



## Fuel Tax Bill 2006

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## Fuel Tax Bill 2006

**Date introduced:** 29 March 2006

**House:** House of Representatives

**Portfolio:** Treasury

**Commencement:** 1 July 2006

### Purpose

To implement a system of credits to offset—partially or fully—the excise that some taxpayers pay on fuels, and to lay the groundwork for extending the tax net to alternative fuels.

### Background

Most fuels are subject to both excise (when the fuel is produced in Australia) or customs duty (when the fuel is imported) and to the goods and services tax (GST). The Fuel Tax Bill 2006—the Bill—relates only to excise and customs duty. The relevant Acts for the imposition of excise are the [Excise Act 1901](#) and the [Excise Tariff Act 1921](#) and, for customs duty, the [Customs Act 1901](#) and the [Customs Tariff Act 1995](#).

The Bill in large measure continues the [Energy Grants Credits Scheme](#) (EGCS) whose legislative authority is the [Energy Grants \(Credits\) Scheme Act 2003](#). However, the Bill extends the remit of the EGCS to include additional fuels and business activities.<sup>1</sup> The EGCS—which came into effect on 1 July 2003—provides grants for business use of:

- diesel and like fuels in [eligible off-road activities](#) (the ‘off-road’ component), and
- diesel and alternative fuels used to transport passengers or goods on [eligible trips](#) (the ‘on-road’ component).<sup>2</sup>

The grants allow users to recover, fully or partially, excise (and customs duty) on fuels. The Australian Taxation Office, which administers the EGCS, publishes the [grant rates](#) on its website.<sup>3</sup>

The purpose of the off-road component seems primarily to be to reduce costs for key sectors, notably agriculture and mining. The purpose of the on-road component is:

... to reduce transport costs, particularly for regional and rural Australia where costs are more pronounced ...<sup>4</sup>

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The on-road component is thus a subsidy to regional areas. For environmental reasons, the on-road use of diesel in vehicles under 20 tonnes wholly in urban areas is generally not eligible.

The EGCS replaced the Diesel Fuel Rebate Scheme (DFRS) and the Diesel and Alternative Fuels Grants Scheme (DAFGS). With some changes, the DFRS became the off-road component of the EGCS and the DAFGS the on-road component. The DAFGS arose from the Government's undertakings under its [Measures for a Better Environment](#) program.<sup>5</sup>

The EGCS has several deficiencies.

First, it discriminates among activities. Agricultural activities are particularly favoured. For example, all on-road trips made as part of a primary production business are eligible. No other industries benefit from this concession, which is an implicit subsidy to primary production.

Second, the EGCS discriminates among fuels: there is one list of [eligible fuels](#) for road transport activities and another for 'other' activities.<sup>6</sup> Further, the scheme discriminates among fuels used in road transport; for example, the grant for the on-road use of diesel is 18.51 cents per litre but there is no grant for petrol. Alternative fuels are excise-exempt (for example, liquefied petroleum gas) or are effectively excise-free (for example, ethanol and biodiesel) and receive an on-road credit to maintain pre-GST price relativities between petrol and diesel.

Finally, the EGCS is complicated, and this imposes compliance and administration costs on business and the Australian Taxation Office. For example, in the on-road scheme, eligibility depends on the vehicle's gross vehicle mass (GVM) and the trips it undertakes. All vehicles over 20 tonnes are eligible for a grant. In the case of vehicles that are at least 4.5 tonnes but less than 20 tonnes GVM, eligible trips are those from a point outside a metropolitan area to another point outside a metropolitan area, or from a point outside a metropolitan area to a point inside a metropolitan area (or vice versa). Trips from one point inside a metropolitan area to another point inside that metropolitan area are not eligible.

## Basis of policy commitment

The Bill is a key element in proposed broader reforms to fuel taxes. The reforms include establishing long-term excise (and customs duty) rates on fuels, taxing currently untaxed fuels, and a new system for credits for tax paid on fuels. The Bill implements the fuel tax credits system. The Bill does not implement the proposed excise (and customs duty) rates or the amounts of the fuel tax credits.

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The Bill's proposals include replacing, on 1 July 2006, all existing rebates and subsidies—including the EGCS—with a single system of fuel tax credits. There are two components to the existing system whereby the amount of excise or customs duty is reduced. The EGCS is the main component; in 2005–06, spending on the EGCS is estimated to be more than \$3.7 billion.<sup>7</sup> The other component is remissions, refunds and rebates of excise (and customs duties), which the *Explanatory Memorandum* describes as follows:

1.15 Section 78 of the *Excise Act 1901* allows remissions, rebates and refunds of excise duty in prescribed circumstances and subject to prescribed conditions and restrictions. A similar provision is contained in the *Customs Act 1901*.

1.16 A remission is a mechanism that allows holders of a remission certificate to obtain prescribed fuel products fuel tax-free for use in prescribed circumstances. Remission and refunds commonly relate to solvent and burner fuel applications, kerosene for some specific fuel uses, and diesel and petrol substitutes for non-fuel uses.<sup>8</sup>

## Reform announcements

The Government has made four announcements about the reform of fuel excise rates and fuel tax credits:

- in the 2003–04 Budget, the Government outlined the reforms<sup>9</sup>
- on 16 December 2003, the Prime Minister elaborated on the Budget announcement<sup>10</sup>
- in March 2004, the Government extended the transition path for fuels becoming subject to excise (see below), and
- on 15 June 2004, the Government released the energy white paper titled [Securing Australia's Energy Future](#) and the accompanying Fuel Excise Reform document.<sup>11</sup>

The white paper proposed a credit scheme to replace the EGCS from 1 July 2006. The [Fuel Tax Credit Reform Discussion Paper](#) that Treasury released on 27 May 2005 elaborated on this proposal.<sup>12</sup>

In a separate but related development, Treasury issued the [Review of the Schedule to the Excise Tariff Act. Industry discussion paper](#).<sup>13</sup> This proposed a wide-ranging review of the *Excise Tariff Act 1921* (discussed below). The *Excise Tariff Act 1921* lists the goods subject to excise (including fuels) and the applicable rates.

## Key features of the proposed reforms

Key features of the proposed reforms are:

- excise will fall into four bands

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- the bands will be based on energy content, namely, high, medium and low; the fourth band is for ‘other’ fuels such as compressed natural gas
- alternative fuels that are now explicitly excise-exempt (liquefied petroleum gas, compressed natural gas and liquefied natural gas) or effectively so (biodiesel and ethanol) will be subject to excise from 1 July 2011.<sup>14</sup>
  - excise on alternative fuels will be phased in. Beginning 1 July 2011, credits will be paid that reduce effective rates below the final rates, which will apply from 1 July 2015
  - the final rates on alternative fuels will be half of what they would be if rates were based on energy content (the so-called ‘discount’ for alternative fuels)
  - grants will continue to apply to alternative fuels under the EGCS until 2010. Beginning on 1 July 2006 and ending on 30 June 2010, the grants will be progressively reduced to zero
- from 1 July 2012, all off-road business use of all fuels will be effectively excise-free
  - this measure will be introduced in stages. A credit of half of the fuel excise incurred in all currently ineligible off-road activities will be available between 1 July 2008 and 30 June 2012; a full credit will be available from 1 July 2012. All fuels, that is, diesel and petrol used in currently eligible activities will receive a full credit from 1 July 2008
- from 1 July 2006, the credit paid to users of diesel in on-road vehicles weighing over 4.5 tonnes GVM will be extended to all excisable fuels
  - the metropolitan boundaries governing eligibility for this credit will be abolished making all journeys in these vehicles eligible for the credit
- the partial excise paid on fuels used in heavy vehicles will be declared an official, non-hypothecated road-user charge (see below) from 1 July 2006, and the charge will be set consistent with future determinations of the National Transport Commission
- all private and business use of all fuels used to generate electricity will be effectively excise-free from 1 July 2006
- the excise currently levied on burner fuels—such as heating oil and kerosene—will be effectively removed from 1 July 2006.

In short:

Under fuel tax reform the effective application of fuel tax will be limited to:

- business use of fuel in on-road applications in motor vehicles with a gross vehicle mass of 4.5 tonnes or less;
- business use on-road in motor vehicles with a gross vehicle mass of more than 4.5 tonnes (with the exception of a carve-out intending to preserve previous entitlements)

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for eligible fuel use in vehicles with a gross vehicle mass of 4.5 tonnes) but only to the extent of the road-user charge;

- for private use on-road in motor vehicles and in certain off-road applications; and
- aviation fuels (where tax is imposed for cost recovery reasons).<sup>15</sup>

The proposed fuel tax credit system is summarised in Table 1.1 in the *Explanatory Memorandum*. This is reproduced as Table 1 below.

**Table 1: Application of fuel tax on 1 July 2012**

	<i>Business use</i>		<i>Private use</i>	
Use on roads	GVM ≤ 4.5 tonnes	Fuel tax payable	Full fuel tax payable	
	GVM > 4.5 tonnes	Fuel tax, payable up to amount of road-user charge, the rest is offset by a fuel tax credit		
Other use	Fuel tax fully offset by fuel tax credit		Electricity generation	Fuel tax fully offset by a fuel tax credit
			Burner applications and non-fuel uses	Effectively fuel tax-free via a fuel tax credit to business suppliers
			Other	Full fuel tax payable

Source: *Explanatory Memorandum*, p. 11.

As noted, alternative fuels that are now explicitly excise-exempt will be subject to excise from 1 July 2011. The Bill seeks to establish the framework for implementing this proposal:

1.17 It is intended that from 1 July 2011, this Bill will also provide the legislative basis for taxing certain liquefied and compressed gaseous fuels, when fuel tax is levied on liquefied petroleum gas, liquefied natural gas and compressed natural gas for the first time.<sup>16</sup>

In the part of the *Review of the Schedule to the Excise Tariff Act* that deals with fuels, it was noted:

The Government's decision in relation to fuel tax reform includes replacing the system of administering excise concessions for business with credits claimable via the Business Activity Statement (BAS), commencing 1 July 2006. As set out by the Treasurer on 15 June 2004, the new business credit system will replace all existing

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rebates and subsidies. In this context, subsidies include concessional and free rates of excise duty. It should be noted that the principles adopted by the Government for reform of fuel taxes apply to all products that are classified in the fuels section of the excise tariff (items 11 and 12). This therefore means that all fuels will be subjected to the full rate of excise (other than aviation fuels and petroleum-based oils), with concessions made available through fuel tax credits.

The Bill picks up the proposals relating to businesses claiming through their Business Activity Statements.

### Proposed excise rates, and credit and effective excise rates on alternative fuels

The following are tables of the:

- proposed fuel excise rates
- fuel tax credit rates that will apply to alternative fuels, and
- the effective excise rates—that is, excise less credit—on alternative fuels.

**Table 2: Fuel excise rates from 1 July 2015**

<b>Fuel type</b>	<b>Energy content (megajoules/litre)</b>	<b>Excise rate (cents/litre)</b>	<b>Discounted rate (cents/litre)</b>
High-energy content fuels: petrol, diesel, gas to liquids, diesel, biodiesel	Above 30	38.143	19.1 (biodiesel)
Mid-energy content fuels: liquefied petroleum gas, liquefied natural gas, ethanol, dimethyl ether	Between 20 and 30	25.0	12.5 (all)
Low-energy content fuels: methanol	Below 20	17.0	8.5 (methanol)
Other: compressed natural gas	Between 38 and 41 (megajoules per cubic metre)	38.0 (cents per cubic metre)	19.0 (cents per cubic metre)

Source: Australian Government, *Securing Australia's Energy Future*, Canberra, 2004, p. 96.

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**Table 3: Alternative fuels credit rates to apply from 1 July 2006 to 1 July 2010 (cents per litre)**

Fuel	1 July 2006	1 July 2007	1 July 2008	1 July 2009	1 July 2010
Biodiesel	14.808	11.106	7.404	3.703	0.000
Ethanol	16.647	12.485	8.324	4.162	0.000
Liquefied petroleum gas	9.540	7.155	4.770	2.385	0.000
Liquefied natural gas	6.504	4.878	3.252	1.626	0.000
Compressed natural gas (cents per cubic metre)	10.094	7.570	5.047	2.523	0.000

Source: Treasury, *Fuel Tax Credit Reform Discussion Paper*, Canberra, 2005, p. 5, and *Explanatory Memorandum*, p.15.

**Table 4: Effective excise rates on alternative fuels from 1 July 2011 (cents per litre)**

Fuel type	1 July 2006	1 July 2007	1 July 2008	1 July 2009	1 July 2010	1 July 2011	1 July 2012	1 July 2013	1 July 2014	1 July 2015
<b>High-energy content</b> Biodiesel	0	0	0	0	0	3.8	7.6	11.4	15.3	19.1
<b>Mid-energy content</b> Liquefied petroleum gas, liquefied natural gas, ethanol	0	0	0	0	0	2.5	5	7.5	10	12.5
<b>Low-energy content</b> Methanol	0	0	0	0	0	1.7	3.4	5.1	6.8	8.5
<b>Other</b> Compressed natural gas	0	0	0	0	0	3.8	7.6	11.4	15.2	19.0

Source: *Explanatory Memorandum*, p. 15.

Note: Rates are cents per litre except compressed natural gas which is cents per cubic metre.

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The following summarises the reform timetable.

1 July 2006	Excise on burner fuels will be removed. A full credit will be provided for all fuels used in power generation. Excise on heavy vehicles will be converted to a road user charge. Excise relief will be provided for petrol and all other taxable fuels used for business purposes in heavy vehicles. Urban-regional boundaries will be removed. Spending under the Fuel Sales Grants Scheme will be converted to road funding. The Petroleum Products Freight Subsidy Scheme will end. Access to excise credits for those claiming more than \$3 million per year will be linked to participation in the Greenhouse Challenge programme. Access to on-road credits for heavy diesel vehicles will be linked with meeting one of five emissions performance criteria designed to ensure vehicles meet the emission standard set under the Diesel National Environment Protection Measure.
1 July 2008	A 50 per cent credit will be introduced for the off-road business use of taxable fuels in activities not previously eligible for credits.
1 July 2011	Effective excise will apply to all fuels used in an internal combustion engine, including concessional excise for biodiesel, ethanol, liquefied petroleum gas, liquefied natural gas and compressed natural gas. The effective excise rates will increase over five equal annual steps, reaching their final rates on 1 July 2015.
1 July 2012	Full credit will be extended to all business use of all taxable fuels in all off-road activities.
1 July 2015	Final effective fuel excise rates will apply to all taxable fuels, including a 50 per cent discount for alternative fuels.

Source: Australian Government, *Securing Australia's Energy Future*, Canberra 2004, p. 102.

### Heavy vehicle cost recovery (road user charge)

As noted, the fuel tax credits scheme will provide only partial credits in some circumstances. They relate to the cost-recovery arrangements for the damage that heavy trucks cause to roads.

Infrastructure costs attributable to heavy vehicle use are recovered through national heavy vehicle charges. The charges (which the National Transport Commission determines) have two elements:

- a notional component of the excise on diesel, and
- an annual registration charge (which varies by truck type) and which state governments collect.

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The notional charge is effected through the EGCS. Under the EGCS, certain business use of diesel is eligible for a grant of 18.51 cents per litre of diesel used. The grant partly offsets the excise. The notional component is the difference between the excise and the grant. The excise on low sulphur diesel—diesel containing 50 or fewer parts per million of sulphur—is 38.143 cents per litre so the notional component is 19.633 cents per litre.<sup>17</sup>

There is currently no formal link between the net excise paid by heavy vehicles and the road user charge. Under the fuel tax credit scheme, the road user charge will be formally recognised, and the credit will be the difference between the excise paid and the road user charge.

In October 2005, the [National Transport Commission](#) issued a [Regulatory Impact Statement](#) dealing with proposed changes to charges. The main consequences would have been:

- registration fees would be effectively ‘frozen’ for 53 per cent of the vehicle fleet
- an increase of less than \$40 in registration fees for 44 per cent of trucks, plus a further \$16 per axle for towed trailers
- an increase of less than \$3,000 over two years for B-Doubles and road-trains (three per cent of heavy vehicles)
- a B-Double charge subsidy of between \$5,500 and \$7,500 to encourage safe and efficient fleet choices, and
- a 2.1 cents per litre increase in the road user (fuel) charge; representing a 10.5 per cent increase over the last six years.<sup>18</sup>

The Commission’s proposal would have increased registration fees for B-doubles and road trains by about one-third, and the notional component of the excise from 19.633 cents per litre to 22.1 cents per litre.

On 17 March 2006, the Federal Minister for Transport and Regional Services, the Hon. Warren Truss, [announced](#) that the Australian Government would oppose the determination at a meeting of the Australian Transport Council—which consists of Commonwealth, and state and territory transport ministers—on the grounds that the proposed charges would over-recover costs.<sup>19</sup> The Australian Transport Council subsequently rejected the National Transport Commission’s proposed changes.<sup>20</sup> An editorial in the *Australian Financial Review* was critical of the Australian Transport Council’s decision:

It’s a depressingly familiar story. A government agency decides on an economically sensible pricing regime only to have politicians, acting under heavy lobbying from vested interests, reject it. But on this occasion the politicians concerned - state and federal transport ministers - are not just flying in the face of economic logic. They are defying their own policies, and the desires of their masters - the Council of Australian Governments - to achieve an efficient freight system.

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The National Transport Commission believed it was implementing agreed principles that all heavy vehicle classes should pay their own way when it recently recommended a new charging regime for very heavy trucks. The idea was to increase registration and fuel charges for the long, so-called, B-double prime movers. These road monsters are cross-subsidised 21 per cent by smaller trucks in terms of charges. Cross-subsidisation, the NTC says rightly, is not the way to promote optimal use of roads and vehicles ...

Australia needs a rational national road-charging regime, perhaps based on transport corridors, and one that is competitively neutral not only between the size of trucks but between road and rail. Whether that is set by the NTC or not, transport ministers have shown they need to be kicked off the job.

COAG at its meeting last month asked the Productivity Commission to examine the whole issue of efficient pricing for road and rail infrastructure via competitively neutral pricing. The political interference of transport ministers already is a bad omen for the outcome of that inquiry.<sup>21</sup>

## Environmental requirements

As noted, for environmental reasons, the on-road use of diesel in vehicles under 20 tonnes wholly in urban areas is generally not eligible for grants under the EGCS. Further, alternative fuels now effectively do not attract excise but are eligible to receive an on-road credit under the EGCS. The Bill proposes two new environmental measures:

- the requirement for large fuel users to be a member of the [Greenhouse Challenge Plus Programme](#), and
- vehicles using diesel fuel in on-road applications must comply with emissions performance criteria.<sup>22</sup>

The Greenhouse Challenge Plus Programme is designed to:

- reduce greenhouse gas emissions
- accelerate the uptake of energy efficiency
- integrate greenhouse issues into business decision-making, and
- provide more consistent reporting of greenhouse gas emissions levels.<sup>23</sup>

The Bill proposes that:

Businesses claiming over \$3 million each year in fuel tax credits will need to be members of the Greenhouse Challenge Plus Programme. Under this programme member businesses must measure their greenhouse gas emissions, develop action plans for greenhouse gas abatement and report to the Government on their actions.<sup>24</sup>

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The Bill also proposes that operators of diesel vehicles with a GVM of more than 4.5 tonnes be required to meet one of four emissions performance criteria in order to be entitled to receive fuel tax credits. The criteria are:

- the vehicle must have been manufactured after 1 January 1996
- the vehicle must be part of an accredited audited maintenance programme
- the vehicle must meet the Australian Transport Council's in-service emission standard (referred to in the [National Environment Protection \(Diesel Vehicle Emissions\) Measure](#))<sup>25</sup> or
- comply with a Government-endorsed maintenance schedule which includes an emissions component.<sup>26</sup>

The following is background to the Fuel Sales Grants Scheme and the Petroleum Products Freight Subsidy Scheme.

### Fuel Sales Grants Scheme

The fuel sales grants scheme is a grant to fuel retailers for the sale of petrol and diesel to consumers in regional and remote areas where fuel prices are generally higher than in urban areas. The grant is paid to fuel retailers for sales to final consumers in defined non-metropolitan zones. This includes sales by distributors of bulk fuel to end users such as farms and mines where the sale occurs in a defined non-metropolitan zone. Retailers must be registered for the scheme before they can claim a grant. Eligible fuels are leaded and unleaded petrol and diesel including light fuel oil, two stroke and premium unleaded.

For the non-metropolitan zone, the grant is one cent per litre. For the remote zone the grant is two cents per litre. If fuel has been sold consistently in a remote area at not less than \$1.20 per litre, fuel retailers may, subject to certain conditions, receive an additional one cent per litre of fuel sold. The non-metropolitan and remote zones have been defined using the accessibility/remoteness index of Australia.

Fuel retailers are expected to pass on the full effect of the grant to consumers. The Australian Competition and Consumer Commission (ACCC) monitors petrol and diesel prices to ensure the grant is passed on to consumers. Fuel retailers may be required to provide detailed pricing information to the ACCC as part of its monitoring activity.

The estimated cost of the scheme is shown in the table (\$ million).

<b>2000-01</b>	<b>2001-02</b>	<b>2002-03</b>	<b>2003-04</b>	<b>2004-05</b>	<b>2005-06</b>
205	210	215	220	269	270

Source: Australian Taxation Office, Portfolio Budget Statements, various years.

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## Fuel Taxation Inquiry and the Fuel Sales Grants Scheme

The [Fuel Taxation Inquiry](#) examined the Scheme and was highly critical.<sup>27</sup> The Inquiry recommended that the Scheme be abolished. The following is the relevant excerpt from the Inquiry's report.

### **'6.6 Fuel Sales Grants Scheme**

The Fuels Sales Grants Scheme (FSGS) provides registered retailers with grants of one cent per litre in non-metropolitan zones and two cents per litre in so-called remote zones; there is an additional grant of one cent per litre where the fuel price is consistently over \$1.21. The scheme was introduced on 1 July 2000 as part of *A New Tax System*.

#### **6.6.1 Problems identified**

The Inquiry received considerable criticism of the scheme and comparatively little support of it. It appears that the best that can be said of the scheme is that it has had little noticeable impact.

For example, the National Farmers' Federation submitted:

It is arguable whether this scheme has had the intended outcome and, further, unless this grant is indexed, as the price of fuel increases, the extent to which it offsets the GST is diminished. The NFF believes that the funding for the Fuel Sales Grants Scheme could be better channelled into providing more tangible returns of taxes to business.

The Inquiry's attention was also drawn to a number of boundary anomalies in the application of the scheme, including instances where service stations on the fringes of capital cities were eligible for the grant, giving them an advantage over competitors in close proximity.

For example, the West Australian Small Business and Enterprise Association Inc. referred to the recent report of a State Parliamentary Committee that had pointed to problems with the geographic boundaries for eligibility. The West Australian Government confirmed problems with FSGS boundaries and was concerned that they conflicted with the administration of the State's petroleum pricing laws.

The Premier of South Australia also identified geographic anomalies in his submission to the Inquiry.

The Premier of Queensland supported the scheme but was not satisfied that it compensated for the impact of the GST in rural and remote communities when crude oil prices — and thus prices of refined product — were high. It also questioned the appropriateness of the use of the Accessibility/Remoteness Index of Australia that had been designed for service

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provision purposes, since it did not necessarily direct fuel grants to the areas experiencing the highest fuel prices.

Another problem with the FSGS involves the eligibility of bulk end users such as mining companies located in non-metropolitan and remote areas. These bulk end users receive the FSGS grant even though they also receive input tax credits on their fuel purchases. As Treasury submitted:

The grant is also paid to business (or bulk end users) for purchases of petrol and diesel even though the purchase price of petrol and diesel they face wasn't affected by the GST due to the availability of GST input tax credits for businesses.

### **6.6.2 Assessment and recommendation**

The Inquiry is concerned at the difficulty in identifying the benefits of the scheme to consumers in rural and remote regions. The Inquiry notes continuing debate about whether the scheme results in lower prices to final consumers, but is also aware that the ACCC has found no evidence to substantiate claims that the grants have not been passed on to consumers. The ACCC announced the results of its investigations into the FSGS on 1 June 2001, including the following statements:

The ACCC received several inquiries from Caltex franchisees alleging that Caltex had altered its price support system following the introduction of the FSG in such a way that they were unable to pass on the FSG without cutting their own margin. ... The ACCC conducted an extensive investigation into these allegations. As a result of this investigation the ACCC did not establish a failure to pass on the FSG to customers. ...

The ACCC also investigated alleged breaches by Shell, Mobil and BP in relation to their response to the introduction of the FSG. While the material supplied by some of the oil majors, and in particular by Shell, may have been open to an interpretation that the oil companies may have cut margins to their franchisees, and in effect appropriated the FSG, on the evidence available this could not be established.

In any case, it is not clear that any benefits accruing to regional Australians are proportional to the level of public expenditure, estimated to be \$210 million in 2001-02, nor that this programme is the best use of the funding.

Some interested parties were of the view that it would be preferable for the Commonwealth to address, directly, the causes of city-country price differentials. One option suggested to the Inquiry was the introduction of mandatory Terminal Gate Pricing that would ensure that the ex-refinery price was the same for all service stations and bulk purchasers. The Inquiry was aware that Terminal Gate Pricing was an issue that had received attention in the ACCC inquiry into Fuel Price Variability.

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The Inquiry concludes that there are anomalies arising from the geographic boundaries determining eligibility for the lower and higher grant rates, and that these anomalies are likely to have an adverse effect on resource allocation and competition.

The Inquiry faced a difficult choice between:

- recommending amendments to the design of the FSGS to address identified problems such as boundary anomalies and bulk end users; or
- recommending the dismantling of the scheme, and spending the funds saved in other ways.

### ***Recommendation 12: Fuel Sales Grants Scheme***

The Fuel Sales Grants Scheme should be discontinued from 1 July 2004<sup>7</sup>.

#### **Abolition**

On 22 January 2004, the then Deputy Prime Minister, the Hon. John Anderson, [announced](#) that the Scheme would be phased out from 1 July 2006, and the funds transferred to road funding.<sup>28</sup>

#### Petroleum Products Freight Subsidy Scheme

Grants under the [Petroleum Products Freight Subsidy Scheme](#) are paid under the [States Grants \(Petroleum Products\) Act 1965](#). The Fuel Taxation Inquiry also examined this scheme. The following is the relevant excerpt from the Inquiry's report.

#### **Fuel Taxation Inquiry and the Petroleum Products Freight Subsidy Scheme**

'The Petroleum Products Freight Subsidy Scheme was introduced in 1965 with the purpose of reducing the prices of petroleum products in **regional** areas. The scheme was abolished in 1974, reintroduced in 1978 and amended in 1983 to target assistance at **remote** communities.

The scheme reimburses fuel freight costs above a 'Customer Pays Margin', presently 15.3 cents per litre. The margin increased over time from 0.44 cents per litre in 1981-82, increasingly limiting the application of the subsidy to more remote areas.

Subsidies are paid to fuel distributors who are required to sign undertakings that they will pass on the savings to their customers.

Subsidies are delivered through State schemes, with programme funding provided to the States by the Commonwealth. The scheme presently costs the Commonwealth around \$3.5 million per annum, a fraction of its expenditure of \$148 million in 1981-82.

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The majority of eligible locations are in Queensland, Western Australia and the Northern Territory; many are remote indigenous communities. There are no eligible communities in Victoria, Tasmania or the Australian Capital Territory and only one each in New South Wales (Lord Howe Island) and South Australia (Amata).

The value of the subsidy varies by location. Generally speaking, island communities receive substantial subsidies whereas remote coastal or inland subsidies may be worth just a few cents per litre or even less than one cent per litre. For example:

- the highest levels of subsidy are paid to Lord Howe Island (26.5 cents per litre for petrol and 29.7 cents per litre for avgas) and Badu Island in Queensland (up to 19.7 cents per litre for petrol and up to 37.6 cents per litre for avgas sent by seatainer);
- the lowest level of subsidy is paid to Arapunya in the Northern Territory which receives 0.1 cents per litre on avtur only, while Port Hedland in Western Australia receives 0.2 cents per litre on aviation fuels only; and
- Cape York, the northern extremity of the continent, is eligible for 4.7 cents per litre on petrol and diesel and 5.2 cents per litre on aviation fuels.

The Northern Territory and Queensland Governments supported continuation of the scheme.

### Identified problems

Low level of awareness

The Inquiry received no comments about the scheme in its consultations around Australia.

Since the subsidy is paid to oil distribution companies, it is not apparent that the ultimate beneficiaries — remote communities — are necessarily aware of its existence. This may not hold true for some remote island communities where the subsidy has a high value.

Economic impact

The design of the scheme is an inherent disincentive for the adoption of more efficient and less expensive modes of fuel transport to remote communities. Once freight rates exceed the Customer Pays Margin, the Commonwealth meets all freight costs.

The freight subsidy does not offset other high costs involved in supplying fuel to remote communities, such as reseller margins. However, even if the subsidies are not well targeted, it is hard to deny that they make remote fuel distribution cheaper than it would otherwise be.

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## Administration

In 1999, responsibility for administering the scheme was transferred from Customs to AusIndustry. This coincided with the transfer of responsibility for diesel rebates to the ATO. It is unclear to the Inquiry why the programme is not being administered by the ATO along with other fuel programmes.

- The programme is not primarily an industry assistance scheme, though fuel-using industries in remote areas may benefit incidentally from the subsidy.
- AusIndustry does not have an auditing/enforcement capacity for a remote communities programme, whereas there may be economies of scale in administering the programme with other fuel programmes in the ATO.

## Calculating subsidies

Until 1999, the petroleum products industry was regulated by the Prices Surveillance Authority and its successor, the ACCC. It was easy to obtain reliable data for calculating subsidies in this environment. Oil companies provided information to the ACCC on the freight costs of transporting eligible petroleum products from refining ports and seaboard terminals to various points of sale including remote locations.

Now that the ACCC's formal regulatory oversight has ceased, there is no longer a mechanism for establishing the freight differentials on which subsidy rates are based, and the scheme is currently operating using outdated information.

## Assessment and recommendation

The Inquiry is concerned that there has not been a recent assessment of the effectiveness of the Petroleum Products Freight Subsidy Scheme.

In any case, the current justification for providing assistance of this type is questionable. Remote communities face a range of higher living costs, and the Inquiry cannot see why just one cost—fuel freight—should be the subject of a specific subsidy scheme. If Governments — State or Commonwealth — want to reduce the general costs of living, there are much better and more transparent ways of doing so.

Subsidising residents of, or visitors to, places like Lord Howe Island is even less justifiable. The data on which subsidies are determined are now of questionable accuracy. The total cost of the subsidy is small and its administrative costs are disproportionately high.

### ***Recommendation 13: Petroleum Products Freight Subsidy Scheme***

The Petroleum Products Freight Subsidy Scheme should be discontinued from 1 July 2004.'

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### Cost and abolition

Payments under the scheme fell e.g. from \$147.5 million in 1981-82 to only \$3.8 million in 1993-94. The amount now allocated to the Scheme is \$3.5 million annually.

The Government decided to abolish the Petroleum Products Freight Subsidy Scheme with effect from 1 July 2006.<sup>29</sup>

### Position of significant interest groups/press commentary

The Australian Chamber of Commerce and Industry (ACCI) in a [submission](#) to Treasury's Fuel Tax Credit Reform Discussion paper, said, among other things, that:

- the proposed changes will:
  - remove or reduce taxes on business inputs
  - reduce the tax level on many businesses
  - reduce compliance and administration costs, and
  - increase the tax neutrality between different activities and fuels.
- the ACCI was generally supportive of the proposals except for the proposal to reduce excise exemptions
- the ACCI accepted, on balance, that the business compliance costs under the new system will be lower than under the current system
- the effect on cash flows will differ, depending on the current arrangements that taxpayers use, and
- the government should explore ways of aligning and simplifying the transitional period for some of the arrangements.<sup>30</sup>

The Australian Seafood Industry Council, in its [response](#) to the Treasury Fuel Tax Credit Reform Discussion Paper:

- noted that some members would suffer a cash flow disadvantage, and
- argued that the current system—whereby claimants give permission to a third party to make and/or receive grant claims on their behalf—be maintained.<sup>31</sup>

[KPMG](#) noted that:

- the road transport, construction industries and remote communities are the likely winners
- the shift to claiming credits through the Business Activity Statement may create some transitional problems for business

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- the shift from a grant scheme to a tax credit system will cause initial administrative problems since businesses will need to align their fuel tax credits with their GST processes, and
- another challenge for businesses will be the need to comply with new environmental requirements in order to claim fuel tax credits. All businesses claiming fuel tax credits will need to comply with some basic emission control standards and large claimants will also have to join the Greenhouse Challenge Plus program and this may mean more comprehensive fleet management systems will be required.<sup>32</sup>

The Minerals Council of Australia—in its [submission](#) to the taskforce on Reducing the Regulatory Burden on Business—stated that:

... the phasing in of reductions in taxation of fuels used as business inputs is desirable. It is possible that aspects of the current proposals could impose an unnecessary regulatory burden on the Australian minerals industry. To reduce the potential for this to occur, it is desirable to ensure:

- the range of activities eligible for credits is not restricted during the transition to the new arrangements;

- compliance costs are minimised by making the administration and compliance regime (under the umbrella of the *Taxation Administration Act 1953*) that underpins the reforms as efficient and effective as possible. Aggregating fuel tax credit claims in the running balance accounts will be problematic, so this might include, for instance, addressing concerns with the Tax Office's administration of the GST refunds;

- businesses required to be members of the *Greenhouse Challenge Plus Program* (as they claim over \$3 million per annum in fuel tax credits) and meet all relevant requirements under existing and new schemes should *not* be impacted by the transition;

*de minimus* and safe harbour requirements are included in the legislation, to give effect to the intended reduction in record-keeping required to substantiate entitlements once the fuel tax credit system is fully implemented; and

e-grant claims for fuel tax credits are continued instead of being made through the Business Activity Statement (BAS), as currently proposed, because that would raise compliance costs. Although the BAS arrangement would align the mechanism for claiming fuel tax credits with that for claiming GST input tax credits, it would remove a recently introduced arrangement that is beginning to gain acceptance and generate benefits.

The National Farmers' Federation in its [Submission in response to the Treasury Fuel Tax Credit Reform Discussion Paper](#) stated, among other things, that:

- 2008 is an unreasonable amount of time to wait for the off road extension to begin at a 50 per cent rebate, and 2012 far too distant for the full 100 per cent rebate

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- the NFF opposes the proposal to scrap the e-Grant program that allows farmers and others to purchase fuel at the pump effectively excise free on the grounds that this will potentially create cash flow problems
- NFF considers that the requirement for those businesses with turnover of under \$50,000 be required to claim rebates on a Business Activity Statement, despite not having to be registered for GST purposes, as inconsistent with the spirit and intent current tax law, and
- the paper needs to provide greater clarity regarding the policy intention for vehicles less than 4.5 tonnes as many farm vehicles used off road fall into this category.<sup>33</sup>

### Any consequences of failure to pass

Failure to pass the Bill would result in the continuation of the existing system of grants and remissions. The existing system is arguably generally less efficient than the Bill proposes. For example, the discrimination among business activities and fuels that is a feature of the current system would remain. Failure to pass the Bill would also mean that the framework for bringing alternative fuels into the tax net would not be established.

## Financial implications

The estimated revenue forgone from the proposals in the Bill is set out in Table 5.

**Table 5: Estimated revenue forgone (\$ million)**

2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
40	20	260	240	230	220	540

Source: *Explanatory Memorandum*, p. 5.

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## Main provisions

### Chapter 3—Fuel tax credits

#### Part 3-1—Basic rules

#### Division 41—Fuel tax credits for business taxpayers and non-profit bodies

##### Subdivision 41-A—Entitlement rules for fuel tax credits

#### **Clause 41-5 Fuel tax credit for fuel to be used in carrying on your enterprise**

**Subclause 41-5(1)** sets out the general terms for entitlement to receive a fuel tax credit for fuel used in a business. The effect of Note 2 to this subclause is that entitlement includes the use of blended fuels. **Subclause 41-5(2)** provides that entitlement exists only if the business is registered for GST or required to be registered for GST. However, **subclause 41-5(3)** provides that the requirements of subclause 41-5(2) do not apply to non-profit bodies and emergency services.

The Explanatory Memorandum elaborates on the meaning of ‘use’ in clause 41-5:

1.40 The term ‘use’ in section 41-5 is intended to cover use of the fuel to make a blend that cannot be used as a fuel in an internal combustion engine. In most instances it will be self evident whether the blend can be used as a fuel, but to ensure certainty in cases where it is not self evident, the Commissioner is able to make a determination under section 95-5 that a blend of a fuel and another product does not constitute a fuel.<sup>34</sup>

##### Subdivision 41B—Disentitlement rules for fuel tax credits

#### **Clause 41-20 No fuel tax credit for fuel to be used in light vehicles on a public road**

The Bill does not define a ‘light vehicle’. But **Clause 41-20** effectively defines a light vehicle by providing that entitlement to a fuel tax credit does not exist when fuel is used in a vehicle with a gross vehicle mass of 4.5 tonnes or less.

The effect of this clause is that most trucks will not be eligible for fuel tax credits because most trucks have a gross vehicle mass equal to or less than 4.5 tonnes. These trucks will therefore have to pay the full amount of excise.

The 4.5 tonnes gross vehicle mass was chosen because:

- it reflects an existing break-point in the fuel taxation system
- additional licensing requirements must be met in all Australian jurisdictions to drive a vehicle of this mass or greater, and

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- it is more difficult to distinguish between private and business use in small vehicles.<sup>35</sup>

**Clause 41-25** No fuel tax credit for fuel to be used in motor vehicles that do not meet environmental criteria

**Clause 41-25** establishes the requirement that motor vehicles must meet one of four environmental criteria for its use to be eligible to receive a credit. The criteria which are set out in **subclause 41-25(1)** are:

- the vehicle was manufactured on or after 1 January 1996
- the vehicle is registered in an audited maintenance program that the Secretary of the Department of Transport and Regional Services has accredited
- the vehicle meets Rule 147A of the Australian Vehicle Standards Rules 1999, and
- the vehicle complies with a maintenance schedule that the Secretary of the Department of Transport and Regional Services has endorsed.

**Subclause 41-25(2)** exempts from these environmental requirements vehicles used in carrying on a primary production business and that are primarily used on an agricultural property.

#### Division 42—Fuel tax credit for non-business taxpayers

Currently, a credit is available for the private use of fuel used to generate electricity for domestic use. As noted, the Bill will extend this entitlement to the business use of all fuels used to generate electricity for domestic use; such use will be effectively excise-free from 1 July 2006. Further, the excise currently levied on burner fuels—such as heating oil and kerosene—will be effectively removed from 1 July 2006.

##### Subdivision 42-A—Fuel tax credits for non-business taxpayers

#### **Clause 42-5 Fuel tax credit for fuel to be used in generating electricity for domestic use**

**Clause 42-5** establishes that non-business use of fuels for generating electricity for domestic use is eligible for a credit.

##### Subdivision 43-A—Working out your fuel tax credit

#### **Clause 43-5 Working out your fuel tax credit**

**Division 43 (Working out your fuel tax credit)** deals with calculating the amount of fuel credit to which the claimant is entitled. **Subclause 43-5(1)** defines the amount as the ‘effective fuel tax’. **Subclause 43-5(2)** defines effective fuel tax as the fuel tax amount less any subsidy received, that is, the net amount. This is to prevent claimants from double

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dipping, once from the subsidy and once from the fuel tax credit. However, **subclause 43-5(3)** provides that certain items are not considered to be subsidies. The items are:

- a grant under the Biofuels Capital Grants Program
- grants for on-road alternative fuel under the *Energy Grants (Credits) Scheme Act 2003* (alternative fuels are biodiesel, ethanol, liquefied petroleum gas, liquefied natural gas and compressed natural gas)
- grants under the [Energy Grants \(Cleaner Fuels\) Scheme Act 2004](#), and
- a benefit paid to waste oil recyclers and for eligible uses of specific oils under the *Product Stewardship (Oil) Act 2000*.

The effect of subclause 43-5(3) is to not reduce the amount that a claimant is entitled to receive. As the Explanatory Memorandum notes, these:

... grants are paid for reasons other than to offset the fuel tax payable on a fuel and therefore do not reduce the amount of the taxpayer's fuel tax credit.<sup>36</sup>

### **Clause 43-10 Reducing the amount of your fuel tax credit**

**Subclauses 43-10(3) to 43-10(5)** deal with the mechanism whereby the road user charge is implemented. Subclause 43-10(3) provides that the amount of the fuel tax credit is reduced by the amount of the charge.

Currently, the excise on low sulphur diesel is 38.143 cents per litre and the road user charge is 19.633 cents per litre, so the maximum that can be claimed as a credit is 18.51 cents per litre. The 18.51 cents per litre is paid as a grant under the EGCS.

### **Division 44—Increasing and decreasing fuel tax adjustments**

The Explanatory Memorandum explains how a fuel tax adjustment can arise:

2.94 Fuel tax adjustments can arise in a number of ways. It may be that the activity in which a taxpayer actually uses the fuel is different from that which was intended. For example if fuel, or some of it, is used for a private purpose or the consumption of the fuel results in a different fuel tax credit amount being applicable to the actual use.<sup>37</sup>

#### **Subdivision 44-A—Increasing and decreasing fuel tax adjustments**

### **Clause 44-5 Increasing and decreasing fuel tax adjustments for change of circumstances**

There are two types of adjustments: decreasing and increasing. **Subclause 44-5(3)** defines decreasing adjustments as when the taxpayer is entitled, in effect, to receive additional

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credits, while **subclause 44-5(4)** defines increasing adjustments as when the taxpayer has received too much credit.

### Part 3-3—Special rules

#### Division 45—Greenhouse Challenge Plus Programme

##### Subdivision 45-A—Greenhouse Challenge Plus Programme

#### **Clause 45-5 Certain entities to be members of the Greenhouse Challenge Plus Programme**

**Subclause 45-5(1)** provides that taxpayers are not entitled to receive more than \$3 million in net fuel tax credits in a financial year unless they are members of the Greenhouse Challenge Plus Programme [**paragraph 45-5(1)(a)**] or another programme that the Environment Minister determines by legislative instrument [**paragraph 45-5(1)(b)**].

**Subclause 45-5(2)** provides that where taxpayers become members of the Greenhouse Challenge Plus Programme, they will be entitled to claim fuel tax credits for fuel they bought or used *before* they joined the Programme, by making a ‘decreasing fuel tax adjustment’ for the amount of fuel tax credit that they were previously not entitled to take into account.

This provision applies to taxpayers who could not claim more than \$3 million in fuel tax credits because they were not members of the Greenhouse Challenge Plus Programme, and so provides an additional incentive to join the Programme.

#### Division 46—Instalment taxpayers

##### Subdivision 46-A—Instalment taxpayers

#### **Clause 46-5 Instalment taxpayers**

**Subclause 46-5(2)** establishes that if taxpayers pay GST quarterly, the periods for which they claim fuel tax credits are the same as those for the GST. But under **subclause 46-5(3)**, taxpayers can opt not to submit a return for the first three quarters. An exception to this option is where the taxpayers have an ‘increasing fuel tax adjustment’. Currently, GST instalment payers can choose whether or not to lodge a return in any of the four quarters. But when taxpayers have an increasing fuel tax adjustment, the taxpayer must lodge a return for the last quarter while lodging a return in the preceding quarters is optional.

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## Chapter 4—Common rules

### Division 60—Net fuel amounts

#### Subdivision 60-A—Net fuel amounts

There are two net fuel amounts: negative and positive. A negative fuel amount is when the taxpayer is owed money for fuel tax credits. A positive fuel amount is the opposite.

#### **Clause 60-5 Working out your net fuel amount**

**Subclause 60-5(1)** sets out how a taxpayer's net amount is calculated. The net fuel amount in a period is the sum of: total fuel tax less total fuel tax credits, plus increasing adjustments less decreasing adjustments.

### Division 61—Returns, refunds and payments

#### Subdivision 61-A—Returns, refunds and payments

#### **Clause 61-5 Entitlement to a refund**

Taxpayers are entitled to a refund when the net fuel amount for a period (or fuel tax period) is less than zero [**subclause 61-5(1)**]. Conversely, taxpayers must pay the Commissioner of Taxation when the return is more than zero [**subclause 61-5(2)**].

#### **Clause 65-1** states:

Fuel tax credits and fuel tax adjustments are attributed to tax periods (or fuel tax return periods).

Generally, if you are a business taxpayer, your fuel tax credit for taxable fuel is attributed to the same period as your input tax credit for the fuel (to reduce compliance costs). If you are a non-business taxpayer, your fuel tax credit for taxable fuel is attributed to the fuel tax return period in which you acquire, manufacture or import the fuel.

**Clause 61-20 Fuel tax return periods**—defines fuel tax return periods (referred to in clause 65-1) that are applicable to non-business taxpayers. **Subclause 61-20(1)** provides that if the taxpayer is neither registered for GST, nor required to be registered for GST, the fuel tax return period is the period specified in the return. However, **subclause 61-20(2)** provides that taxpayers must end a fuel tax return period within 90 days (or any longer period allowed by the Commissioner) if the taxpayers become aware of an increasing fuel tax adjustment, that is, the taxpayers have received more in credits than their entitlements.

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## Part 4-3—Special rules about entities

### Division 70— Special rules about entities

**Division 70** applies the rules relating to entities with respect to GST to entities seeking fuel tax credits:

2.140 The GST Act provides special rules that tailor the operation of the GST to the way particular entities are organised. If a special GST rule applies to the way a taxpayer's business is organised, the same rule will generally apply to them for fuel tax credits.<sup>38</sup>

The *Explanatory Memorandum* describes the provisions of Division 70, including examples, in paragraphs 2.140 to 2.151.

## Part 4-4—Anti-avoidance

### Division 75—Anti-avoidance

#### Subdivision 75-A—Application of this division

**Part 4-4** contains anti-avoidance provisions, which are based on the anti-avoidance provisions in the GST Act.<sup>39</sup> **Clause 75-5 When does this Division operate?**—sets out the general circumstances which constitute avoidance. They are:

- there must be a scheme from which the avoider obtains a fuel tax benefit [**paragraph 75-5(1)(a)**]
- the benefit does not derive from the fuel tax or GST laws [**paragraph 75-5(1)(b)**]
- the main purpose of the scheme was to obtain a fuel tax benefit [**sub-paragraph 75-5(1)(c)(i)**]
- the main effect of the scheme was to obtain a fuel tax benefit [**sub-paragraph 75-5(1)(c)(ii)**] and
- the avoider derives the benefit after 1 July 2006 [**paragraph 75-5(1)(d)**].

The remaining clauses in **Subdivision 75-A—Application of this division** define and expand on these circumstances. Paragraphs 2.161 to 2.183 of the *Explanatory Memorandum* explain these clauses.

#### Subdivision 75-B—Commissioner may negate effects of schemes for fuel tax benefits

**Subdivision 75-B** provides the Commissioner of Taxation with powers to deal with avoidance. **Clause 75-40 Commissioner may negate avoider's fuel tax benefits** gives the Commissioner power to make a declaration stating the avoider's net fuel amount. The

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declaration can cover several periods (**clause 75-60**) and the Commissioner can require the avoider to refund the benefit obtained (**clause 75-50**).

## Part 4-5—Miscellaneous

### Division 95—Miscellaneous

#### Subdivision 95-A—Miscellaneous

An issue in determining whether an item is subject to excise—and hence potentially subject to a fuel tax credit—is whether the item is a fuel and, in particular, whether it is a fuel that can be used in an internal combustion engine. The Explanatory Memorandum contains the following explanation of **clause 95-5** Determination of blends that no longer constitute fuels:

2.202 An entity may produce blends of fuel products with other products, for use other than as a fuel — for example, for use as a solvent. If the blend can be used as a fuel, the end user will claim a fuel tax credit for that fuel under section 41-5. Some of these blends incorporate the addition of non-excisable products to fuels — for example, a non-excisable product such as methyl ethyl ketone is blended with toluene, a fuel, to make thinners. At some point in time the non-excisable product makes up a sufficient component of the blend, so that the end product does not present a significant risk of substitution as fuel.

2.203 The Commissioner may determine by legislative instrument that such a fuel blend does not constitute a fuel [subsection 95-5(1)]. If the Commissioner has made such a determination then the producer of the blend is considered to have used the fuel, rather than the end user, and is entitled to a fuel tax credit.

2.204 There are several factors that the Commissioner must take into consideration when making the determination [subsection 95-5(3)]. The factor that he must give greatest weight to is the risk that the blend may be used as a fuel and the resulting financial impact on the Commonwealth [paragraph 95-5(3)(d)].<sup>40</sup>

## Concluding comments

Overall, the fuel tax credits scheme is an improvement on the Energy Grants (Credits) Scheme (EGCS) which is the main scheme the Bill supersedes. The Bill retains the entitlements under the EGCS and extends them to additional businesses and fuels.

The Bill should improve economic efficiency. The extension of the credit to all off-road business use and to all fuels will remove the distortions in the EGCS whereby only certain activities and only certain fuels are eligible. The additional businesses which will be able to claim credits for the first time will experience a reduction in costs.

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A consequence of extending eligibility to additional activities and fuels will be to relieve some businesses from excise on fuel used as business inputs. Taxing intermediate inputs such as fuel used in businesses distorts the allocation of resources. Excise increases the cost of petrol and diesel that businesses use as intermediate inputs particularly in industries that use these fuels relatively intensively. This increases the output prices of such industries relative to the prices of other industries. This, in turn, lowers demand for the output of the industries that use fuel relatively intensively, causing resources to leave them. In short, taxes on intermediate inputs distort both consumption and production.

An alternative to the fuel tax credits scheme, which would also relieve businesses of the excise on fuel used as inputs, would be to abolish the excises and replace them with GST. But to be revenue-neutral, the GST rate(s) on petrol and diesel would have to be higher than the standard GST rate of 10 per cent. This would have several disadvantages. One is that the higher rate would increase administration and compliance costs. Second, the higher rate would require changes to Commonwealth–state financial arrangements whereby the Commonwealth now pays to the states all GST revenue it raises. However, a multi-rate GST system is possible: several countries have different rates of value added tax (the GST is a value added tax by another name).

As noted, the Bill paves the way for alternative fuels to be subjected to excise. The energy white paper acknowledges that the excise-exempt status of some alternative fuels has harmed economic efficiency.<sup>41</sup> The decision to bring exempt fuels into the excise net should therefore improve economic efficiency. The phasing of fuel tax credits will give the affected industries time to adjust.

The fuel tax credit scheme should ease generally administrative and compliance burdens. In particular, the abolition of the metropolitan boundaries should reduce the need for record keeping. The replacement of all concessions, refunds and remissions with fuel tax credits should also simplify administration. Further, the ability of businesses to claim credits through their Business Activity Statements should ease the administrative burden on business. On the other hand, as the *Explanatory Memorandum* acknowledges, some measures, such as those relating to the environment, will entail additional administrative costs for some businesses.

As noted, the Bill proposes two additional environmental measures, which should benefit the environment. On the other hand, the abolition of the metropolitan boundaries could adversely affect the environment in urban areas. As noted, under the EGCS, the on-road component generally does not apply to the use of diesel in urban areas for environmental reasons. Under the new credit system, vehicles with a GVM of more than 4.5 tonnes will be able to claim a full credit to the extent that the amount of excise paid on fuel used exceeds the road-user charge regardless of where the vehicle is driven.

The Bill proposes that vehicles used in carrying out a primary production business that are used primarily on an agricultural property be exempt from compliance with the environmental performance criteria on the grounds that these vehicles do not generally

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contribute to urban air quality problems.<sup>42</sup> Whilst the point about *urban* air quality is correct, the proposal ignores the fact that such vehicles nonetheless contribute to air pollution and greenhouse gases.

On the matter of cash flows, some businesses have complained that by having to apply for credits through the quarterly Business Activity Statement rather than monthly as is now the case under the EGCS, the businesses will be forced to borrow to finance the cost of buying fuel.<sup>43</sup> Such businesses are, in effect, using the EGCS as a form of government-financed interest-free loan. This is inequitable and discriminatory: the government does not provide interest-free loans to other businesses.

## Endnotes

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1. The following draws on Richard Webb, 'Excise taxation: developments since the mid 1990s', *Research Brief*, no. 15, Parliamentary Library, Canberra, 2005–06 at <http://www.aph.gov.au/library/pubs/rb/2005-06/06rb15.pdf>. Web address accessed 18 April 2006.
2. Eligible alternative fuels are liquefied petroleum gas, compressed natural gas, liquefied natural gas, ethanol, biodiesel, and blends of biodiesel and diesel that consist mainly of biodiesel.
3. Australian Taxation Office, *Rates for the energy grants credits scheme*, <http://www.ato.gov.au/nonprofit/content.asp?doc=/content/35004.htm>. Web address accessed 27 March 2006.
4. *Explanatory Memorandum*, paragraph 1.14, p. 9.
5. Hon. John Howard, (Prime Minister), *Changes to the goods and services tax (GST)*, [http://www.pm.gov.au/news/media\\_releases/1999/changes3105.htm](http://www.pm.gov.au/news/media_releases/1999/changes3105.htm). Web address accessed 27 March 2006.
6. Australian Taxation Office, *Eligibility requirements*, <http://www.ato.gov.au/businesses/content.asp?doc=/content/35174.htm&page=2&H2>. Web address accessed 27 March 2006.
7. *Portfolio Budget Statements 2005-06*, Treasury portfolio, p. 221.
8. *Explanatory Memorandum*, p. 10.
9. 'Budget strategy and outlook 2003–04', *Budget Paper No. 1*, 2003, Canberra, pp. 1–22 and 1–23.
10. Hon. J. Howard (Prime Minister), *Fuel excise reforms*, media release, Canberra, 16 December 2003, [http://www.pm.gov.au/news/media\\_releases/media\\_Release624.html](http://www.pm.gov.au/news/media_releases/media_Release624.html). Web address accessed on 27 March 2005.

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11. Australian Government, *Securing Australia's Energy Future*, Canberra, 2004, p. 93, [http://www.pmc.gov.au/publications/energy\\_future/docs/energy.pdf](http://www.pmc.gov.au/publications/energy_future/docs/energy.pdf). Web address accessed on 27 March 2006.
12. Treasury, *Fuel Tax Credit Reform Discussion Paper*, Canberra, 2005, <http://www.treasury.gov.au/contentitem.asp?NavId=037&ContentID=986>. Web address accessed 27 March 2006.
13. Treasury, *Review of the Schedule to the Excise Tariff Act. Industry discussion paper*, Canberra, 2005, at <http://www.treasury.gov.au/documents/984/PDF/Review%20of%20the%20SETDP.pdf>. Web site accessed 28 April 2006.
14. The exemption for liquefied petroleum gas (LPG) dates back to 28 June 1979 when the excise on LPG was removed to help reduce reliance on imported oil and petroleum products. The Fuel Taxation Inquiry was sceptical about the cost-effectiveness of using excise exemption to increase fuel security and recommended that LPG be brought into the excise net.
15. *Explanatory Memorandum*, paragraph 1.3, p. 7 and paragraph 2.3, pp. 23–24.
16. *Explanatory Memorandum*, paragraph 1.17, p.10.
17. On 1 January 2006, the sulphur standard for diesel was reduced to 50 parts per million under the *Fuel Quality Standards Act 2000*.
18. National Transport Commission, 'Charges reflect a cautious and conservative approach', news release, 17 October 2005 at <http://www.ntc.gov.au/NewsDetail.aspx?page=A024003055000002000154>. Web address accessed 20 April 2006.
19. Hon. Warren Truss (Minister for Transport and Regional Services), *Australian Transport Council—vote on the National Transport Commission's recommendation on heavy vehicle charges*, media release 034WT/2006 at [http://www.ministers.dotars.gov.au/wtr/releases/2006/March/034WT\\_2006.htm](http://www.ministers.dotars.gov.au/wtr/releases/2006/March/034WT_2006.htm). Web address accessed 20 April 2006.
20. 'Truckies cheer \$7000 rego win', *Daily Telegraph*, 25 March 2006.
21. 'Ministers' drive is a bad omen' *Australian Financial Review*, editorial, 23 March 2006, p. 62.
22. *Explanatory Memorandum*, paragraph 1.46, p. 18.
23. Department of the Environment and Heritage web site at <http://www.greenhouse.gov.au/challenge/about/>. Web address accessed 19 April 2006.
24. *Explanatory Memorandum*, paragraph 1.47, p. 19.
25. Environment Protection and Heritage Council website at [http://www.ephc.gov.au/nepms/diesel/diesel\\_intro.html](http://www.ephc.gov.au/nepms/diesel/diesel_intro.html). Web address accessed 19 April 2006.
26. *Explanatory Memorandum*, paragraph 1.48, p. 19.

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28. Hon. John Anderson (Minister for Transport and Regional Services) and Senator the Hon, Ian Campbell, *Major downpayment on Australia's Transport Future*, joint media statement APM4/2004, 22 January 2004.
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31. Australian Seafood Industry Council, 3 July 2005, at <http://www.asic.org.au/policy/item.php?pid=554>. Web address accessed 20 April 2006.
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33. National Farmers' Federation, *Submission to the Treasury Fuel Tax Credit Reform Discussion paper*, 3 August 2005 at [http://www.nff.org.au/pages/sub/Treasury\\_Fuel\\_Tax\\_Sub\\_July\\_2005.PDF](http://www.nff.org.au/pages/sub/Treasury_Fuel_Tax_Sub_July_2005.PDF). Web address accessed 20 April 2006.
34. *Explanatory Memorandum*, paragraph 1.40, p. 16.
35. Australian Government, *Securing Australia's Energy Future*, op. cit., p. 97.
36. *Explanatory Memorandum*, paragraph 2.73, pp. 39–40.
37. *Explanatory Memorandum*, paragraph 2.94, p. 43.
38. *Explanatory Memorandum*, paragraph 2.140, p. 53.
39. *Explanatory Memorandum*, paragraph 2.152, p. 57.
40. *Explanatory Memorandum*, paragraphs 2.202 to 2.204, p. 66.
41. Australian Government, *Securing Australia's Energy Future*, op. cit., p. 96.
42. *Explanatory Memorandum*, paragraph 1.50, p. 19.
43. Elizabeth Kazi, 'Changes to scheme fuel rebate worries' *Australian Financial Review*, 4 April 2006.

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