-based rates based on 38.143 cents per litre for low-sulphur diesel. Ethanol rate is with the production subsidy (see below).

Table 1 shows that, compared to current rates, the recommendations would have resulted in a decrease in the excise on petrol and an increase for ethanol and liquefied petroleum gas (LPG).

Budget proposals¹

In the 2003–4 Budget, the Government proposed that excise-exempt fuels—LPG, compressed natural gas (CNG) and liquefied natural gas (LNG)—be subject to excise. The Government also proposed changing the taxation of ethanol. It is now subject to an excise and a production subsidy, both of 38.143 cents per litre, thus reducing the effective excise rate to zero. The Government proposed that the excise rates on exempt fuels and the effective rate on ethanol be increased in five steps beginning 1 July 2008. Final rates would be effective from 1 July 2012. Biodiesel would be treated similarly to ethanol.² Final rates would have regard to energy content.³ The Government did not, however, say at the time what the final rates would be.

Criticisms

Criticisms of these proposals came from two main sources. The first was based on the claim that imposing excise on exempt fuels would reduce their use. In particular, the industry that converts car engines from petrol to LPG use

was concerned that it would suffer. The second source was environmental groups who claimed that taxing 'alternative' fuels—such as ethanol and biodiesel—was contrary to the Government's policy of encouraging their use.

Revised proposals

In response to criticism from bodies such as the [Australian Liquefied Petroleum Gas Association](#), on 16 December 2003, the Government announced changes to the Budget proposals. The changes are:

- a banded excise system will be adopted with different rates for high, medium and low energy fuels
- excise on (low-sulphur) diesel and petrol will remain at the current rate of 38.143 cents a litre⁴
- the excise on alternative fuels will be half the rate that would apply if excise were levied on energy content
 - the final rate for LPG and ethanol will be 12.5 cents per litre, and 19.1 cents for biodiesel
- excise will not be levied on domestic use (for example, for heating and cooking) of gaseous fuels such as LPG, and
- business use of LPG, CNG and LNG in non-transport applications (for example, power generation) will be also effectively excise-free.

The Government also announced adjustment assistance for the LPG car conversion industry. From 1 July 2008 (when excise on LPG will be 2.5 cents per litre) the Government will provide a \$1000 subsidy, for three years, to buyers of a dedicated or dual-fuel LPG vehicle delivered new.⁵

Table 2 sets out the proposed final rates.

Table 2: Current and final excise rates (cents per litre)

Fuel	Excise now	Final rate	Change
Diesel	38.1	38.1	0.0
Petrol	38.1	38.1	0.0
LPG	0.0	12.5	12.5
Ethanol	0.0	12.5	12.5
Biodiesel	0.0	19.1	19.1

Table 2 shows that, compared to current rates, the proposals would increase the excise on LPG, ethanol and biodiesel.

Comments

Several aspects of the proposals are noteworthy.

As noted, alternative fuels are to be subject to excise at half of the rate that would apply if excise were levied on energy content. The 50 per cent 'discount' seems to be arbitrary and has been reported to bear the hallmarks of a political compromise.⁶ Nor do the final rates seem to be related to the [rates for the energy grants credits scheme](#). Rather, it appears that, for reasons of administrative simplicity, the Government has decided to set the final rate for LPG and ethanol at the same level of 12.5 cents per litre. (Setting final rates for LPG and ethanol at half the energy-based rates would have yielded rates of 13.0 and 11.6 cents per litre respectively).

The final rates diverge from the energy-based rates as shown in Table 3.

Table 3: Energy content-based and final excise rates (cents per litre)

Fuel	Energy content based excise	Final rate	Difference
Diesel	38.1	38.1	0.0
Petrol	33.8	38.1	4.3
LPG	25.9	12.5	-13.4
Ethanol	23.1	12.5	-10.6

The most notable feature of Table 3 is that if the excise on petrol were based on energy content, it would be 4.3 cents per litre lower than the final rate. The final rates on LPG and ethanol bear little relationship to their energy content-based rates.

The current rate of excise on diesel and petrol came into effect on 2 March 2001. The final rates on these fuels are not scheduled to come into effect for more than eight years. Hence more than eleven years will have elapsed between the time when the current rates came into effect and when the final rates become operative. Inflation has already reduced the real value of the excise on diesel and petrol: if the rate had been increased in line with the consumer price index, it would have been around 40.8 cents per litre at 30 September 2003. Under the Government's proposals, the real value will fall even further.

Conclusions

The proposals, as they now stand, are a mixed bag. On the one hand, they will have the positive effect of reducing the discrimination that now exists in favour of excise-exempt fuels. The Fuel Taxation Inquiry concluded that the use of fuel tax concessions to encourage the production and use of alternative fuels has significant resource allocation effects that can no longer be justified.⁷ The Inquiry further noted that the existence of industries, such as the LPG car conversion industry, is based on this artificial tax advantage.⁸

More generally, the proposals appear to do little to advance the

objective of a more consistent approach to fuel taxation. In particular, the proposals do not meet the criterion of taxing fuels on a neutral basis such as their relative energy content.

1. The proposals are discussed more fully in Richard Webb, 'Fuel Taxation Proposals', *Current Issues Brief*, no. 2, Parliamentary Library, 2003–04.
2. On 11 September, the Government introduced the *Energy Grants (Cleaner Fuels) Scheme Bill 2003* to effect its decision with respect to biodiesel.
3. Budget Paper No. 1, 2003–04, p. 1–22.
4. The excise on high-sulphur diesel is 40.143 cents per litre.
5. Prime Minister, Hon. John Howard, *Fuel excise reforms*, media release, 16 December 2003, and Minister for Transport and Regional Services, Hon. John Anderson, *Excise decision boosts regional Australia*, media release A163/2003, 16 December 2003.
6. A. Crabb and O. Guerrero, 'Compromise on LPG, ethanol excise', *The Age*, 17 December 2003.
7. *Fuel Taxation Inquiry Report*, March 2002, p. 42.
8. *ibid.*, p. 22.

Richard Webb Economics, Commerce and Industrial Relations Group Information and Research Services

Views expressed in this Research Note are those of the author and do not necessarily reflect those of the Information and Research Services and are not to be attributed to the Parliamentary Library. Research Notes provide concise analytical briefings on issues of interest to Senators and Members. As such they may not canvass all of the key issues. Advice on legislation or legal policy issues contained in this paper is provided for use in parliamentary debate and for related parliamentary purposes. This paper is not professional legal opinion.

© Commonwealth of Australia
ISSN 1328-8016