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Diesel Fuel Rebate Scheme Amendment Bill 2002

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I N F O R M A T I O N A N D R E S E A R C H S E R V I C E S

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No. 147 2001-02

Diesel Fuel Rebate Scheme Amendment Bill 2002

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24 May 2002

Contents

Purpose	1
Background	1
Basis of policy commitment	2
Position of significant interest groups	2
Pros and cons	3
Main Provisions	5
Concluding Comments	5
Endnotes	6

Diesel Fuel Rebate Scheme Amendment Bill 2002

Date Introduced: 16 May 2002

House: House of Representatives

Portfolio: Treasury

Commencement: Day of Royal Assent

Purpose

To extend eligibility for rebate of the excise on diesel under the Diesel Fuel Rebate Scheme (DFRS) to retail and hospitality businesses that use diesel to generate power when they do not have access to mains electricity.

Background

The DFRS provides a full rebate of excise and customs duty on diesel (and like fuels¹) used off-road for particular activities. Since 1 July 2000, the use of diesel in the following activities has been eligible for rebate subject to certain exemptions:

- in mining operations (otherwise than for the purpose of propelling any vehicle on a public road)
- in primary production (otherwise than for the purpose of propelling a road vehicle on a public road)
- in rail transport (otherwise than for the purpose of propelling a road vehicle on a public road) in the course of carrying on an enterprise
- in marine transport (otherwise than for the purpose of propelling a road vehicle on a public road) in the course of carrying on an enterprise
- at residential premises to generate electricity used in providing food and drink, lighting, heating, air-conditioning, hot water or similar amenities for, or meeting other domestic requirements of, residents of the premises at a hospital or nursing home or at any other institution providing medical or nursing care or at a home for aged persons.

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Current rebate rates are 38.143 cents per litre (cpl) for diesel and 7.557 cpl for like fuels.

Legislative authority for the DFRS is section 78A of the [Excise Act 1901](#), section 164 of the [Customs Act 1901](#), and the regulations under those Acts. The Australian Taxation Office administers the scheme.

The scheme's origins lie in the time when fuel excise revenue was earmarked to fund road construction. All diesel used off-road was exempt from excise. However, this (Exemption Certificate Scheme) was abused. To halt the abuses, the Fraser Government, in the 1982 Budget, announced that the exemption would be abolished and a rebate paid in its place for the off-road use of diesel in certain activities.²

A feature of this scheme and subsequent variants was that the scheme did not apply to all off-road activities. The scheme thus discriminates in favour of some activities and against others. In 1998, the Government—under *A New Tax System* (ANTS)—announced its intention to extend the scheme to include all off-road business use of diesel. However, following negotiations with the Australian Democrats to have the Senate pass the ANTS legislation, the scheme was extended to only rail and marine transport. Further, a full rebate was extended to activities that were previously eligible for only partial rebate, eg mining and residential activities. The scheme was also extended to include rebates for like fuels. So the situation remains that some activities are eligible for rebate but others are not.

Basis of policy commitment

The second reading speech states that the Bill:

... gives effect to a policy initiative announced by the Government during the 2001 election campaign...

This policy, as set out in *Securing Australia's Tourism Future*, states:

Another measure which will help tourism operators is the extension to the Diesel Fuel Rebate Scheme. A re-elected Coalition Government will extend the eligibility for the Diesel Fuel Rebate Scheme to small retail/hospitality businesses producing their own electricity from diesel, provided there is no access to grid power. Businesses such as caravan parks, tourist resorts and road houses will benefit from the Scheme which will cost \$80 million over four years.

Position of significant interest groups

As noted, the DFRS is selective in that only some activities are eligible for rebate. Industries that use diesel in off-road activities but are not eligible have, not surprisingly, sought to have the scheme extended to include their activities. This is evident in some of the [industry submissions to the Fuel Taxation Inquiry](#). For example, the Association of Marine Park Tourism Operators argued for:

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- extending eligibility under the DFRS to diesel acquired by Bareboat charter operators in the course of their business
- the expansion of concessions to remote power generation for resort operators without access to alternative energy sources, and
- the expansion of the concessions to include petrol used in marine vessels in situations that are identical to those where the existing diesel fuel rebate operate.

Pros and cons

The anomalies, administrative complications, and incentives to which selectivity of activities gives rise are described in the Department of Transport and Regional Services' [submission to the Fuel Taxation Inquiry](#):

The existing arrangements maintain diesel tax for business users in some sectors. Under the DFRS where some industries, such as construction, are required to pay significantly more for diesel used off-road than most other industries, there are also incentives to misreport fuel usage to avoid fuel tax. Misreporting, fuel mixing with solvents (eg toluene) and fuel substitution (eg use of heating oil as transport fuel) are some examples. The development of new fuels may create additional opportunities for fuel mixing/substitution – both legal and illegal - to take advantage of differences in excise rates between sectors and fuels.

The application of off-road rebates to some sectors and not others also results in anomalies. For example, diesel for domestic electricity generation is rebated (under DFRS), but if members of small communities combine to more efficiently generate electricity they are no longer eligible for the rebate. The rebate which they pay goes towards funding the Remote Renewable Power Generation Program (administered by the Australian Greenhouse Office) which is designed to subsidise the purchase of renewable power generating facilities in off-grid communities. Under the way in which Program money is allocated, however, not all communities who pay excise will benefit from the Program in the form of subsidies for renewable energy infrastructure.

The DFRS also raises equity issues. For example, the costs of running power generation for small mixed retail businesses in isolated regions not connected to the power grid are significant, and excise imposts can further disadvantage already isolated and poorly serviced communities.

In recognition of this, the Government has made a commitment to extend the DFRS to small retail/hospitality businesses producing their own electricity from diesel, provided there is no access to grid power. It is intended that businesses such as caravan parks, tourist resorts and road houses will benefit from the extension.

Rail uses diesel or electricity almost exclusively. It currently receives the full rebate of fuel tax under the DFRS for fuel used off-road. However, diesel usage in rail terminals is not rebated despite terminals not being part of publicly maintained road networks. Most rail operators also operate and maintain terminals to transfer goods

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from rail to road for collection by the customer. This requires them to maintain separate records of diesel usage on rail and in terminal (eg for operation of fork-lifts and other equipment to transfer containers from trains to trucks), adding to administration costs.

The Department would encourage the Inquiry to consider the merits of extending off-road business fuel tax rebates on diesel to those sectors and off-road activities that do not currently benefit from rebates.

The anomalies in the DFRS also distort the allocation of resources. As Treasury noted in its [submission to the Fuel Taxation Inquiry](#):

There are a number of anomalies within the current DFRS which mainly revolve around industries that remain ineligible for the rebate. For instance mining operations are eligible for a rebate while quarrying and dredging are not; electricity generation at commercial premises is not covered, although private premises are; and manufacturing and construction industries continue to remain ineligible. The DFRS also discriminates between activities within an industry.

Due to the anomalies within the current scheme, the overall effects of the DFRS on resource allocation are varied. The DFRS assists in removing the distortionary effects of excise on eligible activities that use diesel (and 'like' fuels) as an intermediate input, which has a positive effect on resource allocation. But due to the anomalies outlined above, the DFRS also contributes to the inefficient allocation of resources between industries. The discrimination between industries and activities within an industry result in non-eligible industries and activities not being compensated for the negative effects of excise on their intermediate inputs. In addition, the DFRS also distorts resource allocation as it provides a price incentive to use diesel (or 'like' fuels) over petrol (and other fuels not covered).

In short, while the proposed extension of the DFRS to retail and hospitality businesses would remove some of the scheme's anomalies, the extension does not address other anomalies. Consequently, the scheme will continue to discriminate among and within industries. A less piecemeal approach to the DFRS than contained in this Bill would address remaining anomalies. Such an approach is contained in the [Fuel Taxation Inquiry](#), whose main recommendations the [Government rejected](#). Among the reasons the Government gave for its decision are:

- taxing fuels on their relative energy content would violate its election commitment to maintain excise exemptions for fuel ethanol and biodiesel
- acceptance of the recommendations would violate the Government's undertaking with the Australian Democrats to restrict full rebates to certain classes of on and off-road use, and

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- the Government would not terminate the Fuel Sales Grants Scheme and the Petroleum Products Freight Subsidy Scheme because they assist consumers in regional and remote areas.

Main Provisions

Schedule 1

Proposed clauses 1 and 6 respectively amend the *Customs Act 1901* and the *Excise Act 1901*. These clauses contain identical wording and define eligibility conditions. The clauses provide that where a business ('enterprise'), whose principal function is retailing or the provision of hospitality, uses fuel to generate electricity used in the business and that business does not have access to mains electricity ('commercial supply of electricity'), that business is eligible to receive a full rebate. However, **proposed clause 3** defines retail sale to exclude the retail sale of electricity. Paragraph 1.7 of the Explanatory Memorandum indicates that this clause was inserted to exclude businesses, whose principal function is to sell electricity, from being defined as a retailer to ensure that they are ineligible to claim a rebate.

Proposed clauses 2 and 7 respectively amend the *Customs Act 1901* and the *Excise Act 1901*. These clauses also contain identical wording, and provide that the amount of the rebate is the same as if retailers and hospitality providers were primary producers.

Sections 164AC(5) of the *Customs Act 1901* and 78AD(5) of the *Excise Act 1901* deal with the audit of diesel fuel rebate applications. **Proposed clauses 4 and 9** respectively amend these sections and empower an officer to examine the premises of retail and hospitality businesses claiming a rebate. However, the officer can examine residential premises only with the occupant's consent and only if the rebate relates to fuel bought for use at the premises.

Proposed clauses 5 and 10 limit the availability of the rebate to fuels bought on or after 1 July 2002.

Concluding Comments

This Bill is an example of 'fiddling at the edges' policy. By rejecting the recommendations of the Fuel Taxation Inquiry, the Government has passed up an opportunity to bring long-overdue rationality to fuel taxes. The financial press has been critical of the Government's rejection of the Inquiry's recommendations.³ The Government intends to replace the DFRS and the Diesel and Alternative Fuels Grants Scheme with the Energy Grants (Credits) Scheme (EGCS).⁴ The objectives of the EGCS, as set out in the *Diesel and Alternative Fuels Grants Scheme Act 1999*, are:

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The purpose of the Energy Grants (Credits) Scheme will be to provide active encouragement for the move to the use of cleaner fuels by measures additional to those under this Act, while at the same time maintaining entitlements that are equivalent to those under this Act and the Diesel Fuel Rebate Scheme, including for the use of alternative fuels.

The proposed introduction of the EGCS on 1 July 2003 could provide an opportunity to address some of the anomalies in the DFRS.

Endnotes

- 1 Like fuels attract a lower rate of excise than diesel.
- 2 For further background, see 'Petrol and Diesel Excises', Department of the Parliamentary Library, *Research Paper* No. 6, 2000-01, at <http://www.aph.gov.au/library/pubs/rp/2000-01/01RP06.htm>
- 3 'Fuel tax fiasco must be fixed', *Australian Financial Review*, 21 May 2001, p. 70.
- 4 The commitment to introduce an EGCS is contained in the *Measures for a Better Environment* statement of May 1999.

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