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ECONOMICS LEGISLATION COMMITTEE

**Reference: Fuel Tax (Consequential and Transitional Provisions) Bill 2006;
Fuel Tax Bill 2006**

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SENATE
ECONOMICS LEGISLATION COMMITTEE
Monday, 5 June 2006

Members: Senator Brandis (*Chair*), Senator Stephens (*Deputy Chair*), Senators Chapman, Murray, Watson and Webber

Participating members: Senators Abetz, Adams, Bartlett, Bernardi, Boswell, Bob Brown, George Campbell, Carr, Colbeck, Conroy, Coonan, Eggleston, Chris Evans, Faulkner, Ferguson, Ferris, Fielding, Fifield, Forshaw, Hogg, Joyce, Kirk, Lightfoot, Ludwig, Lundy, Ian Macdonald, Marshall, Mason, McGauran, Milne, Murray, O'Brien, Parry, Payne, Robert Ray, Sherry, Siewert, Stott Despoja and Wong

Senators in attendance: Senators Allison, Brandis, Joyce, Murray, Stephens, Watson and Webber

Terms of reference for the inquiry:

Customs Amendment (Fuel Tax Reform and Other Measures) Bill 2006, Customs Tariff Amendment (Fuel Tax Reform and Other Measures) Bill 2006, Excise Laws Amendment (Fuel Tax Reform and Other Measures) Bill 2006, Excise Tariff Amendment (Fuel Tax Reform and Other Measures) Bill 2006, Fuel Tax (Consequential and Transitional Provisions) Bill 2006 and Fuel Tax Bill 2006

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Committee met at 9.09 am

CHAIR (Senator Brandis)—I declare open this meeting of the Senate Economics Legislation Committee. The Senate has referred to this committee the provisions of the Fuel Tax Bill 2006 and a related bill. The bills provide a single system of fuel tax credits to remove or reduce the incidence of fuel tax levied on taxable fuels and a framework for the taxation of gaseous fuels from 1 July 2011, when fuel tax is levied on liquefied petroleum gas, liquefied natural gas and compressed natural gas for the first time. The bills will replace the current system of fuel tax concessions with a single fuel tax credit system from 1 July 2006. The committee has resolved to table its final report to the Senate on Tuesday, 13 June 2006.

These are public proceedings, although the committee may agree to any request to have any evidence heard in camera or may determine that certain evidence should be heard in camera. If any witness wishes to have their submission treated as confidential and heard in camera, they should indicate that to the committee and we will consider that application.

I remind all witnesses that in giving evidence to the committee they are protected by parliamentary privilege. It is unlawful for anyone to threaten or disadvantage a witness on account of evidence given to this committee, and any such action may be treated as a contempt of the Senate. It is also a contempt of the Senate to give false or misleading evidence. If a witness objects to answering a question the witness should state the ground upon which the objection is taken and the committee will determine whether it will insist on an answer, having regard to the ground on which the objection is made. If the committee determines to insist on an answer, a witness may request that the answer be given in camera.

Any claim that it would be contrary to the public interest to answer a question may only be made on behalf of an agency by a minister and must be accompanied by a statement setting out the basis of the claim. The Senate has also resolved that an officer of a department of the Commonwealth or of a state shall not be asked to give opinions on matters of policy and shall be given a reasonable opportunity to refer questions asked of the officer to superior officers or to a minister.

[9.12 am]

GOW, Mr Neil, National Manager, Government Relations, Australian Trucking Association

CHAIR—Welcome. Would you like to make an opening statement before we proceed to questions?

Mr Gow—Yes. The Australian Trucking Association has made a submission to the inquiry, which I am sure you have before you. We welcome the opportunity to discuss the bill with the committee, as it is a complex and multifaceted bill. Our key issue is addressed in our submission, and it was addressed by the government in the announcement by Minister Dutton last Thursday, 1 June, recognising that a transitional arrangement for the claiming of fuel tax credits will be in place for two years from 1 July 2006 in order to address the cash flow issues that businesses, particularly small businesses, would have in relation to claiming their on-road fuel grants—that is some 18.51c per litre—in their trucking operations. So we welcome that announcement of 1 June. I will also quickly address a few other areas of the bill, possibly to anticipate questions and to make the ATA's position clear on them.

Firstly, the abolition of the metropolitan boundaries is welcomed. That eliminates the taxes on business input for the vehicles operating in metropolitan areas which has exacerbated the over-recovery from the total industry. That is a welcome measure from the ATA's point of view. It will also simplify administration for the businesses that have 4½- to 20-tonne trucks running either in or across the soon to be defunct metropolitan boundaries. I understand that even Australia Post has not desegregated its travel for those trucks since 2000 because they feel that the administrative cost would be greater than the amount of grant they could gain from it. That will be gone from 1 July and we welcome that. An interesting aside, the news has produced, the eternal problem of our very competitive trucking industry. Being aware of that grant becoming available for the smaller trucks in metro areas, there are already commercial pressures on many of our members to review their rates—of course downward—for their services in those areas. Their customers are aware that the reform will come into effect on 1 July.

Secondly, the bill will introduce a mechanism for the Minister for Transport and Regional Services to set the heavy vehicle road user charge, otherwise known as the net diesel excise. We welcome the government's announcement in the budget that that will be set at the rate of 19.633c per litre—in other words, maintaining the status quo in recognition that the industry does pay its way and also, of course, that the excess excise tax paid by trucking businesses should, like the GST input tax credits, be returned to them.

Just as an aside, I will mention that our numbers indicate that the net diesel excise from heavy vehicles yields some \$1.346 billion per year to the Commonwealth and we estimate that is growing at 7.5 per cent per year—some \$101 million per year at the current rate. We also welcome the announcement that, at that time, the rate for the registration of federal interstate registered trucks will not be altered from the current rate.

The other issue that we addressed in our submission is the abolition of the Fuel Sales Grants Scheme. We welcomed that announcement in January 2004 on the understanding that

the money would be spent on roads in the areas where the Fuel Sales Grants Scheme had applied—in other words, regional and remote Australia. We believe that has happened with the announcement of increased road expenditure in the budget on 9 May. We believe generally that the best way for governments to address the issue of fuel price is to make an arrangement relating to excise—rebates, if you like—payable to business, as is done with the net diesel charge for heavy vehicles that I have just spoken about.

The BAS payment proposal is an area in which we had concerns. Although the transition to a single reporting system is welcomed, businesses will need extra working capital in the transition period because of the payment times for fuel credits and the payments on their fuel bills. We had approached the Australian Taxation Office about giving some understanding to that issue. I would like to table for the inquiry both our letter to and reply from the tax office. The ATO were helpful in their approach; however, we still felt that a change to the legislation was necessary to fully address the matter. We welcome the change that was announced on 1 June. We believe that will give the opportunity for trucking operators, particularly small businesses, to make the transition in the two-year period and we will continue to educate our industry about that matter.

The bill also proposes an excise differential or increase of some 0.7c on diesel to encourage early production of zero sulphur diesel from 1 January next year. We welcome the move to cleaner fuels; however, we believe that the imposition of that excise increase should not corrupt the amount of heavy vehicle road user charge paid by the industry which would, otherwise, lead to over-recovery.

On the matter in the bill of older trucks having to meet environmental emission criteria, we support that move and welcome the fact that the Department of Transport and Regional Services has now published the details of the maintenance schedules and other requirements for pre-1996 trucks to meet those standards. The Australian Trucking Association has a product called TruckSafe. It has been fully amended and is awaiting approval from the department that it is a recognised audited maintenance scheme for those older trucks.

We also recognise that, under the bill, larger operators will have to be inscribed in the Greenhouse Challenge program. Many of our operators already are. We have encouraged that program since the mid-nineties, and transport is the second largest population of industries within the Greenhouse Challenge. Now there will be a legislative imperative to be in that scheme for those claiming over \$3 million worth of fuel tax credits per year, whether on- or off-road, and we will continue to support that.

The change for claims, of switching to the BAS, was proposed to take effect from 1 July this year. But this is not the only issue that would impact on our industry from 1 July. I made a quick mental summary yesterday evening, and there are about six or seven issues that businesses will have to handle from that time.

The first is that, if they do have older trucks, under this legislation they are going to have to set maintenance programs in place to address the conditional credits arrangements. There is a proposal to extend higher mass limits in New South Wales on a very limited network, from the Victorian border as far as Goulburn, Senator, but not to Sydney. As yet no working details

are available from the New South Wales Roads and Traffic Authority at this stage. So people are waiting for that, and waiting to adjust their business systems for it.

We understand a concessional mass loading scheme will be introduced nationally. But, once again, although ministers have agreed to that in principle—and by ministers I mean all state ministers—that matter is being voted on out of session by the transport council until 8 June, which is at the end of this week. People want to adjust to these things quickly. So that is also on their horizons.

There is also a revision of the weight tolerances that are allowed nationally on trucks. That will also come into effect on 1 July. South Australia is bringing in new compliance and enforcement legislation that will affect not only South Australian vehicles but also those passing through. There are also new fatigue laws in New South Wales. As well, state ministers are apparently going to increase registration charges on trucks by 2.7 per cent from 1 July. So that is the smorgasbord of issues against which we were considering the issue of this bill and we therefore doubly welcome the transition period that was announced on 1 June.

CHAIR—Thank you, Mr Gow. We will now move to questions.

Senator STEPHENS—Thank you, Mr Gow, for your appearance this morning. Could you clarify for me the announcement last Thursday of the two-year transition regime. Was your industry consulted about that at all?

Mr Gow—We have been consulted about the whole matter from the announcement of the energy white paper in June 2004, directly by government and through a forum called the Fuel Schemes Advisory Forum. That forum is run by the Australian Taxation Office, which puts a lot of effort into consulting with all industries—not just trucking but anybody in receipt or potential receipt of a fuel tax credit—to make sure the administrative arrangements are sound. Certainly, we have consulted with our industry about the issue of the BAS and have engaged with government about that in more recent weeks.

Senator STEPHENS—You have suggested that there might be some compliance costs for your members in the two-year transition regime, in terms of the additional resources needed to try and move to a monthly BAS claim. Taking the time to think about this transitional model, can you tell us whether or not you think it will be workable after the transition period?

Mr Gow—In theory, one would say yes, because we believe it will be workable in the transition period. We have signed up to a transition period and we will be educating our industry to make that transition by 1 July 2008.

Senator STEPHENS—Does the transition regime apply to everyone in your industry, or only to small and medium enterprises with a turnover of less than \$20 million?

Mr Gow—Not only will it apply to everyone in the trucking industry but also a strong point we made in advocating such a scheme was that it should apply to any claimant for fuel tax credits, because businesses are often not singular; they may be applying for on-road and off-road fuel tax credits. People have a variety of interests in their business. It is based simply on the fact that a business is claiming on-road or off-road credits.

Senator STEPHENS—My understanding was that after the two-year transition period it applied only to small and medium enterprises.

Mr Gow—That is not our understanding.

CHAIR—For the committee's information we have obtained a copy of the Assistant Treasurer's press release of last Thursday, I think it was, that sets out the details.

Senator STEPHENS—You talked about other industries that will be affected by the transition period. My understanding is that you can claim the fuel tax credit at the time you pay the fuel tax.

Mr Gow—At the time you purchase the fuel, that is correct. It is a flexible arrangement. You can claim, I understand, on a written form, although we have not had advice from the ATO at this stage on exactly what paperwork will be required. No doubt they are working on that and will inform us as early as possible. That credit would be paid to the business. The ATO, since the institution of these fuel grants from 1 June 2000, under two schemes so far—this is our third, so we are getting quite good at this—is going to be paid in the normal ATO service charter period. The normal payment time to process a claim is about seven days.

Senator STEPHENS—That is your experience generally in the industry—it is paid within seven days?

Mr Gow—That is right. The processing of claims by the ATO for the fuel schemes has been very efficient.

Senator STEPHENS—You tabled the response from the tax office.

Mr Gow—That is correct.

Senator STEPHENS—I am just looking at what they did not agree to do.

Mr Gow—Can I help you with that?

Senator STEPHENS—Yes.

Mr Gow—We asked several things. The thing they did not agree to do was to allow people to claim a fuel tax credit when they are obligated to remit their pay-as-you-go withholding—that is, that section of wages that employers have to remit to the tax office if they are over \$25,000 per year in that category. We thought that an extra box on the form might be a solution. They were reluctant to accept that, but that has now become totally academic since the solution of 1 June was announced.

CHAIR—So you got everything from the tax office that you wanted except one thing, which is now academic.

Mr Gow—That is correct.

CHAIR—You did pretty well.

Senator WATSON—Approximately how long does it take the average trucking firm to fill out the new rebate form? I know it is very quick for farmers. How long would it take the average trucking company to fill out the current form?

Mr Gow—There are three ways that trucking companies purchase their fuel. One is through a fuel card arrangement. They get an account from the fuel card supplier and they would use that as the basis for their claims. That would be extremely quick. Second, they may be bulk purchasers, having tanks in their depot or depots if they are national operators. Once

again, that would be an invoice based scheme, and that would be the basis of their claim. Some, however, who fuel at the pump using their own system might spend some time to aggregate their fuel purchases over the period they are claiming for. Normally, that would be aggregated on their credit card statement or even a fuel card statement so it should be a short process.

Senator WATSON—The current system does not take very long to fill out the form, does it?

Mr Gow—No, and I maintain that in the system envisaged this supplementary claim to the claims that will also be made on the BAS, if appropriate, will also be as quick.

Senator WATSON—Once it goes on the BAS, if you are a quarterly BAS client you may have to wait a month or two before you get your money back. If you purchase early in the period you have to wait until the end of the period plus about 14 days or something.

Mr Gow—That is correct and that is why we asked for transitional arrangements to be put in place, particularly for those smaller businesses that remit their tax obligations on a quarterly BAS.

Senator WATSON—Under the current system, how long does the filling out of the form actually take?

Mr Gow—At the moment, the form merely relates to the total amount of diesel that is eligible for a claim, so an amount of litres is filled in on that form. It does not have to be disaggregated for each vehicle so it is simply a matter of picking up that data from your invoice or invoices from your supplier or your fuel card system.

Senator WATSON—How long does that take from the time you put the stamp on the envelope until the time you aggregate it?

Mr Gow—It is a simple case of looking at one or more invoices and adding them up if necessary and putting it on the form. I would say just a few minutes.

Senator WATSON—In two years time, what is the extra time it will take?

Mr Gow—Let me take one step back. There have been various administrative schemes developed by the ATO in response to industry concerns. For example, if there was non-eligible use of fuel in a bulk supply one can establish by statistics with the ATO that, say, 80 per cent of your fuel use is eligible. You would be able to continue to use that number into the future. There is a little bit of effort to establish that if all your fuel is not eligible, but then it is back to a few minutes in applying, for example, the 80 per cent to the total quantity of fuel purchased.

Senator WATSON—Have you been assured that there will be no incremental movement in the transitional period until the full two years is up?

Mr Gow—We have had a mixed reaction from industry. Some have said they would wish to move straight to the BAS particularly those who are now reporting on a monthly basis because the issue of working capital is not as long term as it is for the three-monthly reporters. There are others who have felt, justifiably, that that would have a real impact on their business—particularly the small businesses in our industry and there are many of those. Some

70 per cent of trucking businesses in Australia are single or small fleets, of about 42,000 businesses. Thirdly, there is a group who have not fully engaged with this change yet and that is simply because the legislation is not through the parliament and an association like the ATA needs to be somewhat cautious in providing advice to its members about what it should do.

Senator WATSON—Absolutely.

Mr Gow—Whereas, in the transition to the first fuel scheme and the general GST arrangements, the legislation was in place some 12 months before the implementation date and we were able to address these issues over a longer period of time.

Senator WATSON—For people who claim their rebate on a quarterly basis, there is no incremental change required for two years?

Mr Gow—There is no change required to the BAS for two years but incrementally they can put in these supplementary claims to gain money along the way.

Senator WATSON—If they wish to.

Mr Gow—Yes; it is an option. We favour options at the ATA.

Senator WATSON—I just wanted to bring that point out. Basically, you are happy with the changes that the Commonwealth has brought about. The impediments or problems that you spoke about really seem to be state based.

Mr Gow—The only state based issue I raised was the fact that—

Senator WATSON—South Australia and New South Wales are two that I recall.

Mr Gow—Those are in relation to heavy vehicle regulation and there are a number of state based heavy vehicle regulation issues around, not only the implementation of compliance and enforcement regimes but also the lack of extension of higher mass limits into New South Wales and Queensland, in a lesser manner. The particular issue I raised was the apparent appetite of state transport ministers using the National Transport Commission's research to increase truck registration fees by 2.7 per cent from 1 July. We note that the Commonwealth has announced it will not increase those under FIRS, the Federal Interstate Registration Scheme—registration from that date.

Senator WATSON—Basically, you can give a big tick off to this bill? You are quite happy?

Mr Gow—We are, and I will leave a copy of the ATA's media release giving that big tick. I will leave that with the committee, along with a copy of our submission to the Productivity Commission inquiry which includes the statistics about the recovery of revenues from the industry.

Senator WATSON—Thank you.

Senator ALLISON—Mr Gow, your submission makes no mention of the effect of the changes on biofuels. Is this because you do not see any problem?

Mr Gow—Generally, that is correct. Biofuels and gaseous fuels have been trying to penetrate the market for some time, as you are well aware. But at this stage the arrangements to apply them to heavy vehicles are extremely limited. We are waiting for more viable

solutions. We believe that the tax regime applied to those fuels is favourable. That is not an impediment to the development of the industry. There are other very practical issues from our industry's point of view that you are aware of—the volume of the fuel because it has less power per unit, et cetera. Many of those practical problems have not been overcome yet. When they are, I can assure you that the trucking industry will be more than happy to take up an alternative fuel if it is cheaper than diesel at \$1.40 a litre.

Senator ALLISON—It is in fact cheaper, as I understand it, for some blends in some areas. Can you spell out what you think those barriers are, with a bit more precision, if I can ask for that?

Mr Gow—The barriers to the uptake of biofuels and gaseous fuels in heavy vehicles—

Senator ALLISON—Can you just focus on the biodiesel?

Mr Gow—are technical issues and supply issues. We know that biofuels produced from canola came to a grinding halt during the drought because the supply of canola seed was not available for refining. There are other feedstocks, as you know—tallow and used vegetable oil—which are also being used but these are not large suppliers and the amount of biodiesel that is on the market is basically being blended into diesel without any effect on its performance.

Senator ALLISON—You are saying that supply is the biggest problem for heavy vehicles in the trucking industry?

Mr Gow—The supply is more a problem for the producers and marketers of those fuels. As I say, diesel has, for example, five per cent biodiesel in it now that there is a standard for that and that does not void any engine warranties for people buying expensive trucks from their suppliers. So there are not any engine warranty issues. The trucking operator is just buying diesel. The problems are more for the producers and marketers to be able to sustain a supply, particularly to market it as B100.

Senator ALLISON—You support the definition of biodiesel being five per cent biofuel and 95 per cent petrodiesel, do you?

Mr Gow—No, all I am suggesting is that a blend of up to five per cent is quite compatible with the warranty requirements of engine manufacturers.

Senator ALLISON—So, by definition, others are not? Higher blends are not?

Mr Gow—No, I am sorry—I am misleading you and me. The technical advice is that biodiesel works fine in any engine even up to B100, but B100 is not available.

Senator ALLISON—As you would be aware, this bill changes the definition of biodiesel to limit it to B5. The industry has suggested in submissions to this inquiry that that will effectively rule out the future of biodiesel in this country.

Mr Gow—I will have to take that question on notice.

Senator ALLISON—You might find it interesting to read some of the submissions that make that suggestion. The trucking associations would not be in favour of that outcome—if I can ask it that way.

Mr Gow—As I say, I have taken your question on notice and we will get back to you. I am not in a position to express a view at the moment.

Senator ALLISON—We have a short reporting time frame. I do not know whether the chair would like to put a time frame on when we would need your response.

CHAIR—The report has to be drafted this week. How long do you think you would need, Mr Gow?

Mr Gow—A very short time. We are familiar with these issues, but I want to make sure that I address the particular issue.

CHAIR—Could you check that and perhaps communicate with the committee—you can do it by email to the secretariat—by the close of business tomorrow?

Mr Gow—Yes, certainly.

CHAIR—Does that suit you, Senator Allison?

Senator ALLISON—Yes, thank you. You have made some recommendations at the end of your submission. Do you agree with a number of others that have suggested that the e-grant proposal should continue to apply in conjunction with BAS statements? Do you see that as a possibility?

Mr Gow—The e-grant had the virtue of being a flexible claiming system, but we feel that the transitional arrangements announced on Thursday are a flexible claiming system that covers off any issues that may have arisen with the loss of the e-grant and other third party claiming arrangements.

Senator ALLISON—I am sorry, I am not up with the announcement on Thursday. There will be an amendment to the bill, will there, to reflect some added level of flexibility? Information comes at the last minute. We will have a look at that.

Senator JOYCE—One of the submissions said that a diesel engine uses about 66 per cent of the fuel requirements of what a comparable petrol engine would use. Would that be a fair statement?

Mr Gow—The energy contained in a litre of diesel is much greater than a litre of petrol and that is why it is used extensively in heavy engines, otherwise you would have to carry more fuel on your vehicle.

Senator JOYCE—I just wanted to clarify that. It is understandable that there is a lot less refining in diesel.

Mr Gow—That was historically the case. Since the imposition, which we accept, of national fuel standards for diesel from 1 September 2003 that set levels of pollutants in diesel—particularly sulphur, which would deliver lower emissions—and then the tightening of those standards from 1 January this year down to only 50 parts per million, the refining cost has gone up considerably.

Senator JOYCE—I am fleshing out some information that has come to me and, since you are here, I want to ask you about why we have a diesel fuel levy when it uses less fuel all up and it is also less to refine. They argue the point that it is also less damaging to the

environment. Seeing you are the ones driving trucks around, what are your views on that issue?

Mr Gow—The view that it is less refined is historical and no longer the case in Australia either for product that is refined here, which has to meet that national standards, or for product that is imported. I do not understand their point about if it has more energy per unit than petrol, why there should be a diesel rebate. I am sorry.

Senator JOYCE—They are trying to remove the diesel fuel levy. Is it right that we pay diesel at a world parity price? Is that correct? Is that what happens at the moment?

Mr Gow—I think they probably include a view about the resource rent tax. Oil produced in Australia is at world parity price—that is correct.

Senator JOYCE—I just wanted to clarify that. I can write back to them and tell them that I asked the question.

Mr Gow—I hope I answered it.

Senator JOYCE—I now have only 299 emails to answer. I am following up on Senator Allison's queries. We have been approached by a number of people who are in the biodiesel industry and produce biodiesel which is 49 per cent tallow based and 51 per cent diesel based. They say that one of the ramifications of this is that, whilst an industry is just starting to get up and running, it will have a major effect on them. You have just said on the record that it does not matter whether it is 100 biodiesel; it will still work. Are you seeing the progression of new, independent fuel bodies around the countryside, apart from the major four oil companies, producing this biodiesel?

Mr Gow—We understand that that is happening, but, as I say, those producers are usually not marketing that product directly. It is blended with diesel, and we know the usual outlets that our people use to buy their other fuel supplies.

Senator JOYCE—Do you think it would be healthy if there were a greater diversity in the market with regard to places where your association members could source their fuel requirements?

Mr Gow—If that diversity were able to address the cost of fuel, I am sure our members would be interested in that. But I have mentioned that, even with the current production and tax arrangements on biofuels, they are not significantly cheaper than petrodiesel.

Senator JOYCE—Do you think it would be worth going in the other direction? Do you think that if there were greater centralisation of where fuel was sourced that that would inhibit any competition in the market? Do you think a greater centralisation of the retailing outlets of fuel would be an unwarranted outcome?

Mr Gow—Certainly generally, considering that I represent such a competitive industry—as I mentioned, some 40,000 trucking businesses from owner drivers through to larger fleets. We have a fundamental article of faith that market competition will deliver a better outcome. So moving towards a more centralised production or marketing arrangement for the fuels you are mentioning would not appear to deliver the outcome we are looking for.

Senator JOYCE—The reason it relates to this bill is that I believe the section that defines biodiesel as five per cent will probably inhibit some of these people coming into the market. Are you aware of the current investment grant arrangements and the ability for people to still claim an excise—that there is a 38c investment grant out there at the moment for people who are producing biodiesel?

Mr Gow—Yes, we are well aware of the program administered by the department of industry to meet the government's target of 350 million litres of biodiesel by 2010.

Senator JOYCE—Do you think there would be any reticence about using new producers of biodiesel in the market?

Mr Gow—No, because the biodiesel producers would have to meet the standards that have been in place nationally under the Fuel Quality Standards Act passed by the Commonwealth parliament some years ago. As I say, provided biodiesel meets those standards we have advice from engine manufacturers that that will not affect the warranties of engines that are in vehicles using biodiesel.

Senator JOYCE—Does your association have any views on how long it would take a new biodiesel industry—basic farmers' cooperatives that are especially evident in places such as Western Australia—to get up and running? How many years would it take for that new sector of the industry to become well established?

Mr Gow—We could not express a view on that. As you say, it is a new industry in Australia, although of course biodiesel has been produced overseas for many years, particularly in Europe. But, as so often with new industries in this country, there are particular and peculiar circumstances they have to address. If, by developing that product, they can get it on the market and compete with petrodiesel—and, considering the price of petrodiesel, that competition would now be more likely than ever—and deliver a product to the national standard that is price competitive, our industry will use it.

Senator JOYCE—Do you think we should encourage the development of that product?

Mr Gow—We believe that there are measures in place to encourage the development of the product already. Government needs to take cognisance of the fact that, should the product develop more, the current cost recovery from heavy vehicles in Australia, which is based on the registration paid to state governments and to the net diesel excise paid to the Commonwealth, is based only on petrodiesel. So, if and when the fuels that you are speaking of gain a larger share of the market, there will not be any cost recovery for those vehicles for their road wear. As an association, we are very conscious of our need and wish to pay our way for using the nation's roads and to be fully recovered for that use. So there is an issue in the development of biofuels about whether or not those vehicles should or should not pay some sort of fuel excise—some level of net fuel excise—to pay for their road use, alongside that of diesel-using vehicles. So our view at this stage would be that we welcome the development of biofuel but, on the other hand, if the market shifts considerably then the burden, if you like, of paying for road use amongst heavy vehicles—currently some \$1.3 billion a year—cannot fall simply on diesel vehicles.

Senator JOYCE—When you talk about the market moving considerably, what portion of the market do you think would be a considerable portion to be held by biodiesel?

Mr Gow—When I say ‘considerably’, I am reflecting on that roughly \$1.3 billion a year. So even 10 per cent would mean an increase on the net diesel excise of petrodiesel-using vehicles to still recoup that same amount to government.

Senator JOYCE—Say if 10 per cent is considerable, five per cent would not be considerable; five per cent would be a minor part of the market.

Mr Gow—That is probably correct but, if it were part of a trend—

Senator JOYCE—I am not holding you to it; I am just—

Mr Gow—If it were part of a trend then, of course, at the point that it reached five per cent, if it had been four per cent the year before and there was a trend, that issue would need looking at.

Senator JOYCE—I am just getting an idea from you. I am not holding you to it and I am not going to quote it back. I appreciate that you are in favour of the amendments that you have in regard to transitional arrangements for claiming of your rebate. Obviously, there was a lot of lobbying that went into getting that position. What do you see will be the case at the end of that transitional arrangement? Do you think your association members will be affected in any way? Do you think that, after the transitional period, they will be in a position to claim their rebate on their tax?

Mr Gow—On their BAS?

Senator JOYCE—Yes.

Mr Gow—We believe so.

Senator JOYCE—Thank you very much.

Senator WEBBER—In view of the time, I will try to keep this as brief as possible. You said in your earlier comments that you think these new transitional arrangements will handle the cash-flow difficulties lots of industries face. How often do your members put in a BAS? Are they monthly, quarterly or six-monthly?

Mr Gow—All of those options are available to them. I do not have any industry wide statistics. Possibly they would be available from the ATO for you. We do not have such statistics but we have always encouraged people to align their BAS cycle with their business cycle. Then it is up to businesses to decide exactly how they do that. Some report monthly; some quarterly. I believe very few would report at a more lengthy period than that.

Senator WEBBER—If they are six-monthly reporting entities—say, people who are owner-operators of prawn trawlers in Western Australia, not so much members of yours—do you think the transitional arrangements will be sufficient to allow them to adjust their cash flow?

Mr Gow—I cannot offer you a view on prawn trawling. We do not have any amphibious trucks yet!

Senator WEBBER—No, it is just that, if they are quarterly or six monthly, obviously they have fewer cycles over which to adjust their cash flow.

Mr Gow—But the transitional arrangements for prawn trawlers or truckies will in fact allow them to claim fuel whenever they wish and then square that off on their BAS, even if it is six monthly. They have two years to look at their business to make that adjustment if they wish to continue to claim after six months, after the two-year period. I believe they will have time to address that transition in their business.

Senator ALLISON—Mr Gow, what can they actually do? What can small operators, for instance, for whom it is a cash flow problem now, do to make a difference in two years time?

Mr Gow—I will just take a very simple example of somebody driving the standard six-axle semitrailer that we all love so much. If they were doing about 200,000 kilometres a year, an average distance for long haul work, they would be claiming about \$1,700 a month in fuel tax credit, on-road credit. That is at the lower rate, not the full excise amount, of course. So they have two years to somehow or other amortise that \$1,700 of extra working capital that they are bringing into their business in that first month, to arrange how to amortise that over a two-year period and get it down to the zero. Then of course it would not have any impact if they are claiming on their BAS—or, if you multiply that by three, which I think is \$5,100, over a quarterly BAS arrangement. It is two years to fundamentally save up that amount of money or pay it off, whichever way you look at it.

Senator ALLISON—I have just had drawn to my attention the remarks of the NFF president, who says the two-year transition does not mean the problem will go away, at least not for farmers. But you think it will for truckers?

Mr Gow—Certainly the ATA will assist people in our industry through education and information. I will be in Melbourne on Thursday at a workshop of some 100 people at least down there who are already inscribed. They are very hungry for information about the legislation in general and this arrangement in particular, so we will be out there on the road putting in our best efforts to make this transition period work.

Senator MURRAY—Mr Gow, there is a minority of every profession and every industry that is less than honest. Can you tell me whether you think that this new system will produce more roting or less roting than the previous system and why?

Mr Gow—History is a good guide to the future, I believe. The interesting thing since the introduction of the on-road grant for heavy vehicles on 1 July 2000 is that it has always run to budget. So there is obviously no macro problem with the claiming systems that have been and are in place for the on-road grant. The budget figures for those amounts have increased each year because of course our economy is growing, the transport industry is growing and owners of vehicles are trying to get more utilisation out of them by using two-up driving, staged drivers et cetera, so more fuel is being used. But the increase in the budget has been aligned with those growth figures, and there was no indication when the ANAO did its report on the Energy Grants Credits Scheme early last year that there are any systemic problems in terms of those less than professional or less than honest people you claim are in every industry. Also, the system that is proposed for this transitional period is fundamentally exactly the same as what is in place now. The fact is that it has to be accounted for on the BAS at the end of your claiming period, so I understand that there are no loose accounting arrangements. They are

not introducing a looser accounting arrangement. Consequently, I can see no change from the current practice and therefore no loss to revenue as you are implying.

Senator MURRAY—As I said to you, there is always somebody somewhere who wants to have a lend of a system. We cannot make perfect systems. Does the trucking association employ an audit or monitoring capacity or do you just leave it up to the ATO?

Mr Gow—We have had a close relationship with the ATO since this system has been in place. We are aware that they prioritise their clients for on-road grants—and, presumably, off-road grants as well, which are not within our area of interest—for farming, mining and rail et cetera, who all get the full amount of their excise back on their fuel usage. For trucking operators, I am aware of individual businesses, whether small or large, that have been thoroughly audited by the ATO and, as I say, no problems emerged within the Audit Office report last year. However, there have been a couple of cases involving off-road grants, including one gentleman in this region who was prosecuted quite early in the new tax system period, and I believe that sent quite a strong signal.

Senator MURRAY—I want to ask you about what are known as the coherent principles approach to tax design, which I happen to support as an approach. Essentially, it means that the law is more principles based than black letter law, and this legislation change is designed with that in mind. But it does mean, of course, that, in the development and application of the law, regulation and administrative guidelines become more important. In the explanatory memorandum there is a telling statement:

1.63 After enactment, the law will continue to be unfolded, where necessary, through practical application of the law, including, as is currently the case, by rulings made by the Commissioner.

Everybody in business should be as alert as possible to that because it can mean that the goalposts shift and the ground shifts under you because the administration and regulation of the process will change over time. Critical, therefore, in that coherent principles system are proper consultation and continuous consultation so that, if administration is changed, the people affected are fully consulted and informed. Do you feel that your access to and consultation with the key regulators and the key bureaucracies such as Treasury and the ATO is strong and that you have a continuing level of relationship? Do you think that you will be consulted properly as the scheme unfolds?

Mr Gow—We certainly believe that to be the case. We were aware of the policy announcements in June 2004, and they were discussed with those agencies as far as we could in that period. Then in May 2005, Treasury put out a discussion paper, as this was the first example of coherent principles based law that the ATA had encountered. Their discussion paper was thorough not only in explaining that approach but in the details of the proposed legislation. Submissions were made on that basis. They were taken note of, in our case before the legislation was drafted. There has been further consultation about the draft legislation, and of course a lot of attention was given to it during the period since it was introduced into parliament at the end of March. We have no issue with the degree of consultation.

Senator MURRAY—You misunderstood the question. The statement says, ‘after enactment’; you are talking about before enactment.

Mr Gow—Correct.

Senator MURRAY—The statement says:

After enactment, the law will continue to be unfolded ...

I want to be assured that you think you have the sort of relationship which will guarantee proper consultation and that you do not get hit with regulatory administrative change for which you are unprepared and which you do not foresee.

Mr Gow—Fortunately, in this legislation, the complications are more to do with off-road fuel tax credits rather than on-road fuel tax credits. I mentioned a forum organised by the Australian Taxation Office called the Fuel Schemes Advisory Forum, which all affected industry associations are invited to participate in—and we do. We have participated in that forum for years. At its last meeting, approximately two weeks ago, we were given draft rulings covering a range of issues generally covered under the bill. So that consultation is taking place even now, prior to enactment, and we would expect it to continue after enactment. But I would emphasise that for on-road credits it is a relatively straightforward story compared to the larger off-road credits section of the bill.

CHAIR—Thank you very much, Mr Gow. That has been very helpful.

[10.06 am

BROCK, Mr Craig William, Director, Industry and Strategy, ACCORD Australasia Ltd
PILKINGTON, Mr David Lloyd, Industrial Manager, Recochem Inc.

CHAIR—Welcome. I invite each of you to make a brief opening statement, if you wish to do so.

Mr Brock—Thank you. I will kick off with an introductory statement and then David will make some comments. Firstly, we welcome this opportunity to present to the inquiry. The industry that I represent has concerns with the bill in that it will fundamentally impact on the business operations of a number of our industry members. My colleague, Mr Pilkington, will be able to explain some of these impacts in detail. For example, Recochem's business will be adversely affected by the changes introduced in the bill in terms of cash flow and finances through the need to increase the company's level of working capital and overall paper work burden. Our industry association has, at last count, 87 member companies, and it is estimated that about 20 of these companies will be affected in ways similar to the impacts on Recochem, which Mr Pilkington will elaborate on for the committee.

An issue with the bill is that its impact mainly targets our members that have Australian manufacturing operations. We have a number of members who import product fully formulated, but those who have chosen as part of their business to participate in the Australian manufacturing business will be impacted on directly by this bill. It is particularly unfortunate, because this segment of the industry is the one that is under most stress from a fairly flat manufacturing economy as well as increasing global competition. Within our membership we have a number of small to medium privately owned Australian operations. Many of these businesses are doing it tough, but they are keeping their heads above water. These companies represent an important segment of Australia's chemicals and plastics industries. For the most part, these are low-margin businesses operating in a very competitive environment.

So why do we have problems with the bill? Our submission presents the following reasons. Firstly, it changes the treatment of key ingredients used by ACCORD members in their product formulations. Hydrocarbon solvents are important in many products made by our industry. These are non-fuel uses. Under the existing system, these ingredients can be purchased for such use without attracting excise—subject, of course, to certain conditions. The bill applies fuel excise at 38.14 cents per litre on these ingredients for these non-fuel uses. Sure, companies can eventually claim this back; the problem, however, is that this whole raft of changes fundamentally changes the business operating model for these companies at a time when they can least afford it.

The key question we hope this inquiry will consider is not whether this is fair but whether it is indeed necessary. As a matter of principle, why should non fuel users of hydrocarbons attract a fuel excise? My colleague Mr Pilkington will elaborate on the actual financial implications for one of the affected companies. Another specific problem we have with the bill is its Greenhouse Challenge provision, mandating that companies receiving more than \$3 million in fuel tax credits be required to join the Greenhouse Challenge Plus. We support the Greenhouse Challenge Plus in Australia's efforts to reduce greenhouse gas emissions.

However, to require companies to join purely on the size of their tax credit and not on their actual carbon dioxide emissions is a poorly targeted policy measure. Greenhouse Challenge Plus needs to be targeted to combustion use of hydrocarbons. The problem is that if the bill stays as it is, it will potentially adversely impact on the credibility of Greenhouse Challenge Plus.

We also challenge what appear to be invalid assumptions regarding how readily many specialty hydrocarbon solvents used by our industry would be substituted for either petrol or diesel in internal combustion engines on two grounds. The first is simple economics. The fact is that many of these materials cost more than the fuels that they would apparently be substituting in the first place. The second is chemical incompatibility with engine parts. The routine use of many of these hydrocarbon solvents, if you were to put them into internal combustion engines, would destroy the asset they are used in. I will hand over to Mr Pilkington now for him to give some details about the financial impacts on industry.

CHAIR—Before you start: may we assume that you adopt what Mr Brock says?

Mr Pilkington—Absolutely.

CHAIR—Okay. Go on.

Mr Pilkington—As a prelude, whilst I work for Recochem, we are the aligned Shell chemicals distributor for Queensland, the Northern Territory and Western Australia. I have also spoken to our sister Shell distributors, Auschem in New South Wales and Oilchem, who represent Shell in Victoria, South Australia and Tasmania. I have also spoken to competitive distributors because I was the only one coming to this forum and the other companies, ASCC and GSB in Victoria and Queensland, will also be affected in the same way we will be by this bill—only the detail will be slightly different.

Firstly, I will talk about the financial impact. The announced transitional changes are a good start. We understand, the same as Mr Gow does, that we will be included in these transitional arrangements. We currently remit excise weekly and we see that in future or during the transition we would be able to claim that excise back weekly. That is the only way that we would take no impact. Otherwise, we are talking about an impact of a substantial sum of money of extra working capital for ourselves in the region of \$700,000. For the other companies I have mentioned it would involve similar sums, and they are businesses whose turnover is only of the order of between \$20 and \$50 million, depending on which one. The other thing, as Mr Gow mentioned, is that we do not want this to occur again in two years. What we need to do is to ensure that the transitional arrangements just allow time so that we can get this in place with minimal impact.

We are also very concerned about the cost of compliance. Under the current regime, we and our customers operate under a system of remission certificates or continuing permissions from the ATO to obtain the products excise free. Currently, in Queensland, we have 30 customers who have remission certificates from the ATO. We have just done a mail-out, and there are 150 customers in Queensland who will be affected by these changes. They range from major multinationals to small mum and dad companies with two employees. Nationally, because the transitional arrangements have been unclear, we believe that excise will apply down to packs as small as one litre of certain products. That has already caused a stir amongst one of the

national retail chains, who have asked not to be mentioned. I have an eight-page email circuit going with them. However, it will affect all of the other retailers, and they do not know what is going on.

The other problem, of course, is the change in IT. We believe there is going to be a substantial problem with IT systems for a large number of companies. In our case, a new charge similar to GST will need to be introduced within the IT system. We believe many of our customers will be affected in the same way. We have had several sessions with the ATO. We believe that all products down to a one-litre size will now attract the excise. The only exemptions will be packs of mineral turpentine, kerosene, white spirits and high-flash kerosene, which will be exempt in pack sizes of 20 litres and less. These are the products that you buy at your supermarket or hardware store. However, there are related products which will also be affected. The other thing is that, as with fuel prices, solvent prices move with oil prices. We import some solvents; they are made from oil; we pay overseas oil prices. We also buy locally from various producers, and the prices move monthly with the oil prices. So, if a solvent is more expensive than fuel today, then it will be more expensive next month or next year.

Also, we have many blends which are totally unsuitable for use in an engine. Most paint thinners contain things like acetone or MEK, which will chew out hoses and seals, so such products should be automatically exempt. In those blend applications, we have identified—and I am sure other people will identify others—thinners, degreasers, printing washes, tyre shines, concrete form oils and timber treatments. What we need from the ATO in the case of these products is some blanket approval, where, if you have X per cent of a certain component, you get automatic exemption. Otherwise every one of the chemical formulating companies is going to be running to the ATO for individual approvals.

Bad debts are a major problem. If we have someone who goes down owing us a quarter of a million dollars at roughly a dollar a litre, they will now owe us another hundred thousand dollars. Under the current set-up, we believe that we will not be able to get that money back as we would if it were a GST system.

We believe Greenhouse Challenge Plus is a good institution, but it does not apply to companies like ours—we do not use energy. We report solvent emissions through the national pollutant inventory anyway, so those emissions are already covered. One of the things that I find interesting, since we act as distributors for Manildra ethanol as well, is that on the hydrocarbon side of this equation a very hard line has been taken, whereas on the ethanol side the whole system has in fact been freed up. The excise on potable ethanol is about \$60 a litre, so it is interesting. I hope that our contribution to this debate helps everyone obtain the correct outcomes, that revenue is protected for the government and that we end up with simple, easy to understand and administer, excise-free solvents for industry. Thank you.

CHAIR—Mr Brock, do I understand the point of what you and Mr Pilkington have been saying to be that you maintain that the non-fuel use of hydrocarbons by an industry such as yours ought not to be excisable?

Mr Brock—As a matter of principle, that would be the ideal outcome we would seek. That has been the way the existing arrangements have worked, to a certain extent—by continuing

permissions and the remission certificates. They basically recognise that those uses are non-fuel uses and that the fuel excise, therefore, can be dealt with through those administrative arrangements.

CHAIR—I was just going to ask about that. What happens now? Is it that the solvents that you use that are hydrocarbon based are excisable but there is a remission from the ATO in respect of non-fuel uses of those hydrocarbon based solvents?

Mr Brock—That is correct. There are some conditions on that. Probably David Pilkington, who is involved with that, would be able to explain some of those conditions.

CHAIR—I do not really need to know the administrative details. How does that change under the new bill?

Mr Brock—The new bill will remove all remission certificates. The new bill introduces a new philosophy that everyone pays the excise on things that are excisable and then receives a credit, in the form of a fuel tax credit, at a later date.

CHAIR—Yes, I understand that. What is the bottom-line position for your industry? Won't the credit replace the remission?

Mr Pilkington—Yes, and that is fine. If we can do claims and payments to the ATO back to back, we will not have an issue.

CHAIR—So the issue for you is not that your bottom line is going to be changed, at least in theory; it is basically a cash flow issue for you?

Mr Pilkington—Yes.

CHAIR—And that is all?

Mr Pilkington—No, we also have those other technical issues. But that is the main one.

CHAIR—But it is not as if an essential product of your industry is going to attract excise under these arrangements which it does not attract at the moment or that some method of remission is not going to be available to you that is not available at the moment; it is merely a change of the method by which that remission is paid to you. Is that right?

Mr Pilkington—Yes, that is correct.

Senator STEPHENS—You touched briefly on the impact of the transitional arrangements announced on Thursday. Would you like to elaborate on how you think they might affect your industry?

Mr Brock—We have not had a lot of time to digest those changes. At the moment we are presuming that those changes will cover our industry. It is what we understand, to some extent.

CHAIR—Have you seen the Assistant Treasurer's press release, Mr Brock?

Mr Brock—We have. It does mention the paint industry, as such, so we are assuming that that will also then apply to the formulators within our industry sector who generally make cleaning products and so forth.

CHAIR—We will inquire of the Treasury officials who give evidence later in the day to clarify that point for you.

Mr Brock—That would be worth clarifying.

Mr Pilkington—It is covered in the press release. Paragraph 7 of the press release says:
... businesses who use fuel other than as fuel or use burner fuel.

CHAIR—That would appear to cover you.

Mr Pilkington—Yes.

Senator STEPHENS—As Senator Brandis said, we will clarify that with the Treasury officials. You mentioned the fact that you had also been in consultation with the ATO. In discussions about the other concerns that you have regarding the cost of compliance, hydrocarbon solvents, bankruptcy, liquidation and the Greenhouse Challenge, what has been the ATO's attitude to those concerns?

Mr Pilkington—Originally, we thought we had agreement on the small packs and products which could not be used in a vehicle. We thought we were going to get automatic exemption. We found later that that was not the case and only the certain products that I listed—mineral turpentine, white spirits, kerosene and high-flash kerosene—will be exempt. The blends are not going to be exempt as of 1 July, and that is going to cause some major problems. That will mean that every paint company will need to go to the ATO to get an exemption for every thinner blend they sell.

Senator STEPHENS—That is a significant unintended consequence, one would imagine.

Mr Pilkington—I am sure Mr Hambrook will address that later.

CHAIR—But presumably, if you are right about that, that could be fixed up in a regulatory fashion?

Mr Pilkington—One would hope so.

Senator STEPHENS—Did you get any comfort from the ATO regarding the bankruptcy and liquidation concerns that you had?

Mr Pilkington—Unfortunately not. The only feedback we have had from the ATO is third hand. I spoke to the General Manager of Oilchem in Melbourne, who spoke to the ATO. Their view is that this is an excise and therefore it is not refundable but that GST is a tax and therefore it is refundable. From a business point of view, we really do not care what it is called, if we are out of pocket by a substantial amount of money.

Senator STEPHENS—It could be a significant amount of money—for example, as in the case study that you provided to us this morning. You have raised what I think is quite an important issue about the Greenhouse Challenge Plus. Have you had any discussions about that with the Greenhouse people, or with anyone?

Mr Brock—Not really at this stage, Senator. We hope that by raising it though this inquiry we will get Treasury and others looking at it. It appears to be an unintended consequence of the drafting of the bill.

CHAIR—It does. If you do not burn any of this fuel it is hard to see how greenhouse issues apply to you.

Mr Brock—I would agree. It does appear to be an anomaly, and in the finalising of the bill it is one that should be corrected.

Senator MURRAY—I agree your industry is very important since you apply your products in just about every possible circumstance you can imagine. In your point about bankruptcy you say that at present if someone goes bankrupt the GST component of that bankruptcy process is effectively refunded to you; you are not exposed to that portion. That is correct, isn't it?

Mr Pilkington—That is my understanding. I must clarify: I am a chemist and a sales guy, not an accountant. That is what our accountants tell me.

Senator MURRAY—I cannot remember that provision but if that exists that is very helpful to people in bankruptcy circumstances. You then say that you know that the excise will not have the same concession available to you and that that could be a very significant exposure.

Mr Pilkington—Absolutely.

Senator MURRAY—We will ask that question of the Treasury officials as well. But just so we can get an idea of the extent of the problem, rather than being theoretical, is bankruptcy a big issue in your industry? Are there a large number of people who go bust? Is the exposure unusual or is it a normal business risk?

Mr Pilkington—It is a matter of public record so I can answer that a very large chemical company in Queensland burnt to the ground last year and we were owed more than \$250,000.

Senator MURRAY—That does not answer the question. Bankruptcy is a general condition which applies across all industries. I just want to know whether in your industry it is more a feature than in other industries.

Mr Pilkington—I would not think any more or less.

Mr Brock—I would agree with that statement. It would be the same as most other manufacturing industries in terms of the rate of bankruptcy—no more or less.

CHAIR—I suppose you would have to examine the comparative figures. But you have no reason to believe that it is otherwise?

Mr Brock—Exactly.

CHAIR—Thank you very much, Mr Brock and Mr Pilkington, that has been very helpful. You are excused.

[10.29 am]

HAMBROOK, Mr Michael, Executive Director, Australian Paint Manufacturers Federation Inc.

CHAIR—Thank you for appearing before us this morning. I invite you to make a brief opening statement.

Mr Hambrook—We have a very simple case to make. We are the downstream users of the solvents that companies such as Michael Pilkington's supply.

CHAIR—Let me just get the relationship straight. Your industry is the purchaser of product from companies like those represented by the previous witnesses.

Mr Hambrook—Yes, that is correct. Most of the paint companies buy their solvents from companies such as Mr Pilkington's company.

CHAIR—All right.

Mr Hambrook—I will make a very brief opening statement. We have a very simple situation: the paint manufacturers buy the solvents and they turn them into cans of paint. There is currently no excise duty payable on those solvents because, as I said, they are turned into cans of paint and you cannot really run a motor car on a can of mission brown. So the companies simply do not pay the excise at all. Under the new provisions, as we heard earlier, Mr Pilkington's company will be invoicing the paint companies within two weeks of delivery of the paint, and the companies will have to fork out that money and then they will claim it back through their BAS. We have done a survey of our members and we would estimate that two-thirds do quarterly BASs, so they are left having to carry that amount of cash for a couple of months. We have actually found one company that does an annual BAS, but I think that is rather exceptional.

In our submission we did a rough estimate of what was involved cash wise. The total usage of solvents is over 42 million litres and, if you multiply that by 38c a litre, it comes to about \$16 million. That might not sound like a lot of money, but actually it is if you add \$16 million overall to your cash flow and you are paying an interest rate of about nine per cent or so. So it does have a significant financial impact on the industry. Not only is there the financial impact on the industry but there is also the red tape. Where you have no reporting requirement at all for the purchase of the solvents, and then suddenly you do, you have an impost. Again in our submission, which you have seen, we have cited comments from individual companies. I will not go through them now. They are simply saying, 'This is going to be a significant problem for us.'

I can very briefly put the paint industry in perspective. This is not a growth industry. Twenty years ago, there were about 156 paint companies. Ten years ago, we were down to about 120. Today, we are down to about 50—and possibly, shortly, we will be down to 49. It is not just the number of companies that is decreasing; the actual production levels have fallen for three years in a row. In fact, we made less paint last year than we did 12 years ago, in 1994. So the industry is shrinking. On the other hand, imports are increasing. Last year, imports were up seven per cent. That is a nice rise.

Senator MURRAY—Just so I understand you: you are saying that the paint industry growth runs at the same pace as the economy, but it is the import sector that is taking that growth, not the domestic sector?

Mr Hambrook—No. In the paint industry, local manufacturing is not growing at the rate the economy is growing; in fact, it is actually falling.

CHAIR—Senator Murray's point was: is that because of competition from importers or is it because the aggregate volume of sales from all sources, both domestic and imported product, is reducing?

Mr Hambrook—There are actually two reasons: one is imports, because they have increased substantially; and the other is that we are importing a lot of pre-painted products, such as metal—for example, the steel for roller doors is coming in coated.

CHAIR—So is less paint being sold in Australia now than was the case a few years ago?

Mr Hambrook—Absolutely correct, Chair. Less paint is being sold in Australia.

CHAIR—Sorry, Mr Hambrook. Please go on.

Mr Hambrook—The point I simply make there is that this is not a rich and affluent industry, so when additional costs get lobbed onto the industry, particularly the small to medium sized businesses, that is really going to hurt them. These are the guys who until now have not had this as a worry on their books at all. But now they are doing their quarterly BAS, they have to churn out the money to pay for the solvent within a few days of receiving the solvent, and they will not get it back for two or three months.

The only other point I want to make, if I may, is that the deferment for two years is excellent news. It is very encouraging but, as I think your committee noted in some of the earlier questioning, it is not a solution; it is just a deferment of the problem.

CHAIR—I suppose that is what transition periods do. The whole point of them is not to change the policy but to give people some time to get used to it and adjust their arrangements so as to give them a greater capacity to anticipate what is to come.

Mr Hambrook—I think they would have very little room to adjust their arrangements, because the basics are still very simple. They are going to be required—where they are not required at the moment—to front up with the money and pay the excise duty within two weeks of receiving the product or even less. They are going to have to do that. Unless they change from a quarterly BAS statement to a monthly BAS statement, they are going to be seriously short of cash. They could change to a monthly BAS statement and that would add work for them. Our understanding is that the government's intention is to reduce red tape. To conclude, I ask the simple question: is this necessary? I do not think it is. We believe there must be a way around this. There must be some way in which paint companies at least can be exempted. We do not believe it is an either/or situation in which either paint companies will be exempted or the whole system will fall apart. We think there must be some solution in the next two years.

CHAIR—You just want exemption from the scheme. That is basically what you are asking for?

Mr Hambrook—Basically. We believe some form of exemption should be achievable.

CHAIR—I suppose you would say there would not be a cost to the revenue, because it is reclaimable as an input anyway, and that the only effect would be to fix up your cashflow problem?

Mr Hambrook—That is correct. There would be no cost to revenue, because no-one argues that paint companies should pay excise on solvent used in a can of mission brown.

Senator MURRAY—Unlike the trucking association, you are saying the existing remission system is very simple and easy to administer and follow.

Mr Hambrook—From a paint manager's perspective that is absolutely correct. It is very simple. They are exempt.

Senator MURRAY—So you are saying you are going from a simple system to a more complex system?

Mr Hambrook—That is correct. Even with the interim position you are going to have a requirement that they report their purchases and then get a refund—which will come out very quickly—and they would do that before they submit their normal quarterly BAS statement. So, if I may say so, you would have a mini BAS statement followed by the real BAS statement three months later. So even the interim position is hardly an advantage.

CHAIR—Thank you, Mr Hambrook. I think you have made your point very clearly.

Senator WATSON—You talk about quarterly BAS statements, but wouldn't people like Wattyl, Dulux, Berger and Bristol be on monthly BAS statements?

Mr Hambrook—That is absolutely correct. As I said at the beginning, we are really looking at the small to medium sized companies who do quarterly BAS statements.

Senator WATSON—How many manufacturers of paint do we have in the small range? What is the split between large and small in terms of numbers or percentages?

Mr Hambrook—At the moment, the largest company is Dulux, the second largest is Wattyl and the third largest is Taubmans. They have bought out many companies over the years, so they have a lot of brand names. But we have 50 companies, so there are still another 47 companies after the big three.

Senator WATSON—So you have 47 small to medium sized paint manufacturers in Australia?

Mr Hambrook—Yes. There are one or two industrial companies. You have your big ones—Dulux, Wattyl and Taubmans—and then you have a couple of industrial companies like Akzo Nobel and two or three other large and medium sized companies.

Senator WATSON—So there would be monthly supplies.

Mr Hambrook—That is correct. But you would probably end up with about 40 companies that are doing quarterly BAS statements.

CHAIR—Are you able to tell us, even if it is only an estimate, what percentage of the market the 40 small to medium enterprises represent?

Mr Hambrook—It certainly is a much smaller percentage.

CHAIR—Wattyl, Taubmans and Dulux comprise, between them, more than 50 per cent of the market, presumably.

Mr Hambrook—That is correct. In rough terms, you would probably be looking at about 35 to 40 per cent of the market in volume for the small companies. But I think there is still an important point to be made here. While you have the larger companies who will still be affected by this, because of the additional paperwork, I believe that we tread in dangerous waters when we turn our back on the smaller paint companies.

Senator WATSON—Yes, that is a point. But how is it that there will be extra paperwork? At the moment you just supply your invoice totals, as it were, and that is all you will be doing on a BAS statement, isn't it?

Mr Hambrook—They would now be required to establish an audit trail of the quantity of solvent that is purchased. They would probably have solvent deliveries coming in every day—or every second or third day—from different companies. That is for the larger companies but it would be at least once every two weeks or so from the smaller companies. Now they would have to track that coming in, and they would have to track the 38c a litre excise payment. Then they would have to track when that product is sold. In actual fact there would be quite a complex paper trail. One of the companies, in their submission to us, said, 'We would have a significant problem in doing this. We would have to introduce disciplines that would ensure the rebate system was accumulated and deducted accurately and promptly. The current system is simple for end users.' Another company said, 'We do our BAS statements on a quarterly basis. To do it monthly would involve our admin staff in a lot of extra work.' There would be quite a bit of accounting and auditing.

Senator WATSON—But even for the purpose of the new arrangement you would have to be able to satisfy yourself in establishing an audit trail, because the integrity of the system, as I understand it, is not changing.

Mr Hambrook—There are two things. One is that they are taking on board the solvent they are purchasing. That would come in; it would be a raw material and it would just go into normal processing. But the key thing now is that you have to track the 38c a litre. You have to ask: am I accurately accounting for that 38c a litre that I have had to pay to my supplier? Am I claiming it back at the right time from the ATO? So you now have a parallel tracking system.

Senator WATSON—But you have to do that at the present time.

Mr Hambrook—Not at all; they do not pay the 38c.

Senator MURRAY—An automatic remission statement, you are saying?

Mr Hambrook—Yes. They do not pay it at all at the moment.

CHAIR—That came through clearly from the previous witnesses, as well.

Senator STEPHENS—I think you have explained the situation of your industry very well—thank you very much; I can see that there is a very logical argument for maintaining some kind of a system for your industry. You did make the point about why your industry, in the same way as others such as primary producers and charities, cannot be granted exemption. Thank you for your submission; it has given us a lot of food for thought.

Senator MURRAY—It seems to me that, as far as matters of scale are concerned, this is an easy one for the government to solve. You heard earlier witnesses from the Australian Trucking Association talk about 40,000 small and large businesses. That is a considerable administrative issue in terms of scale. Just let me understand absolutely the scale of your industry and involvement in the remission certificate system. Is it just the 50 companies you mentioned or are there more companies than that?

Mr Hambrook—No. We are only looking at the 50 companies—plus or minus a few—that manufacture paint and ink. Of all the paint manufacturers, 97.6 per cent are members of the APMF. You are looking at about 50 companies, and that includes three ink companies. You are looking at probably not more than 40 companies that will be substantially affected by this bill.

Senator MURRAY—So for the government to continue a system which seems to work very effectively—at least from the user's point of view—and only affects 50 people, which is easy to administer and track, it does not seem that there are any issues of scale that would make it attractive to the government to impose a \$16 million extra financing cost on your industry at a nine per cent interest rate. That seems a little high—but, if interest rates rise, it will reach that anyway.

Mr Hambrook—I agree with you, Senator Murray. There are not a lot of numbers there, and we think that it should not be too hard. We would hope that, in the two-year interim period, this committee might recommend some mechanism be established that would provide permanent relief. We do not want to wake up two years down the track and find that we have this little nightmare in front of us.

CHAIR—Your best point, I think, is that there is no cost to revenue.

Senator WEBBER—Yes.

CHAIR—We have the best minds in the land in Treasury who will, no doubt, be able to address the issue.

Senator JOYCE—Mr Hambrook, your organisation has been lobbying our office about this issue. What you have put forward today clearly outlines your case, and hopefully we can come up with some reasonable arrangement for your industry.

Mr Hambrook—Thank you, Senator. There are small paint companies all over Australia that are hanging in there—from Western Australia to Tasmania. Let us not damage these guys.

CHAIR—Thank you very much, indeed, Mr Hambrook. That was very helpful.

Proceedings suspended from 10.48 am to 11.04 am

GRUNDELL, Mr Harold, Executive Director, Transpacific Industries Group Ltd

PULLINGER, Mr Robert Lenard, Director, Australian Oil Recyclers Association Ltd

Evidence from Mr Grundell was taken via teleconference—

CHAIR—We will now take evidence from Transpacific Industries Group Ltd, who appear by teleconference. I also welcome to the table Australian Oil Recyclers Association Ltd. Before we begin, can I indicate to everyone that submission No. 20 from Transpacific Industries Group Ltd has, at the request of that company, been marked as a confidential submission. Mr Grundell, you are appearing at the moment in public proceedings. There are other people in the room, including possibly representatives of the media. I want to make sure we understand each other.

The course I propose is that, if senators have questions which you, Mr Grundell, consider might impinge on the confidentiality of your submission, you should indicate that before answering any question. Senators who wish to ask questions of Mr Grundell, please be sensitive to the fact that the submission is a confidential one. I assume it contains commercial-in-confidence information; therefore, do not quote from the submission or reveal its content. Subject to those guidelines, I do not immediately see any difficulty in proceeding in this public forum. Do you have any problems with that approach, Mr Grundell?

Mr Grundell—No, not at all.

CHAIR—Thank you. Would either of you like to make a brief opening statement?

Mr Pullinger—I gave a copy of the submission to the committee secretariat.

CHAIR—Perhaps it could be circulated; nevertheless, would you make it orally, please.

Mr Pullinger—Yes, certainly. The Australian Oil Recyclers bring an important job to the Australian economy in regard to environmental issues. Currently, we collect over 200 million litres per annum of used oil. A lot of it is in capital cities but it is also in regional and remote areas from mines and farmers. As an example, one litre of used oil can contaminate one million litres of drinking water if it is allowed to leach into the system. From an economic position, we are now a net importer of crude oil. Used oil helps adjust the imbalance and reliance on overseas crude as well as the balance of payments. In five years, used oil will have replaced one billion litres of imported crude into the Australian economy and will continue to do so year after year. By utilising used oil as a fuel for industrial purposes and as a lubricating oil, Australian companies save enormous amounts of money, as a recycled product is generally cheaper than the imported virgin product. From a social perspective, the industry employs in excess of 400 people directly in all states of Australia. Nearly all of these people are employed in small- to medium-sized enterprises. They collect used oil in capital cities but, more importantly, in rural, regional and remote areas of Australia.

The changes to the Excise Act as currently proposed will severely affect the ability and viability of oil recyclers and collectors to survive in business and to continue and collect trade in used oil. It will also put in jeopardy the government's goal and strategy of taking used oil out of the environment. Oil recyclers have been captured by this legislation to the detriment of our industry, we believe.

The greatest challenge we face at the moment is markets. The markets for used oil and oil generally are shrinking because of gas and other areas that are not excisable. Securing markets and keeping them is probably one of the major issues that face our industry. We have looked at some markets in the past and discussed them with the ATO. Who determines what a transport fuel is? Is marine fuel classed as a transport fuel and therefore subject to excise, even though the product may be going overseas? Are collectors of used oil to come under ATO excise control? Before a collector picks up generator, filtered and dewatered oil, is the waste oil excisable? We cannot seem to get answers to these questions from the ATO at this stage.

One of the major issues in this legislation is cash flow. I have heard the paint people talking about the same thing. We have a similar exercise and so cash flow is probably one of the major problems for our industry, because the companies tend to be small to medium enterprises, apart from Transpacific Industries, which is a national company. This new legislation will effectively cost \$73 million in excise, which oil recyclers will have to find in order to fund their obligations under the Excise Act. Should a customer go bankrupt, all of a sudden that means the oil recycler loses a lot of money based just on the excise he has paid. As an example, an oil recycler will currently sell a filtered dewatered product for approximately 15c a litre. If you add GST, that is 16.5c a litre. Under the new excise regime, that product will go to 58.5c a litre, and customers are saying, 'We can't afford it,' from the cash flow perspective of their businesses as well.

CHAIR—But only temporarily, subject to getting it back.

Mr Pullinger—Correct.

CHAIR—So this is a cash flow issue?

Mr Pullinger—That is what I said originally. It is a straight cash flow issue, but the small customer looks at how they fund it over a period. Of course, what Senator Dutton put out—or is it Mr Dutton? I am not sure—

CHAIR—Mr Dutton, whom I know very well, would be mortified to be described as a senator!

Mr Pullinger—Please, let us not have him mortified at this stage. We can see that the customer will get their excise back, but that does not help the supplier of the product. Another recycler from Western Australia was informed by the ATO that they will have to pay excise on stored product, which is ridiculous, because he stores the product trying to get rid of it, and it will cost him \$2.7 million in excise should this legislation go through.

The other area that we are concerned about is consistency in the application of the legislation. Under the information paper, *Excise tariff reform—recycled fuel products*, solvent, if it is reused in the business, is not considered manufacture and therefore is not subject to excise. Our company has been informed by the ATO that we will have to pay excise on recycled product used in manufacture of our business, so the consistency issue does not seem to be coming through.

In the same paper under the heading 'How are recycled fuel products affected by the changes to the excise tariff?' the ATO and Treasury recognise that diesel and petrol are part of

a used oil product through leaking into the sump and they are now going to tax that product twice. From what we understand, Treasury is using the line, 'It is more than 55 parts per million of sulfur, so therefore it cannot be the same product.' This is ridiculous, in as much as the 50 parts per million of solvent is brought about by the degradation of the fuel oil and the diesel and petrol coming into contact with high-sulfur lubricating oils. Again, the same product has had excise paid on its original manufacture and now it is being paid again, so it is a double taxation issue, which probably brings in the validity of the legislation as it relates to our industry. To us, it is double taxation and excise on secondary manufacture, and I think the ramifications of that should be looked at.

We accept that, if recycled products are refined, they are subject to excise because a new product is produced. However, we do not produce new products; all we do is recover and clean up products that are already there. So it is not that we are actually making a new product or changing the molecular structure of a product. We use the same products that are already there and just recover them for use. And it comes down to refining: what is refining as it relates to used oil? Only one company currently claims a refined product; therefore, the manufacturing side of things is not consistent with the intention of this legislation. As far as I am concerned, that is fine.

CHAIR—Thank you very much, Mr Pullinger. Mr Grundell, do you have some opening remarks?

Mr Grundell—Thank you very much for the opportunity to make a submission on behalf of the Transpacific group. Just to reiterate some of the things that Mr Pullinger has already covered—obviously, they affect our group in much the same way—

CHAIR—Can I just stop you there, Mr Grundell. Should we take it that you adopt and agree with what Mr Pullinger has said?

Mr Grundell—In the main, yes.

CHAIR—Right. To the extent that there are important differences, you will let us know, all right?

Mr Grundell—Absolutely. There are some implications from an industry perspective. A lot of the—

Senator MURRAY—Chair, I do not know what is happening, but it is becoming difficult to hear.

CHAIR—We are having some difficulties.

Mr Grundell—Is that better?

Senator JOYCE—Yes, if you pick up the phone that would be better.

Mr Grundell—Okay. I will just give you an indication of some of the practical things we are up against. We have recently met with ATO officials to discuss the impact of the legislation and the changes et cetera, but there are still some to be confirmed. We have a situation where we have to inform customers that their prices are going to go up by 38c a litre as of 1 July, but we cannot do that with any surety at the moment because there are things that are still up in the air. I am concerned that we are going to give customers two days notice that

their prices are going to effectively double and, in some instances, more than double. These customers have never been privy or exposed to the excise regime before.

CHAIR—Can I just interrupt you, Mr Grundell, to draw your attention to the fact that this bill will go to the Senate next week and, whatever this committee decides to recommend in its report and whatever the government's response might be to any such recommendations, I think you would have a pretty good idea what the state of play is going to be by next week.

Mr Grundell—Yes. That is reassuring, but it still gives us only a very short window to communicate these changes to our customers, and that is an issue in itself. There are cash flow implications. To give you an idea of the quantum in terms of the Transpacific group, we are currently picking up between 60 and 70 per cent of all the used oil across Australia. Looking at that in isolation, the impost on our business is going to be to the tune of \$800,000 on a weekly basis that we have to fund and find. Our customers are typically on 30-day payment terms from receipt of invoice, so it will be anything up to between 60 and 90 days before we see a return of those moneys expended, which is a major hurdle for us and, I am sure, for all recyclers in general.

Also, we are effectively more than doubling our debt levels and exposure to the businesses. In terms of a customer becoming insolvent, what hope, if any, do we have of recovering those funds, given they will already have been expended? The whole notion of imposing excise on a product that in no way, shape or form has any chance of being used in internal combustion engines is a bit beyond us as recyclers, but that is what has been decreed to date and is I think something that needs to be properly investigated and looked at.

Getting back to issues of recovering materials from the various recycling processes on which excise has already been paid, those materials if double-excised will not be viable in any way, shape or form, and therefore will not be saleable. What do we do with those materials and how are we going to place them in the future? The very nature of the changes in the bill will preclude our participation in some markets and therefore restrict the movement and placement of materials on an ongoing basis. Our usage patterns, whilst in the main uniform, in some instances are not, and that requires us to stockpile and move materials on a regular basis. If we have to pay excise on those materials, with quite likely six- to 12-months waiting on recovering that in terms of selling the material, that also imposes a severe impost on the business going forward.

As an industry, we are recovering what would otherwise be quite a harmful substance from the environment and putting that to use as an alternative fuel or putting it back into the system as a quality lubricant. The industry is continually evolving and looking to utilise sustained outcomes in the placement of materials. The markets for recovered or alternative fuels are continually under threat and pressure from gas or coal or a combination of both. We are going to find it increasingly difficult to place material, particularly if it is carrying the burden of 38c a litre excise. We want to bring these things to the attention of the committee and the public in general to ensure that everybody fully understands the ramifications of these changes to the recycling industry. We believe that we are caught in the crossfire of the government's objectives in placing this bill on the table. I do not think the effects of this on us as an industry are fully appreciated.

Looking at the Transpacific example where we have four or five different operating companies all performing the same task—that is, collecting used oil and recycling it—if we want to move raw materials between those businesses we have to pay excise to do that, which is not currently the case. It is, yet again, another impost on the business. I would think that it is not intended by the bill but it is a consequence just the same and something that we have to deal with going forward.

We believe it warrants further investigation. We are also conscious of the fact that 1 July is not too far away and we do not have a lot of time. We would absolutely like it to be investigated—particularly the cash flow implications and the fact that excise on recovered materials on which excise has already been paid is going to be levied again. It really needs to have some serious looking into to ensure that the best possible outcome is being achieved for the industry and more certainly for the environment.

CHAIR—I have a question for each of you. I want to make sure I understand this. Do either of you say that, as a result of this bill, there is an aspect of your business which will be subject to a tax which will not be rebatable that you are not subject to at the moment? In other words, is this essentially a cash flow issue for your industry or do you say that you are subject to a new liability?

Mr Grundell—We are certainly subject to a cash flow implication.

CHAIR—Yes, I understand that.

Mr Grundell—Secondly, petrol and diesel that is recovered from waste or oil currently enters the market duty paid. From 1 July there is no mechanism in the new bill to accommodate this. Therefore, it will be excised again.

CHAIR—You have used the expression ‘double excise’. That is an additional liability for which there is no form of remission or rebate?

Mr Grundell—Correct.

CHAIR—Is that the case, Mr Pullinger?

Mr Pullinger—That is correct. I think cash flow is the major thing as far as the collectors/recyclers are concerned, and there is no remission provision in the bill for product that has already had excise levied on it in its primary manufacture.

CHAIR—But isn’t this recoverable as an input through the GST system?

Mr Pullinger—Not at this stage, as I understand it.

CHAIR—We will clarify that.

Senator STEPHENS—Thank you, gentlemen, for yet another interesting submission. Neither of you made much comment about the transitional arrangements announced by the minister last week. Mr Grundell, in your submission wasn’t one of the proposals that, if deadlines for adjustment and payment of excise returned to a monthly cycle in line with the BAS deadlines, that could help alleviate the situation?

Mr Grundell—That is correct, yes.

Senator STEPHENS—Do you have any other comments to make about the transitional arrangements?

Mr Grundell—It will absolutely work in favour of the customer. The customer will be able to claim back the excise paid virtually immediately that the material is delivered, and they can then make an adjustment when they do their BAS, be that quarterly or monthly. That is great for the customers, but there is no obligation on them to pay us on our invoices for fuel supply any earlier than is currently the case. So it does not really help the recyclers' cash flows. It certainly helps the customer.

Mr Pullinger—In the written submission I gave to you I made a comment regarding that; it said:

Whilst the Minister for Revenue's statement ... listened to the issues raised by the National Farmers Federation and the Australian Trucking Association, the same concerns raised by our members were not addressed at all.

Effectively, you have two different people. You have the supplier, who supplies the product, who pays the excise straightaway, within a weekly settlement. Then you have the customer, who works on 30- to 60-day terms. To some degree, it is back to front. The transitional assistance should have gone to the suppliers, so that they could claim the excise back, because they are the ones who are paying it, not the customers. So it is around the wrong way, to some degree.

Senator STEPHENS—Yes.

CHAIR—It all comes back in the end, though, doesn't it?

Mr Pullinger—Not necessarily. Again, we get back to the cash flow issue. Take the example of dealing with a trucking company—and our products generally do not go to trucking companies; we go to industry, more than anything—which pays 30 to 60 days after the end of the month. If they claim the excise back in a week, they get all of their money; so their cash flow is under control to some degree, whereas that of the recycler or the supplier of the product is not. To some degree, the user is getting the benefits of that assistance package, rather than the supplier who actually pays the excise.

Senator MURRAY—I do not understand what you have just said. How can the supplier get a rebate on excise which is also your excise that you get a rebate on?

Mr Pullinger—Sorry. If we are talking about untreated waste oil or treated waste oil, when you supply it to a customer, they can claim back the excise straightaway. As a supplier, you have to wait until the customer pays you—

Senator MURRAY—But that is what I do not understand. There is a litre of oil. There is only one item of excise in there.

Mr Pullinger—Correct.

Senator MURRAY—If the customer claims that excise, you cannot also claim that excise.

Mr Pullinger—That is correct. But he has to pay you. You invoice it. If you look at the example that I have given—

Senator MURRAY—So it is not that you are claiming it; it is just that you are not getting paid by the customer?

Mr Pullinger—Sorry; correct. We are not getting paid by the customer. And if they string the payments out from 60 to 90 days, all of a sudden the impost is dramatic on a small industry, and on, generally speaking, small to medium sized enterprises.

Senator JOYCE—This is an ignorant question, but I will ask it anyway. Isn't that a question between you and your customer? Don't you basically say, 'There is a cost benefit trade-off between the costs of going to my financier and asking for an extension on terms, and the costs of going to my customer and saying, "If you do not pay me on these terms, I am going to put onto you the interest costs from my financier that I'm going to have to wear because I'm carrying you"'?

Mr Pullinger—In a perfect world, that would be fantastic. The problem is that it is not a perfect world.

CHAIR—So you are concerned about the risk of the insolvency of the customer.

Mr Pullinger—This risk of insolvency, the cash flow implications of it and the price of what it does—

CHAIR—But Senator Joyce, who is a very experienced accountant, is right, isn't he: if you leave aside the issue of insolvency, the cash flow consequences could be compensated for by charging an interest payment on outstanding balances?

Mr Pullinger—Which effectively means you are again increasing the price.

CHAIR—No, you are charging the customer who is slow in paying for the value of the use of the money. Doesn't that fix up the cash flow question?

Senator MURRAY—That theory only works if it is a seller's market, and you operate in a buyer's market.

Mr Pullinger—That is right. It is very competitive.

Mr Grundell—The industry has a choice—either to use an alternate fuel or a virgin fuel as supplied by the majors. If it gets too hard from an alternate fuel perspective, industry will take the easy position and use a virgin fuel and we will lose market share as a result.

Senator JOYCE—Because people will be thinking about this question, it is good to have it on the record.

Mr Pullinger—It would be good if we could say, 'There's an interest charge on the excise component of the invoice.' I do not know how legal it is to put interest on a—

CHAIR—It is perfectly legal.

Mr Pullinger—If it is legal, that is fine. I just do not know how it would work in the commercial reality of it all.

Senator JOYCE—Do you feel there are a range of people in your section of the market who would not have the capacity to get a credit increase to cover these contingencies?

Mr Pullinger—Absolutely. Even if you take the largest company, which is Transpacific, it is talking about \$800,000 a week. That is a hell of a lot of money to find every week in

straight cash flow. Smaller collectors—even my business and businesses like mine, such as Wren Oil in Western Australia—are just family companies. Our money is based on our houses, because we are dealing with the banks.

Senator STEPHENS—Mr Pullinger, in your submission you give the example of a recycler who processes and then stores his oversupply of used oil. You make the point that he has been informed by the ATO that he will have to pay excise on the stored product.

Mr Pullinger—Correct.

Senator STEPHENS—Is it a characteristic of your industry that people store a lot of product?

Mr Pullinger—Yes, it is a characteristic of the industry, especially in Western Australia. Western Australia has a particular problem with markets for this product. In this instance, the company involved has a tank at BP in which it stores a lot of product. As soon as it leaves the bond area, the company will be subject to excise. If you relate that to Harold's example as well, as soon as he transfers product from Queensland to New South Wales, for example, he has to pay excise on that product and then has to sell it. So the cash flow impost is dramatic.

Senator STEPHENS—Mr Grundell, does your example about transferring recycled oil between the companies also generate the excise?

Mr Grundell—Yes. It is a significant impost, given that that material is not necessarily going to be sold immediately it is transferred. It is more than likely going to be stored, and it could be stored for anything up to 12 months, depending on the market for that product at the time.

Senator STEPHENS—Neither of you gentlemen raised the issue of the greenhouse scheme and the \$3 million. Is that an issue for your industry particularly?

Mr Pullinger—I do not think it is, based on the fact that we deal in fossil fuel. We approached the Australian Greenhouse Office at one stage to put recycled oil on the Emirates and were turned down bluntly.

Mr Grundell—It was something we were trying to do to enhance the palatability of the fuels we produce and give large energy consumers some more incentive to use the material. The imposition of excise, extra fiddling around and admin associated with this change will make the products that we produce and sell in the market even less attractive than they currently are.

Senator STEPHENS—The point I was making was that, under the new legislation, businesses claiming more than \$3 million a year in fuel tax credits will be required to be members of the Greenhouse Challenge Plus program. Is that likely to have an impact on players in your industry?

Mr Pullinger—It would certainly have an impact on Transpacific Industries and it would probably have an effect on some of the larger collectors as well.

Mr Grundell—It would be fair to say that some of them would already be registered as well.

Senator STEPHENS—You made the point that this impost could preclude you from some markets. Do you want to elaborate on what markets they might be?

Mr Grundell—In terms of recovered materials, they are typically fuel oil markets. The reason we would be precluded from them is that the fuel, once you apply excise to it, is simply not viable to sell into those markets. It will be too expensive.

Senator WATSON—I would like to try and make your product more competitive or equally competitive with the ordinary product. I understand that, when product is put into stock in the wine industry, they have to pay excise. Is that correct? My understanding is that you would not necessarily be singled out, because the arrangements for the wine industry are that they have to pay excise when product is put into stock. Is that right?

CHAIR—Do you know about the wine industry, Mr Pullinger?

Mr Pullinger—I do not. I drink a lot of the stuff, but I do not know about it.

Senator WATSON—I just wanted to make the point that I do not think this is an isolated case.

CHAIR—Thank you, Senator Watson.

Mr Grundell—I suppose the point is that there is currently no imposition of that on our material at all. It is something that is new and being brought to the table as a result of the bill.

Senator ALLISON—At the risk of further complicating this proposal, I am wondering whether you are making a case for there to be a refund on the excise already paid on all oil at the point when all of it is returned for recycling. Would that overcome the problem you have described?

Mr Pullinger—Exactly.

Senator ALLISON—Otherwise, what is likely to be the implication for re-refined oil vis-a-vis what you do with oil—that is, dewatering and letting the bits and pieces fall to the bottom? If this goes ahead in the current proposal will it improve the likelihood of re-refining?

Mr Pullinger—I would say that, until it is cleared up, it would definitely detract from re-refining—mainly because it costs about \$20 million to put together a re-refinery. With this excise, you are so close to the cost of the virgin material that some of the major operators—for example, power stations—are now saying: ‘What’s the point in having recycled products? We may as well just buy diesel.’ With the excise, it is getting so close in price that they take the view: ‘Why should we deal with recycled product when we can buy virgin diesel?’

Senator ALLISON—You say that trucking companies are your main customers.

Mr Pullinger—No, I did not say that.

Senator ALLISON—I thought you did say that. Who are your main customers?

Mr Pullinger—Our main customers are fuel oil customers such as power stations, burning markets, dry cleaners, foundries and brick kilns. They are the major market for re-refined products.

Senator ALLISON—If they do not use recycled oil, what fuel will they use?

Mr Pullinger—Diesel.

Senator ALLISON—Straight diesel?

Mr Pullinger—Straight diesel, because the impost of excise is the same. In the past we did not have to pay excise on straight product. If it was a blended material, we did, but now that it is on straight product they will just go straight to diesel.

Senator ALLISON—Have you discussed with your customers what their reactions are likely to be in having to claim this back where currently they do not?

Mr Pullinger—In terms of straight lube oil, where it is sold, they will change to a straight virgin product or go to gas.

CHAIR—I do not want to overstate the point, but if you are right that means that your industry would go out of business.

Mr Pullinger—That is correct.

CHAIR—Do you agree, Mr Grundell?

Mr Grundell—I do not agree that we would go out of business, but I agree that it would make it very difficult for us to continue in its present form. The harder it becomes to use alternative fuels by way of administration and the payment and claiming of excises, the harder it will be to place the material. A percentage of the customer base will fall by the wayside as a result, because it will be too onerous and expensive for them to continue using the alternative material.

Mr Pullinger—When I answered that question I meant that the small to medium sized guys would be looking at going out of business because the markets for their products would shrink dramatically.

Mr Grundell—You need to have an appreciation that some of the markets that the smaller recyclers and collectors supply into are paying quite nominal amounts for the fuel they are using as an alternative.

CHAIR—Did you say ‘nominal’ or ‘phenomenal’?

Mr Grundell—‘Nominal’. We wish! By ‘nominal’—just quoting numbers—a customer may be paying in the order of 10c to 15c a litre for their fuel, and for them to get their head around paying 50c to 55c for the same material is a quantum leap for them and something that quite a large percentage of them probably are not going to entertain.

Senator ALLISON—I would like to pursue the switch to gas possibility. That would be cheaper, would it not, than the proposed arrangements?

Mr Pullinger—Yes.

Senator ALLISON—Because there is no excise that—

Mr Pullinger—There is no excise on gas, and gas is a cheaper product, anyway, than oil. They do not have any problems with gas, whereas they can have problems with untreated oil.

Senator ALLISON—Would the circumstances in which someone would shift to gas be where they were on the gas grid, as it were?

Mr Pullinger—On the gas lines, yes.

Senator ALLISON—Would they be likely to move to LNG, for instance?

Mr Pullinger—LNG or natural gas—either/or.

Senator ALLISON—Do you regard this as a reversal of the decision made about recycling oil at the time of the diesel changes with GST way back?

Mr Pullinger—Yes.

Senator ALLISON—So it is a very clear reversal of an undertaking made at that point?

Mr Pullinger—Correct.

Senator ALLISON—I do not want to keep leading you, but is it fair to say that investment has been made in that industry as a result of that undertaking, which is now in question?

Mr Pullinger—Exactly. A lot of companies have put money into re-refining technology on the basis that there was no excise; now, all of a sudden, excise has been applied to a product that, again, has already had excise paid once.

Senator ALLISON—So was this canvassed? Your association has an advisory committee that advises and negotiates with government—the tax office and the like?

Mr Pullinger—That is correct.

Senator ALLISON—When was this raised with that committee? What advice did you give the tax office?

Mr Pullinger—We sent a submission to the Treasurer on the occasion of the review of the Excise Tariff Act. We sent it on 2 August 2005 to Patrick Colmer, General Manager, Indirect Tax Division and pointed out all these issues, including the double taxation issues and the excise on recycled product. I have a copy here if you want me to enter it again.

CHAIR—Would you mind tabling that? We will have it photocopied. Mr Colmer is in fact appearing later this afternoon, so we can raise these matters with him.

Senator ALLISON—Would it be fair to say that that advice was ignored?

Mr Pullinger—Yes, absolutely.

CHAIR—Are you in a position to say that? You put up a series of propositions that were not accepted. Perhaps the advice was considered and rejected rather than ignored. There is a big difference.

Senator ALLISON—I will put my question another way. Was your advice rejected or ignored?

Mr Pullinger—Rejected or ignored; yes, it was.

CHAIR—In fairness to the officials, who take these things very seriously, there is a big difference between saying that something was ignored and saying that it was considered and rejected. I think it is unfair to the officials to suggest that something was ignored just because you did not get your own way.

Senator ALLISON—Did you receive a response?

Mr Pullinger—Fred Wren handled that area and I am not sure what he got back in return. I do not have a copy of that particular response to him, unfortunately. However, we have had ongoing discussions with Tax and Treasury on this issue and we do not seem to win at all.

CHAIR—A lot of people do not win—and for good reasons.

Senator WATSON—Have you or anybody else spoken to the bureaucrats or to the ministers?

Mr Pullinger—We made a representation, which unfortunately was lost, to Senator Campbell, the Minister for the Environment and Heritage. We also made submissions I think to Mal Brough, the then Assistant Treasurer. Harold, I do not know what you did, mate.

Mr Grundell—We have obviously made several representations to various ministers and have been given good hearings, but it gets back to having to handle it under the excise and taxation regimes, which is extremely difficult when they are trying to treat us in the same way they would treat an international petroleum manufacturer. It is a completely different set of circumstances. The materials we handle bear no resemblance to the materials handled by the national fuel companies that operate within Australia. It is a difficult task for the officers and ministers involved to try to dovetail or to cater for what is done by the Australian used oil collection and recycling industry. To say that we even fit into that regime is difficult, but I can understand why it would want to be covered by the ATO and excise regimes.

However, having said that, they need to do that while having some appreciation for what it is that we do. Basically, we pick up a material that otherwise would be very harmful to the environment. We put it through various recycling processes, using varying plant and equipment. Then, as best we can, we place that material into alternative fuel markets. In addition, the industry is going down the road of trying to return that material whence it came, which is back into the lubricants market. Again, getting to that area takes on a whole new set of treatment regimes, processes and, indeed, intensive capital investment. That ultimately is the sustained approach. But, today and for the next 10 to 15 years, the industry will have to exist by supplying material into the alternative fuels market, in competition with major oil companies. Anything that makes that road more difficult will detract from the attractiveness of supplying alternative fuels into those markets.

I would not be surprised if eventually a percentage of our customers were to put their hands in the air and say, 'This is too hard; we're going to sign up with one of the major oil companies.' That is the danger. The danger is that, if it gets too hard, the industry per se will take the same view and perhaps a percentage of this used oil material that is being collected currently will not be, because it is too hard to place into the market. They are the real issues that we have to get into. We cannot compete with the virgin oil suppliers because we do not have the same economies of scale. We do not run hundreds of millions of litres of throughput plants that are lightly staffed; therefore, in some instances, the cost of producing alternative fuels exceeds the cost of what is being produced by the major oil companies and that is why we have difficulty in competing. So anything that is imposed on alternative or recycled materials that makes that road harder will detract from our ability to place this material into shrinking markets.

Senator MURRAY—To summarise, you said that you expect, if this goes through unchanged, that your industry will see a loss of business and then used oil will not be recovered. That means it will be dumped, doesn't it? If it is going to be dumped, what is the cost to the community? Where is it dumped and how is it dumped? What happens to the amount of oil that you are presently recycling which will not be recycled and therefore goes where—into landfill?

Mr Grundell—There is a distinct possibility of all those things occurring. Whilst there are responsible industries—and I think the majority of industry is responsible—that will take the responsible line in terms of proper placement of their generated used oil, there are other industries out there that are not so responsible and will take the easy way out and that may lead to dumping of material or quitting it into inappropriate outlets. These are very real issues and things that need to be considered in terms of the impact that the bill may have for the recycling industry.

Senator MURRAY—What happens to oil that is not recycled?

Mr Grundell—Currently, the majority of used oil collected throughout the country is done on a free-of-charge basis.

Senator MURRAY—You are not understanding the question. If oil is not collected, if it is not recycled, what happens to that oil?

Mr Grundell—It will either be stockpiled and/or quitted as a waste material to incineration or things of that nature.

Mr Pullinger—But it will be dumped as well.

Senator MURRAY—It is incinerated, it is stored as eternal waste in drums somewhere or, if it is irresponsibly used, it ends up in our water supplies or in our land—is that correct?

Mr Pullinger—Correct.

Mr Grundell—Correct.

Senator MURRAY—That is the cost to the community of this provision going through, if it results in a loss of business to your industry.

Mr Grundell—That is correct.

CHAIR—Or at least you apprehend that that may happen.

Mr Grundell—It certainly creates a potential for that to happen.

CHAIR—I think it is better not to overstate the case, that is all. There is a risk that it may happen.

Mr Pullinger—I think the other side of that is that collectors will collect in the areas where it does not cost that much to collect, which is major capital cities. The major impact will be in remote and regional Australia.

Senator MURRAY—But you said in your submission circulated today that the collection of used oil has increased dramatically since the introduction of the PSO act in 2000. The result of the agreement between the government and the Democrats, as stated in your submission, is that the industry, 'now collects and processes over two million litres per

annum.’ You say that the changes to the Excise Act, as currently proposed, will severely affect the ability and viability of oil collectors and recyclers to survive in business and continue to collect and trade in used oil. I do not understand why we would be changing a system that works, if it is probably going to result in less used oil being recycled.

Mr Pullinger—That is correct.

Senator MURRAY—It does not make sense.

Mr Pullinger—It does not.

Senator WATSON—My question follows the same vein as Senator Murray’s. You just cannot keep collecting oil in 44 gallon- or 200-litre drums. I am not convinced about what is really going to happen to all this oil, if this industry becomes no longer viable. That is my concern. I speak as a farmer who has a problem with disposing of oil out of tractors.

Mr Pullinger—Taking that issue, I remember just before the PSO was introduced and I was at Moree where one of the farmers had 10,000 litres in 200-litre drums. He said, ‘If I can’t get rid of it, I will bury it.’

Senator JOYCE—So what is Norm Harris up to these days?

Mr Pullinger—Effectively, that is what he said, ‘I will just bury it.’ The other part of it is that the drums start to break down, as you will know.

Senator WATSON—Yes, that is right. You cannot keep storing it indefinitely.

Mr Pullinger—The drums start to rust and the oil leaks. The first casualty of that is the farmer because nobody is going to drive a truck hundreds of kilometres to pick up a 200-litre drum of oil when he can collect it in the city and cover the limited markets he has.

CHAIR—So I suppose, as well as the economic and specifically cash-flow implications of this legislation for your industry, which others—for example, the paint people—were able to point to, you point to a completely different and additional reason: the environmental externality, if I can put it that way, of the bill.

Mr Pullinger—Absolutely.

CHAIR—Senator Webber, I think it is your turn. Do you have any questions?

Senator WEBBER—No, I know Wren Oil very well, so I feel very well informed.

CHAIR—Senator Joyce, do you have any more questions?

Senator JOYCE—Just in summary, basically you are saying that the product that you purchase has already had the excise paid on it and that is the reason that you believe you did not need to pay the excise on it again. Because you are going to have to put the excise on it, the price of your product obviously has to go up. Even though the customer has the ability to claim it back, you are dealing with the cash-flow implications of the extension of credit, and it also puts you now at a comparable price to the major oil companies. So there is a likelihood of the switching across to the major oil companies and away from your product.

Mr Pullinger—That is exactly right.

Senator JOYCE—Okay. I am on board. How much capital has your industry outlaid by reason of this current legislative environment? That might also be a question to you, Harold.

Mr Grundell—It is in the order of tens of millions of dollars. We are currently in the process of constructing a facility that will further value-add to used oil to be used as lubricant. The capital used in that facility is of the order of \$15 million alone. We have several major processing facilities throughout Australia and have spent tens of millions of dollars to establish that infrastructure. We installed a re-refinery in Sydney about 10 years ago on the back of another material we produce being exposed to excise at all levels, but that rule changed shortly after we committed to that capital and we have been wearing the burden of that change up to this point. This is yet another change in the way our products will be treated from an excise perspective, and it is becoming very difficult for us as a company and as an industry to predict with any certainty what our position in business is going to be like next year, the year after that or five years down the track.

Senator JOYCE—Did you envisage in the past couple of years that this may be on the cards? In your analysis of where your business is, have you taken into account that you are working in a legislative environment that is liable to change?

Mr Grundell—There was no way that we would have foreseen excise being applied to a recovered used oil supplied as an alternative fuel. This material is black and contains significant contaminants and in no way, shape or form could ever be used to power an internal combustion engine. It is something that you would never have foreseen. For it to be caught in the same net is quite astonishing from our perspective and for, I suspect, the industry in general.

Senator JOYCE—So the fundamental premise is that you believe the excise had been paid and that was it: you were dealing with a product that had now been through the excise hoop and was not going to go through it again.

Mr Grundell—That is right. The fact that the very nature of the product which encompassed 90 per cent of what is supplied by the industry does not even permit it to be used as a fuel in an internal combustion engine. Therefore, why would you bother trying to cover it under the excise regime?

Senator JOYCE—Do any of the major oil companies recycle oil?

Mr Pullinger—No.

Mr Grundell—No. Shell and Mobil had an association with Transpacific. They were 25 per cent shareholders each in Nationwide Oil, and their involvement ceased about 18 months ago.

Senator JOYCE—Do they have any plans to go into the recycling oil business, to the best of your knowledge? Is there any information in the marketplace that they may be about to go into that line of production?

Mr Grundell—There is certainly no indication from my perspective. I do not know about you, Bob.

Mr Pullinger—I am exactly the same. In fact, I would doubt that they would go in there because of the contaminants in the product going through their hydrotreater and because it is too small—there is not enough volume there for them.

Senator JOYCE—So you are not in the marketplace and there is obviously a void in the marketplace for this product—

Mr Pullinger—Correct.

Senator JOYCE—Is your industry strongly financed? Does it have, basically, a strong debt position on long-term cash flow? You have talked about the multiple millions of dollars to set up a capital plant—is that generally financed by reason of banks or by reason of equity?

Mr Grundell—From our perspective, it is a mixture of both, given that the Transpacific group has recently floated on the ASX. But I would suggest that for the remainder of the recyclers it would be a debt position.

Senator JOYCE—Where do you source your oil? You made a statement about sourcing it from regional areas; do you get out to regional areas to pick up the product?

Mr Grundell—Absolutely.

Mr Pullinger—We have depots in Canberra, Maitland and Orange and we collect right across New South Wales. We travel to farms; we do the lot.

Senator JOYCE—Does your industry have a number showing how much oil is being recycled at the moment? Is that in your submission?

Mr Pullinger—Most of the oil collected basically goes through some kind of processing treatment; the 200 million litres would be processed in some form or another.

Senator JOYCE—In summary, basically, the legislative environment that you have set up and constructed your business in was a representation to you to basically go to the banks and source money for a long-term cash flow position. And you strongly believe that the outcome of this in its current form could have a more than detrimental effect and could take you out of business and leave you with the debt?

Mr Pullinger—Correct. Especially with a lot of the small- to medium-size collectors who do not have the infrastructure that Harold has in terms of processing or that we have in our business. There are only four of us with refineries. All the rest of the other 20 or 30 people just do settling; all they do is collect the oil, settle it and then sell it out as a fuel to burners.

Senator JOYCE—If this situation is resolved in some way that you are more comfortable with, do you think that you as an independent group have the potential to grow your business with the major oil companies in such a way as to be another strong player in the fuel market?

Mr Pullinger—Absolutely.

Mr Grundell—I think we would, but to a limited degree. The volumes that we are talking about are not huge, in terms of the major oil companies, but we certainly could have an impact and a presence in the market, for sure.

Mr Pullinger—As an example of that, both Harold's company and my company supply major power stations. One in particular has already stated: 'We are going to diesel. There is no point in using recycled oil, because it is no cost it is no longer cost competitive.'

Senator JOYCE—I think that is a major issue.

Senator MURRAY—Can you let us know, either on notice or by advising us immediately, how many collection points for used oil there are in this country? You can give me an estimate, if you like. You talk about the farmers, the people doing cooking oil and all the different sources; how many collection points or base suppliers are there?

Mr Grundell—In terms of the Transpacific group, we have in excess of 40,000 customers in our database.

Senator MURRAY—So the oil is collected from 40,000 people or sites and is then reprocessed for resale. And if your business fell by, say, one-fifth of 40,000—it would probably be a far higher figure because the first ones to be knocked out, I presume, would be all the really small drop points—all those people would be left with a disposal problem, wouldn't they? They would either have the cost of disposal, whereas before you were doing the collection, or they would dump it.

Mr Grundell—That is correct.

Senator MURRAY—So isn't sparing the environmental cost and the irritation to 40,000 people not justified? The system presently works very effectively, doesn't it?

Mr Grundell—Absolutely. The moot point there is the fact that at the moment the used oil is collected free of charge. If we as an industry are forced down the road of having to impose a charge on collection, that will also work to the detriment of used oil collection, because people will not want to pay to get rid of it.

Senator MURRAY—This is economic rationalism gone mad.

Mr Pullinger—The other issue is the government's roll-out of tanks as a result of the PSO. The government constructed a large number of tanks for used oil collection in remote areas, and they will be the first casualties. The 40,000 customers that Harold talks about—in our case it is 10,000—could multiply tenfold given that a number of these people are dropping oil into the tanks that the government has rolled out.

Senator MURRAY—When you use the word 'customers' do you mean suppliers?

Mr Pullinger—Yes. We call them customers.

Senator MURRAY—They are supplying you? They are giving you your raw material?

Mr Pullinger—That is right. Correct.

Senator ALLISON—How much of the re-refined oil is being taken by oil companies at the point of sale—service stations?

Mr Pullinger—None.

CHAIR—Mr Grundell and Mr Pullinger, thank you for your evidence today.

[12.07 pm]

HUMPHREYS, Dr Len, Chief Executive Officer, Australian Biodiesel Group Ltd

GARRAD, Mr Peter Milton, Executive Officer, Biodiesel Association of Australia

LAKE, Mr Adrian Philip, President, Biodiesel Association of Australia

MAPSTONE, Mr Christopher John, Member, Steering Committee, Biodiesel Association of Australia

IVERACH, Mr David, Chief Executive Officer, Investments, Transfield Holdings

CHAIR—Welcome. The committee has received your submission, which it has numbered 28. I now invite you to make an opening statement.

Mr Lake—The biodiesel industry in Australia has only just started. In the last 12 months, production has gone from virtually zero to 180,000 tonnes. I have a list of the projects which are currently planned. With the incentives offered by the government so far and the current tax position on excise, it will produce well over one billion litres of biodiesel per annum. Apart from the plants which are currently under construction, the proposed changes to the excise rulings and the way in which the rebate and producer grants are going to work will make 99 per cent of the biodiesel market unviable. The way the biodiesel producer grant is applied will effectively offset the excise paid or payable, or liable, for the production of the fuel—that is how it is treated by the tax office. We want the producer grant to be treated as a producer grant so that, when the excise liable on the production of biodiesel is paid, it can effectively come from the producer grant or from the producer but will be accounted for separately. That way, under the current regime and the proposed changes with legislation, it would have an effective excise of 38c.

The advantage of taking this approach is that there is already a sunset clause and a final rate of excise of 19c in 2015, so it requires no modification to any of the legislation, to any other bills—to the intent of the current legislation. But it effectively means that, while biodiesel currently has a moderate advantage, as of next month biodiesel will suffer a price disadvantage. Definitely, in the case of on-road applications, there will be a price penalty of anywhere between 2c and 4c. In the case of off-road applications, that price penalty is around 38c, the full excise price. What we understood to be the intent of the formation of the biofuels industry was to have biofuels implemented in areas where they would have the maximum benefit, and those do include a lot of off-road applications. We also do understand that the government intends to promote biofuels predominantly for the on-road applications, but, once again, these changes will adversely affect those markets and in a lot of cases result in, as I said, a cost penalty to further that application.

The types of markets for the off-road applications, where biodiesel has the greatest application, include marine applications, such as the trials currently under way for Sydney Ferries and trials operated by Brisbane City Council. Being state governments or local councils, while they will pay a slight premium for environmentally effective products or things that solve other operational issues, such as occupational health and safety, they would not incur the cost penalty for those particular operations. Likewise, in mining environments,

where the emissions profile of biodiesel makes it highly valuable, we will not have time to actually establish and prove the effectiveness of biodiesel. To give you an idea of the time that this often takes, from the initial approach to the New South Wales state government asking for a trial to the trial actually starting took three years, and we are still probably about another 18 months away from the second phase of the trial being completed. So it is a five-year cycle, and a lot of these valid applications for biodiesel are simply not going to be possible and producers will have to scrap the whole program. That is what they are looking at at the moment if this bill goes ahead.

Among the people I have with me is Len Humphreys, who represents the largest current producer of biodiesel in Australia, with an existing plant of 45 million litres and another one of 160 million litres coming online. There are plans for expansion, but I would like to explain the impact that is going to have on him as a producer. Chris Mapstone is representing Gardiner Smith. Gardiner Smith are going to be one of the leading suppliers of feed stocks into this start-up buyer diesel market. The opportunities that they have for the development of those markets and development of those feed stocks, predominantly from Australian production, are going to disappear very quickly because none of these new projects will be viable.

I have with me a list of projects that are currently under way which I will hand out and you can make copies of, so that you can see that this is a real opportunity. Unfortunately, next month, if the bill goes ahead as planned, we will go from nearly a billion litres of biodiesel per annum to a situation within the next two to three years where we will be lucky to keep the couple of hundred million litres that are coming online now.

CHAIR—Thank you, Mr Lake. At the start of your oral presentation, you said that, were the bill to go ahead in its current form, it would wipe out 99 per cent, I think you said, of the biodiesel industry. I am not making light of your concerns, but is that essentially a cash flow issue?

Mr Lake—It is not essentially a cash flow issue. A lot of infrastructure has been put or planned, and there are new projects being planned at the moment, all based on a certain return and a certain revenue opportunity for a period out to the phase-out of the excise or the producer grant. Effectively, we were given a carrot, and that carrot has been put away and the chopping block has been stuck in front of it.

CHAIR—Are you saying that this would expose you to a tax you do not currently pay? Is that your point?

Mr Lake—Yes. Well, it exposes us to the net effect of a tax we do not currently pay.

CHAIR—Leaving aside cash flow issues, why isn't that recoverable through the GST system as an input?

Mr Lake—This is factored in, and the business plans are all factored in, with GST as part of the input.

CHAIR—Yes. But if this is a new tax, and you can claim it back as an input, then leaving to one side—and, as I say, I do not mean by saying that to treat it lightly—cash flow issues, doesn't it all net out the same?

Dr Humphreys—The intent of the producer grant was to give a stimulus to the industry which was equivalent to the excise rate of 38c a litre.

CHAIR—But you still get the grant, don't you?

Dr Humphreys—We still get the grant, but then the grant is effectively extinguished by the change of law that happens between the end of June and 1 July.

CHAIR—Just explain to me again how that works.

Dr Humphreys—Take an off-road situation. We have the producer grant. Then we go to an off-road situation. So we want to sell to a farmer or a mine or anybody—for example, Sydney Ferries; so we want to sell to ferries, mines or farmers. At present, they can blend up to B49—that is, they can take up to 49 per cent of biodiesel in the diesel they use.

CHAIR—So you sell the biodiesel to your customers, and it is excisable. So you pass on the cost of the excise to your customers, do you?

Dr Humphreys—No. We actually give the customer a discount, compared to what they would pay for the fossil diesel portion.

CHAIR—But under the new system you would then have to add the cost of the excise to the cost to your customers. Is that right?

Dr Humphreys—No. Under the new system, the operative term is 'net tax paid'. And they view the biodiesel grant as an extinguishment of the excise that should have been paid on biodiesel. That is the dislocation problem. The biodiesel producer grant was supposed to allow the stimulus of the industry and to allow producers like ourselves to come into the market and form an industry from nothing. That has obviously been very effective, going by the number of biodiesel plants that are now proposed. I, as Adrian said, am the CEO of the largest biodiesel producer in Australia today. We came into the market because of our perception of the intent of the producer grant. It is the intent that is being distorted.

CHAIR—I am not so much concerned about the intent as the effect.

Dr Humphreys—It is the effect that is being destroyed. As of today, if we sell our product to a farmer we give them a discount. It is a new product; you are bringing it to a new marketplace; you are trying to get them to accept a new form of fuel—which they are starting to accept. If they then use that fuel up to B49, then they can still, today, claim the excise back on that, up to a B49 blend. So there is a stimulus for them, and there is a stimulus for the industry, in terms of the producer grant. As of 1 July, just taking that scenario as an example, they can no longer claim any excise back on the biodiesel, because it is viewed as net tax zero, because the law, as of 1 July, takes the view that biodiesel has not paid any effective tax.

CHAIR—I see: it is because of the producer grant.

Dr Humphreys—The producer grant is not being looked at as a producer grant; it is being looked at as an excise offset; hence there is no net tax being paid—

CHAIR—I understand.

Dr Humphreys—hence the farmer can no longer claim tax back. So in one fell swoop it completely closes the door to the biodiesel industry for off-road activity.

CHAIR—Have you made that point to the ATO or to the minister or the government?

Dr Humphreys—We did. They said, ‘Yes, we understand that.’

CHAIR—Obviously your submission was not successful. Were reasons given?

Mr Lake—The exact words that came from one of the parties I spoke to in Treasury were: ‘Our concerns are not the externalities of the fuels, only the simple costs of what comes in and out, and it is your responsibility to make sure that the politicians tell us to change it.’ It was that blunt.

CHAIR—We have officers of the Treasury who are listening to this evidence and will be appearing before the committee later in the day.

Dr Humphreys—I have a letter from Mal Brough when he was in his position in Treasury—last May—that articulates in black and white what Adrian and I have just said.

CHAIR—Do you have that letter from Mr Brough available?

Dr Humphreys—I do not have it with me but I can make sure that it is made available.

CHAIR—Could you perhaps arrange to have it faxed to the secretariat? Can we take it that you propose to table that letter?

Dr Humphreys—Yes.

Senator WATSON—I have no questions. I am in sympathy with the problems that the last two witnesses have articulated before the committee.

Senator STEPHENS—I am overwhelmed. Did the transitional arrangements that were announced last Thursday do anything for you?

Mr Lake—No.

Dr Humphreys—They had no impact whatsoever.

CHAIR—That is not your problem, is it?

Mr Lake—It is not our problem. The crux of it at the moment is that there is a net excise effectively to the end user. So there is something claimable. The intention—and I was involved in some of the initial discussions with writing the energy white paper—was to simplify the tax system and have what was classified as revenue neutrality by Treasury at the time and that neutrality was simply that everything balanced coming in and out. The net effect of the discussions we had then were: the producer grants had been announced and were being administered by the Greenhouse Office; the excise had been made liable and payable to the tax office; they are two separate departments therefore they should be treated as two separate things regardless of what you do to the white paper. They acknowledged that as a situation but said they were not going to consider it. It was that cut and dried for us. That was after also telling us that all other grants and other benefits and schemes would effectively be reduced to zero very quickly come 2006.

Dr Humphreys—The pithy point is that at the moment biodiesel is deemed to have paid excise and after 1 July it is deemed to have not paid excise. That is the crippling thing for the whole industry.

Mr Lake—There are implications of biodiesel hitting this target. If the projects which are currently planned take off within Australia at the moment there is about 400 to 500 million litres of what we consider readily available seed stocks—tallows, used vegetable oil and other feed stocks. That means that in the short term there will be some importing of fats and oils but there is nearly half a billion litres per annum of fats and oils that will need to be met by regional Australia. If that industry does not take off that is not ever going to become a possibility. We mentioned in the submission that I put forward to the committee that we are giving a presentation at the end of this week to another committee that is looking at the benefits of regional development with the developing of a true alternative fuel industry in Australia. It is such a problem that even the departments of agriculture from several states have lent full weight behind us because they can see the potential.

CHAIR—I do not want to oversimplify it, but as I understand it, your point is a very simple one and that is that the change in the arrangements will nullify the effect of the producer grant. That is it in a nutshell.

Mr Lake—That is it.

Senator STEPHENS—Mr Mapstone, you come from a particular part of the industry. Would you like to make some comments for the record?

Mr Mapstone—I would like to back up what both Len and Adrian had said with regard to the growth of this industry. In recent weeks I attended Parliament House and spoke with various ministers. What was immediately obvious was that there was little knowledge of where the biodiesel industry is now and where it is heading in relation to the overall biofuels industry, bearing in mind that the original 350 megalitres—

CHAIR—I am sorry, Mr Mapstone. You were saying?

Mr Mapstone—Effectively, the industry has grown very quickly in recent times. As I was about to say, a new plant is operating in Brisbane and another one is being built, and not many people know of the construction of these facilities. Gardner Smith has been in negotiation with these plants to provide the feed stock. As it stands, within 12 months, the industry effectively could be producing over 800 million litres of biodiesel, if 1 July does not occur in our industry.

Mr Lake—That does not include the beta—

Mr Mapstone—Yes, that is external. With other plants currently planned, as a feed stock supplier, we could see a requirement to supply over two billion litres of feed stock to this industry. I was sitting here this morning when the Australian Trucking Association gave evidence and I was not terribly surprised that Mr Gow was not overly aware of the amount of biodiesel that is available, because the same thing is evident with many of the people I talk to, particularly in Canberra.

This industry popping up so quickly has been driven, in part, by the love that the stock market has for energy stocks. What it takes to set up a biodiesel plant versus an ethanol plant—and how you get that product to market—are very different. With ethanol, you must align yourself with a large retail network. With biodiesel, we can make a product that is fit for purpose on spec and we can go direct to end users, whether they be road transport, off-road

users, fishing fleets or the like. That is another reason why the industry is growing so quickly. It will stop very quickly as well, if it is not understood where this legislation will put us.

Senator MURRAY—So you will not be partnering with the oil companies in the future?

Mr Mapstone—The issue with the oil companies is that, if the majors chose to adopt the role of purchasing biodiesel to put it into hydrocarbon diesel at a level of five per cent or less, they could gobble up the 800 million litres we currently have in production and it would not even make a dent. So it does not matter whether we are popular or not. If they wanted it, they could take it. The whole BP issue is totally separate, as far as the Biodiesel Association is concerned. The bulk of the customers that we target currently are customers of the majors—in particular, mining industries. If you also look at where we are with the current specification for diesel, having a low-sulphur diesel of 50 parts per million, biodiesel is being added to that in the US just as a standard B5 blend. That is to add lubricity back into the diesel to prevent wear within fuel systems. So, similarly, it could be taken up as five per cent or less and sold and no-one would even know it was in there.

Senator MURRAY—I have a parochial question. I am from Western Australia and, as I understand it, there are substantial plans for biodiesel to be produced using product from the wheat lands and the grain lands. The product they will use is presently pretty well waste, isn't it? They will not be growing wheat, barley and so on especially for your industry; it will be a by-product, won't it?

Mr Mapstone—They are two different products. The wheat and grain is being grown for use in the production of ethanol. Biodiesel uses a seed—in the case of Western Australia, it is canola—which is crushed. That creates the oil for the production of biodiesel.

Senator MURRAY—Are they converting crops from wheat to canola?

Mr Mapstone—Some of the wheat belt is being used for the planting of canola.

Mr Lake—At the moment, over 100,000 tonnes of biodiesel production is planned for Western Australia in two plants. Currently, one is under construction and another is planned for 60,000—and obviously that is dependent on what happens in the next couple of months. One of the attractions of feedstock for biodiesel is that it is very flexible, unlike current ethanol processes, which take either starch or molasses and convert that by fermentation to ethanol. Biodiesel can use canola oil, animal fats, cottonseed oil, palm oil, coconut oil—a very wide variety of fats and oils. So, as the production of biodiesel expands in this country, it creates a whole new agronomic balance and many opportunities for Australia.

Senator MURRAY—Excuse my technical and scientific ignorance but, from an economic perspective, you are forecasting that, if this regime goes through, those Western Australian proposed projects would not come off?

Mr Lake—They would become unviable; that is correct.

Senator WEBBER—It is important to note that those projects are proposed for fairly small regional communities—I am also from Western Australia, so I will just continue the parochialism—that otherwise do not have employment and economic development opportunities.

Mr Lake—With the development of its canola market, Western Australia has had the problem of not being able to get rid of the seed cost effectively. Biodiesel has given it an opportunity to do that, which it would lose if these plants were not to go ahead.

CHAIR—But that is subject to the price of oil, surely. If the price of oil continues to rise and the price of your feedstock is not a function of the price of oil, it would make you more competitive, surely.

Dr Humphreys—No, there is a whole new dimension coming into the marketplace. The new dimension is that traditionally edible oils, whatever form they take—canola oil, cottonseed oil or sunflower oil—have been dislocated from the price of a barrel of oil. Because of the rise in Europe and in the US of the biodiesel industry, for all the reasons that Adrian and Chris have put, there is now a rapid acceptance of biodiesel around the world. In addition, there is a lot of other stimulus. There now is a direct correlation starting to show between the price of a barrel of oil and the price of our start material, the edible oil. A number of reports have come out recently, particularly in Europe, showing that the demand for canola oil and palm oil in Europe for biodiesel purposes has started to link them to the price of a barrel of oil.

CHAIR—But presumably that is because what you call ‘edible oil’ would be a price leader in that particular market, so it would influence the price of hydrocarbon fuel. Isn’t that the case? In the Australian domestic market, an increase in the internationally traded price of hydrocarbon based oil will not affect the price at which your industry can put its product into the market, will it?

Dr Humphreys—That is a very good point and the answer is that it does because we are not isolated from the international traded commodities of canola, sunflower or cottonseed. Those commodities are influenced more by some of the larger producers around the world, particularly in Europe and the US. Our price here of edible oil is benchmarked against those international standards. Those international standards are now being affected by the increasing use of these oils for biodiesel and that is bringing a new paradigm into the agricultural markets around the world. That paradigm is that now some of these edible oil prices are being influenced by the fossil oil price because of the increasing use of these edible oils for manufacturing biodiesel, which is of benefit to the farming and agricultural community.

CHAIR—But, as I said before, isn’t it the case that the influence is one that edible oils are exercising on the price of fossil fuel oil, because you would be leading the price down?

Mr Lake—The short answer to that is that all fats and oils used by biodiesel and all grains and other materials used for ethanol production are internationally traded commodities. The net effect of the increase in the oil price is that suddenly there is an increased demand on these commodities. That has increased the price of those commodities. That causes the effect that Len mentioned—greater demand, bigger price.

Mr Iverach—You are looking at this from both sides: first of all, if the increased use of edible oils to make biodiesel has such an impact on the demand for diesel, and therefore on crude oil, it will have a depressing effect on crude oil prices. Unfortunately, the scale of that is such that it is having an infinitesimal effect, as we would expect; whereas on the other side, because of the price of crude oil, the highest value use for a lot of these vegetable oils is

rapidly becoming as a feedstock for biodiesel. That is why they used to track droughts et cetera and now they are increasingly tracking crude oil, because that is their highest value use.

CHAIR—I understand now. But that helps your industry, doesn't it? If the increase in the price of fossil oils generates greater demand and, hence, lifts the price of edible oil based fuels then the consequences for your industry which you apprehend from this legislation are going to be mitigated, aren't they?

Mr Iverach—No. If we have—

CHAIR—You are going to get a higher price for—

Mr Iverach—No, the farmers are getting a higher price for their feedstock. The growers of the feedstocks are doing very well, but, because of how the marketplace works, we have to pay a higher price. If we could have feedstock prices of two years ago with today's crude oil prices, I think we would probably be out there busily pumping biodiesel rather than being here. But that is not the reality.

Senator MURRAY—You are saying that the price differential between the two products is narrowing because of market forces and that if this excise change moves through then that price differential will close altogether.

Dr Humphreys—That is a correct statement.

Mr Mapstone—There are already indicators in the forward markets for veg oils that suggest that the gap between hydrocarbon and veg oil will actually narrow over the next two years.

CHAIR—Have you done any economic modelling that produces that conclusion, or is that just your judgment as to the way you think—

Mr Mapstone—A paper has been put out by Gardner Smith.

CHAIR—Can that be supplied to the committee, please?

Mr Mapstone—Yes.

CHAIR—Thank you.

Mr Iverach—One of the ways of looking at it is that we are so used to hearing crude oil in \$US per barrel and vegetable oils in \$A per tonne that we do not easily connect them. But the fact is that the current price of crude oil is about \$A750 per tonne and the current price of a lot of these vegetable feedstocks is in the range of \$A600 to \$A900 per tonne. It used to be that vegetable oils were \$600 per tonne and crude oil was \$300 per tonne, so the prices are just being driven by market forces at work.

CHAIR—But, in any event, to come back to where this part of the conversation began with my intervention, you say that an increase in the price of crude oil is not going to fix up your problem in relation to the effect that this bill will have on your industry?

Mr Lake—In the longer term it will, but then you are talking about economies of scale being developed by the biodiesel industry.

CHAIR—When you say 'in the longer term it will', how do you define the longer term?

Mr Lake—At the moment the industry has built itself on the basis that by 2015 it will be paying a 19c excise and that within that window it will have to establish the infrastructure for distribution, feedstock development and the basic production of biodiesel—

CHAIR—The extinction of that period was the result of a recommendation to government of this committee.

Mr Lake—Yes. And the problem we have is that that recommendation was accepted and has surreptitiously been taken away—or the net effect of that decision has been taken away—by this change.

CHAIR—For the reasons you have already explained.

Mr Lake—Correct.

Senator JOYCE—In summary, there is an investment grant of 38c a litre currently in place. At the moment, the farmer, for want of a better word, can still claim the excise rebate, but after 1 July the farmer will not be able to. Is that correct?

Dr Humphreys—Correct.

Senator JOYCE—Ultimately, that makes your product—you are producing B50 or something like that—dearer than buying B5 from the major oil companies.

Mr Lake—There is a table, which we will submit to the committee, which highlights the effect of the change.

CHAIR—Is that in your submission?

Mr Lake—No, it was not part of the submission.

CHAIR—Can we have that, please?

Mr Lake—Absolutely.

Senator JOYCE—So your product, after 1 July, will be dearer than that produced by the major oil companies. Of course, that means it is ‘goodnight’ for you. Were people in the industry aware of the contents of the fuel tax bill? Do you think there was awareness?

Mr Lake—Generally not. Just last week, in a steering committee meeting, Len and I explained to producers and other industry people what the impacts were, and they asked, ‘How did this happen?’ Part of the problem is that the debate and the discussion have been clouded by a very complex system of grants and credit schemes and, as recently as last week, the tax office still had the wrong script on their telephone information service, so people asking about applications for grants for biodiesel were given the wrong information. Even the tax office has had trouble trying to understand this, and that meant that, when the bill was put forward a considerable time ago, people could not understand the calculation of what grant went where or how it was all applied. They are still trying to work it out themselves.

Senator JOYCE—I am posing a hypothetical question for you to answer, rather than it being the sentiment of what I believe. Some people would say: ‘You’re getting a 38c investment grant and you want the excise as well. You want both.’ How is that fair? Why should you get both?

Mr Lake—We are effectively not asking for both; we are asking for the situation we have now, which is that the producer grant coming to us effectively offsets the liability. One way or another, we are still paying the excise. It just so happens that the excise is coming from the producer grant. It could be paid by my grandmother; it really does not matter. It is being paid from a fund. The reality now is that it is being wiped out.

Senator JOYCE—The purpose of the investment grant, obviously, is to get the industry up and running, and I think that is a very viable reason for you to have an investment grant. Industry is, at the moment, being successful. There is a multiple number—and there must be a lot in Western Australia, because they are the same people who lobby me—coming in to set up the biodiesel industry with smaller regional cooperatives. Is that a fair outcome? Would that be a fair statement of how it is developing?

Dr Humphreys—The group of which I am CEO, the Australian Biodiesel Group, was listed on the Australian Stock Exchange last December. We are the only listed company that owns their intellectual property. We developed our intellectual property to produce biodiesel plants. Not a week goes by when we do not get inquiries from farming communities in the west and rural Australia to go and build them a biodiesel plant. We are now starting to explain to them what the impact of this legislation is, and they are not very happy.

CHAIR—It sounds to me as if the government's earlier decisions in relation to the producer grant and the tax treatment of this industry have been very successful for you.

Dr Humphreys—They have been, yes.

Senator JOYCE—The government has made a decision to give BP a fuel excise exemption for producing biodiesel from tallow which will have a significant impact on the biodiesel sector. Was your industry consulted about this decision and do you think it works in favour of BP? Are you aware of the issue I am talking about?

Dr Humphreys—I am aware of the issue. We are about to open a 160 million litre a year plant in Queensland, at a place called Narangba, which is a couple of miles away from the BP Bulwer refinery. We built that whole plant concept around a steady state condition on a producer grant and on the availability of tallow as feed stock. Even though that was a well-known position, we were not consulted by anybody about the decision on the BP situation and the rationale behind it. Our view—anybody's view—is that the government is now going out to change the legislation because that is not biodiesel; it is purely a diesel that has been formed from tallow. The effect on us is that it will drive up the price of our feed stock because there is not that much tallow available in Queensland. Secondly, BP have been given \$40 million a year to do it. They are being given an excise grant of \$40 million a year to produce this diesel from tallow.

Senator ALLISON—Dr Humphreys, could you explain the difference between tallow which is hydrogenated and then put into the refining process and biodiesel from tallow? Could you spell that out?

Dr Humphreys—Yes. The third-grade tallow is called 'fancy tallow'—that is the industry name for it—which contains less than one per cent free fatty acids. It is the level of free fatty acids in tallow that defines the quality of the tallow. So traditional grade fancy tallow has about one per cent or less free fatty acids, and there are some other specs on moisture. The

biodiesel industry uses fancy tallow—less than one per cent free fatty acids—but also tallow that contains up to three to five per cent free fatty acids which would not normally be used in the food chain. So the biodiesel industry uses a very similar type of tallow to that used in the food chain, but it can also use specifications of tallow that would not normally be consumed in the food chain.

Senator ALLISON—But how is the end product different?

Mr Lake—What is proposed by BP is effectively a modified fat, which is what biodiesel is. The difference is that biodiesel is clearly defined under the biodiesel standard as transesterified fat or oil, which means you are taking away the glycerine and replacing it with an alcohol. BP have effectively developed a brand new type of fuel which has not gone through the same rigours, tests or life cycle studies that biodiesel had to go through to get any support at all from the government. But, through the stroke of a pen, BP have been given the same benefits and rights that we have literally spent the last eight years getting from the government and that, hopefully, with a better outcome on this excise change, we will maintain. The BP process does not use alcohol. By using hydrolysis and hydrogenation, which is very similar to the process of making margarine, it converts those fatty acid chains into a form that they can blend at five per cent. By doing a five per cent blend with their diesel, they are going under the radar as far as any sort of standard for emissions or life cycle is concerned. They have said, ‘We acknowledge it is a biofuel and potentially an acceptable biofuel.’ But we have no open information and there have been no studies. And there was no discussion or debate with the biodiesel industry about their rationale and what they are trying to do with the fuel until after the BP announcement was made.

Senator ALLISON—So greenhouse, tailpipe—what are the differences in the cost of production?

Mr Lake—No-one knows. No-one can tell you that.

Mr Mapstone—The B100 manufactured as part of the biodiesel process has, as you are probably aware, a standard that requires 22 boxes to be ticked for it to be classified as a biodiesel. If it were possible to take the five per cent biodiesel manufactured by BP out and stand it alone, it would not meet that standard.

Senator ALLISON—Yet this whole scheme is geared to B5, to the detriment of other levels of—

Mr Lake—It is geared to five per cent inclusion of their fuel.

Mr Mapstone—Because you do not have to specify that you actually have a biodiesel fuel.

Mr Iverach—Sorry; what whole scheme?

Senator ALLISON—As I understand it, biodiesel is defined, for the purposes of on-road use, as being B5 and that other blends are disadvantaged in relation to that.

Mr Lake—That is correct.

Mr Iverach—Are we sure that is correct?

Mr Lake—Yes, that is correct.

CHAIR—Do you have some concerns about the accuracy of that statement, Mr Iverach?

Mr Iverach—Yes, I do. My reading of the legislation is that there is a standard for diesel. A blend of whatever molecules from wherever which meet that standard of diesel will be sold as diesel. It is a fact that five per cent biodiesel blended with petroleum diesel would meet that standard for diesel, but it is also true that other blends of biodiesel would meet that standard. The way I understand it—and it would be interesting to get clarification from Treasury or others—is that B5 is a shorthand way of saying that whatever mix is sold with the name ‘diesel’ on it meets the highly prescribed standard for how diesel performs in a vehicle.

Senator ALLISON—Submissions to the inquiry suggest there is—

CHAIR—I am sorry, Senator Allison; I think that, given there is uncertainty among the witnesses as to this issue, which can be readily clarified, I imagine, by Treasury, rather than having this part of the discussion proceed on what might be a false premise, it might be more sensible to wait and simply ask the Treasury officers what the position is.

Mr Lake—I agree with that. I just want to clarify the association’s understanding of the position. I think the point Senator Allison was trying to make is that under the energy white paper and the legislation which is due to go through, five per cent biodiesel is given equivalent treatment to regular diesel. Effectively, they said, ‘We’ll gift you at five per cent that excise component.’ The point Mr Iverach was making about the relationship to the BP announcement and the fact that there is confusion—and this is a fear of the Biodiesel Association—is that by effectively allowing an unregulated fuel that literally has not gone through the scrutiny that biodiesel has had to go through to be adopted, even at five per cent or at all as a fuel, this new fuel is being given all the benefits of the other biofuels from an excise and—

CHAIR—This is the BP fuel?

Mr Lake—This is the BP fuel—correct. It opens up a Pandora’s box for people to say, ‘I can do any inclusion of a modified fat or oil and that could still pass as a diesel spec; therefore, I want to get my full grant because it is from a biosource.’ That causes a lot of problems, because one of the big issues biofuels has is in making sure that we meet the standards, making sure those standards are understood, making sure systems are in place for testing and also making sure that we are doing what we are saying we are doing—in other words, the life cycle studies have been done and we are providing the benefit for which reason the grants were given to us in the first place.

CHAIR—This is rather a different point, though—

Mr Lake—Yes, I appreciate that.

CHAIR—from what I understand to be your main point—that the effect of the bill will be to rob you of the benefit of the scheme.

Mr Lake—It is. It is a side topic.

Dr Humphreys—It is the subtlety of a chemical point as opposed to a legislative—

CHAIR—Yes.

Senator JOYCE—Is it a fact that other biodiesel nations, ethanol producing nations, see it as a matter of national importance that this industry be developed? Would that be a fair statement?

Mr Lake—Absolutely.

Dr Humphreys—That is a fair statement, yes.

Senator JOYCE—This might be related. Are you aware of the fact that in 2012, for instance, the excise on ethanol will be reduced to that of imported ethanol, possibly from Brazil?

Dr Humphreys—Yes.

Senator JOYCE—What effect will Australia unilaterally reducing its excise level have on such things as the ethanol industry or the biodiesel industry?

Dr Humphreys—I am not an ethanol producer, but obviously being part of other associations we hear a lot about the effect being articulated, and the effect for ethanol in this country will be damaging because it exposes the people who invested a lot of money in plants here to some economics that just do not happen in Australia. There will be an unfair competitive advantage for imports against Australian produced ethanol.

Senator JOYCE—These are similar effects, obviously. It is on the record that you did not really envisage that this legislative outcome would be as it is and you have set up your business plan surrounded by a sense of security that the legislative outcome is as it is now, but it is going to change on 1 July. How many producers do you think would be affected by this and what sort of investment of money do you think will be compromised by this decision?

Dr Humphreys—If you look at the biodiesel side alone, as Adrian said, if left to the current state it would be at a capacity in 2½ years of between 800 million litres and one billion litres of biodiesel. That would establish a home market here for fuel and would attract an investment of the nature of equivalent to \$400 million or \$500 million from investment communities attracted by the current state. So if it continues on 1 July we would have this situation coming about where we would probably end up with an industry not of 800 million litres but probably of 250,000 litres, which is already out there now. It would probably expel an investment of \$500 million in the industry.

Senator MURRAY—This would involve taking imported product instead.

Dr Humphreys—Yes.

Senator JOYCE—Is there something happening in Western Australia so that this investment is concentrating around there or is it all around the countryside?

Mr Iverach—No, it is not concentrating in Western Australia.

Mr Lake—Out of one billion litres, that was only 100 million litres, so 10 per cent of the projects that are currently under way are in Western Australia.

CHAIR—I think, Senator Joyce, the reason we had Western Australia on the table was the parochial interests of Senator Webber and Senator Murray.

Senator JOYCE—They have been working the corridors down around my corner of the building as well.

Senator MURRAY—You're precious!

Senator JOYCE—They are more effective than the rest of us.

Mr Lake—If you are talking about investment impacts, you may be talking about \$500 million worth of investment impact within the biodiesel production aspect, but you are talking about a multibillion dollar agronomic industry potential for Australia which would disappear overnight.

Senator JOYCE—I am very aware of that, especially now that we know that the Americans are going to come back into the market selling beef to Korea and places like that, so the boom in the feedlotting industry might wane a little bit. Obviously that is going to give an excess of feeds that are going to be looking for a home, which is why I posed the question. That being the case, do you think that over time you will be a viable competitive mechanism for the major oil companies, and how much time do you think would be required before the industry had settled down so that you were?

Dr Humphreys—I would put to you that the scenario existing today would achieve that. As it stands with the concept of producer grants and the regime that is in place today, if left to follow its course, which will start to fade out in 2011 or 2015 to reach 50 per cent with an excise, you have done it. You have it. As Senator Brandis said, it sounds like the government has done it today because of all the interest that now exists in all the biodiesel plants. So you have done it, but on 1 July you will be undoing it.

CHAIR—I think you have made that point very, very clear, Dr Humphreys.

Senator ALLISON—I have one more question. Your industry represents mostly the provision of biodiesel for off-road users.

Mr Lake—For all industry.

Dr Humphreys—We supply both off-road and on-road.

Senator ALLISON—I am clarifying this question of the five per cent.

Mr Lake—The table that has been circulated shows that, for on-road and off-road applications, it goes from a potential cost benefit to users at the moment to a cost penalty for the adoption of biodiesel.

CHAIR—And that is tabulated? It is quantified in your table?

Mr Lake—Yes.

Mr Iverach—Clarifying that question that you were referring to could be really important for discussions later on this afternoon. I think it is extremely important.

CHAIR—We will ask the Treasury representatives about it.

Mr Iverach—Due to the complexity of the bill, the cognate bills and the explanatory memorandum, we have to confess that not all of us have understood the same things from what we have read, so clarification is important.

CHAIR—We will ask.

Senator MURRAY—That is a side issue. The real issue is that, if the current bleeding out of the system which would bring you back to real equality between the two systems later on, in 2015, is maintained, you would be fine. But, if it is not maintained, we are going to be importing product instead of producing our own strategic product in Australia—and we have got a current account deficit. It does not make much sense to me.

Senator ALLISON—Just to be clear: you understand this to be a reversal of several decisions that have been made over recent years on the question of encouraging biofuels into the sector. Did the Prime Minister's target, the energy white paper or the biofuels task force prepare you for this?

Mr Lake—Everything that has been built up and all the benefits that biodiesel enjoys today to establish itself in the market are effectively totally destroyed by this change.

CHAIR—That is what you say would be the effect of this change.

Mr Iverach—But to answer the senator's question: I have gone back and reread the white paper—and other things—and now it is quite clear to me what it was foreshadowing. A lot of different messages have been given about biofuels. Amongst those messages from 2004 and 2005, and with the benefit of the current bill and explanatory memoranda on the table, is a clear message foreshadowing the removal of excise from all fuels used for business purposes on- and off-road. The consequence of that, as you think it through, is that biodiesel will lose its competitive advantage and therefore its opportunity to make sales.

CHAIR—I think, Mr Iverach, as Mr Lake said at the start, assuming your analysis of the effect on your industry is correct, the consequence of applying the bill to you would be to deprive you of the benefit of an existing government decision to encourage the industry via the producer grant. That is what it amounts to, as you say.

Mr Lake—Yes.

Senator MURRAY—But the point you make is that the time frame has shifted. It was always the intention to do it just as you outlined, but the time frame has been changed and that is what produces the problem you have.

Mr Iverach—There are mentions of 1 July 2006 in the white paper.

CHAIR—We do not have the white paper before us so, rather than speculating about people's intentions and motives, you should be telling us about the likely effect. We are not interested in motives or intentions; we are interested in the effect. You could not have been clearer about what you say is the effect on your industry, if you are right.

Mr Mapstone—The effect is not only on our industry.

CHAIR—No, of course not.

Mr Mapstone—Currently, Australia imports more than 20 per cent of its requirement for diesel, and that will continue to grow. If we have the opportunity to produce a percentage of that from biodiesel from local production, that will go some way towards assisting against imports.

CHAIR—Thank you very much, gentlemen. That has been very helpful.

Proceedings suspended from 1.04 pm to 2.06 pm

GORDON, Mr Bob, Executive Director, Renewable Fuels Australia

HILL, Mr Andrew David, Director, Biodiesel, Renewable Fuels Australia

CHAIR—Welcome. The committee has your submission; we have numbered it 25. Mr Gordon, would you like to make an opening statement?

Mr Gordon—We appreciate having the opportunity to appear before the committee today at a time when the world is forced to come to grips with the issue of future liquid transport-fuel security. Geoscience Australia, the government authority on this issue, has identified that Australia's domestic oil reserves will be exhausted in the next nine years. While Australia may be a net energy exporter, in relation to crude oil we are not. Australia is becoming a dominant importer of crude oil and petroleum products. Today, according to ABARE, crude oil and petroleum products make up 63 per cent of the national balance of payments deficit. This adds up to \$10.575 billion as of May 2006 and represents a deficit bill for Australia of \$28.9 million per day for these petroleum fuel imports.

This comes at a time when the transition from traditional petrol and diesel fuels to the fuel technologies of the future has, in our belief, started and this represents both a challenge and a potential crisis for Australia and the rest of the world. Elsewhere around the world, governments are grappling with development policies to make this transition as smooth as possible without major economic, social and political disruption. Renewable fuels, along with other alternative fuels such as CNG and LPG, are seen as playing a vital role in this transition process.

As a consequence of the outcome of the Prime Minister's Biofuels Taskforce in 2005, we have seen a modest surge in confidence, financial investment and growth in our industry. This surge in confidence alone will see the extremely modest 2001 biofuels target of 350 megalitres of biofuels used by 2010 exceeded by industry growth within two to three years if constructive and positive government policies are maintained. Three of the big four oil companies—that is, Caltex, BP and Shell—have also demonstrated that there are clear flaws in the government's existing target of 350 million litres by declaring that they alone can take up and use between 403 and 532 million litres by 2010. Unfortunately, the Fuel Tax Bill 2006 in its current form will bring uncertainty once again to our industry and could bring our industry to a shuddering halt.

In the past, the parliament, particularly the Senate, has played an important role in ensuring that government policy on biofuels continues to meet the national interest. The energy white paper of 2004 clearly identified and recognised the need for effective transitional arrangements to give fuels that are currently untaxed an opportunity to establish their place in the market. This goal has yet to be achieved in Australia. The Biofuels Taskforce also foreshadowed that the single-minded focus of revenue collection could, in the way Treasury translated and constructed the so-called tax reforms, impact heavily on the commercial viability of new ethanol and biodiesel projects, including those associated with current producers.

Unfortunately, by ignoring fundamental barriers of the oil majors to the entry of biofuels in the mainstream transport fuel market, the current Treasury bill denies the biofuels industry

critical time needed to establish itself in this market. Treasury, in our belief, has ignored this, claiming that the industry has already secured three more years in the transition process in 2003 and 2004. Our response to that is: thank God we did! This policy was first introduced in 2001, and we looked like we were losing three years of opportunity to establish new industry growth at the time, and we managed to get at least three years to accommodate for the loss of that vital period for growth. Since 2003, we have seen the loss of at least another four years associated with the barriers set up by the major oil companies to the entry of our fuels into the mainstream petrol and diesel fuel market. For this reason, we are seeking what we believe are and should be a number of practical adjustments to the current bill which do not directly affect the policy structures of those provisions.

We are talking about essentially three issues. One is the phase-in timetables for biofuels entering the new excise import regimes proposed under the bill. The second relates to policy consistencies in implementation of the new biofuels import regime. The third addresses, as we have heard this morning in some confusing ways, market barriers to the access of the off-road and on-road diesel market for biodiesel via tax credits and other mechanisms. Failure to address these issues—and this is the message that hopefully came out of this morning's session—will, in the bill's current form, impact negatively on new project financing and the commercial viability of both current and new projects.

We believe that the consequential changes to the bill are sensible, do not pose serious policy dislocation for the government and should be readily achievable. We have been trying to engage the government on these issues for at least the past six months. It would be correct to say that, over the past couple of years, there have been a range of opportunities to have consultations with Treasury, and we were also given the opportunity to look at the draft bill under in-confidence arrangements. What has been consistent is Treasury's position of saying there will be no change. We will continue to try and work with the government, and that would be our preferred approach, but we will use whatever measures we can to try to get these measures and opportunities for change across to the parliament, particularly the Senate, because the Senate, as I said, has played a major role in our future in the past and we would expect it to continue to do so in the future.

CHAIR—Thank you very much, Mr Gordon. To cut to the chase, do you go so far as to say—as I understood the witnesses immediately before lunch pretty clearly to say—that, were this bill to be introduced from 1 July in its current form, all the benefit of the producer grant scheme legislated for a couple of years ago would be lost?

Mr Gordon—Yes, there is substance to that. And I would add to that—

CHAIR—I am sorry to interrupt you. When you say 'there is substance to that', I appreciate the careful way in which you express yourself but—

Mr Gordon—I would agree with that.

CHAIR—The witnesses before lunch would have had us believe that it is just black-and-white; almost a mathematical certainty. Do you say that?

Mr Gordon—With due respect, this is a very complex bill. It is vague in some areas, and it is difficult to put your hand on the data that is relevant to certain pieces of it. I am not surprised that this morning there was evidence of differences and confusion over the

interpretation of this bill. I do believe that, in those circumstances, it is quite credible to say that this bill could kill our industry and stop us in our tracks.

We are on a platform of modest growth, and we believe it can be maintained. But we need policy certainty. This was what the government promised the industry, and essentially we are saying to the government: ‘Give us that certainty. Give us the time that you said we needed, and recognised that we needed, to establish ourselves in the market. We will get on with the job.’

CHAIR—Thank you, Mr Gordon.

Senator WEBBER—Earlier today, we received a fair bit of evidence about how confusing and internally inconsistent some of the policy approaches are to this issue. I was interested, Mr Gordon, that, when you talked about your three point plan, of phase-in and what have you, you mentioned the need for policy consistency. Can you elaborate on how you think we can overcome some of those inconsistencies, some of which I must admit I was not completely aware of until this morning?

Mr Gordon—In relation to giving new industry growth that certainty and confidence, we are saying that, since 1992—and our focus at that time was mainly on ethanol production alone—our industry has been unable to enter the mainstream petrol market. The same situation exists today, in that we still have not managed to gain entry completely into the diesel fuel or petrol fuel markets.

We do recognise that, in December 2005, the Prime Minister and Deputy Prime Minister announced that the oil companies had undertaken to take up voluntarily up to 532 million litres of biofuels—ethanol and biodiesel—by 2010. Now, for the first time in all this period—given good faith in meeting those commitments—we can count on going forward with the confidence we have not had in the past.

We are saying to the government that we have lost at least another four years for new industry growth—and in this regard I am not talking about assistance to current producers, such as the Manildra Group and CSR. This industry is not going to exist unless we have new industry growth. And this is the importance of giving us the time to establish ourselves that the government itself, in the white paper, identified as being essential. This is a threat widely seen in this current bill.

Before I address a second issue, let me go back a moment. What we are saying to the government is: ‘Give us five years; just stretch it out. Keep the existing policy structure. Give us five years, and we will do the job.’ Of what you have heard this morning, we may not agree with the total aggregate of production increase; we think it is more modest than that. But we think a significant increase in the infrastructure for a new industry in Australia can be established in that period of time.

The second issue relates to the import regime that is being proposed. In 2003, the Prime Minister made an announcement recognising the benefits of alternative fuels. With biofuels, we are talking about future energy security; reducing the balance of payments deficit; reducing, in a positive and significant way, greenhouse gas emissions; and stimulating economic and jobs growth in regional and rural communities in Australia. Imported fuels cannot deliver those benefits. In recognition of those benefits, a commitment was made that

our industry would get—and this also would include LPG and CNG—a 50 per cent discount on our final excise rate. Ethanol's final excise rate, for example, is deemed to be 25c per litre, so our final excise rate with that discount for domestic benefits is deemed to be 12.5c per litre.

Unfortunately, when we looked at the details of the fuel tax bill, it became clear that one of the first casualties would be that 50 per cent discount benefit. We have not been able to get a rational explanation of why we should deliver to imports the benefits of that 50 per cent discount, to which they make no contribution. The best response we have been able to get is, 'Well, we may get a challenge in the world trade court.' Forgive me, I cannot remember what it is called, but you will understand what I am referring to.

However, the reality is that this industry has some unique features. One is that we are talking about producers around the world that are all carefully protecting the domestic development of their industries. To do this, they all have high-tariff barriers of one form or another. This industry has not reached the production level or the position where it is reaching a commodity market. At the moment, the whole emphasis of the world is on increasing production. Brazil is looking at exporting, but the United States and many other countries are not; they are solely focused on providing domestic production security. That is what we are about. We have not even got off the launch pad in Australia, but we desperately need this time to be able to do that—and that is what we felt government policy would provide.

CHAIR—That has been provided by government policy, but your point is that—

Mr Gordon—We believe that this bill is inconsistent with that position. We are not criticising the government; we are saying there is an issue here that we need to address.

CHAIR—Yes, that has been made very clear.

Senator WEBBER—And the announcement by the government last week does not address your concerns; it picks up other concerns. But the two-year transition does not really solve the concerns that you have.

Mr Gordon—The announcement made last week related to the transition for the use of BAS statements. We are saying that we should stretch out the excise regime, the transition process, and deal with the import issue.

The third issue, which had quite a run this morning, is the impact of biodiesel's entry into the Australian diesel fuel market. I do not want to go into any greater detail about that. Treasury will be here later today and I am sure you will be focusing on getting some clarity on some of those issues. But, in our view, there seems to be quite a practical solution. Up to today, for example, we have entry into 100 per cent of the petroleum diesel fuel market. In terms of biodiesel, they produce and sell a five per cent blend. Andrew Hill, a biodiesel director who is with me today, has a contract for a five per cent blend with Caltex, but he also regards it as important that he sells higher biodiesel blends as well. We also can sell a 49.9 per cent blend, which is called B50, or 3100, which is of a biodiesel fuel quality standard.

We are concerned that this regime may significantly reduce our capacity to add to that market and compete equally in that market. We believe this issue can be addressed rather effectively by treating all fuels in the same way—that is, if biodiesel meets the fuel quality standard and the fuel meets the petroleum diesel standard, they both should be treated equally

in terms of grants or credits or otherwise. That reflects the market as it exists today. We would be very concerned if we were looking at a major shift in the market as a result of this bill that could significantly restrict our access to it.

Senator ALLISON—Could you draw the committee's attention to the part of the bill that affects imports that effectively takes away the current tariff?

Mr Gordon—We provided the committee with a copy of our brief and at the end of that, on page 17, I can provide an example. In 2011, we start our entry into a fuel excise regime and we start at 2.5c per litre and we increase by the same amount—2.5c per litre—

Senator JOYCE—Where is this in the bill?

Mr Gordon—I cannot tell you that precisely.

Senator JOYCE—That is all right.

Mr Gordon—By 2015, we reach our final excise rate of 12.5c per litre. Unfortunately, under the bill, the interpretation we have been given is that in 2011 imports will drop from 38c per litre to zero and then join ethanol—the example we use—at 2.5c per litre, and they will walk up with us until the final excise rate of 12.5c per litre is reached in 2015. This means the complete excising of that 50 per cent benefit which the government proposed to give us the opportunity to use for future development.

Senator ALLISON—So the excise drops to zero in 2010—does it?

Mr Gordon—At the first point, yes, and then it comes up and walks up with us. Beginning at 2011, we are at zero, then we commence our rise into our new excise rate.

Senator JOYCE—It is at zero now and then it walks up to 12½ per cent. What is going to happen in 2012? Imported ethanol will meet us on the road up, so we will have imported ethanol at the same price as domestic ethanol. Therefore, domestic ethanol will collapse.

Mr Gordon—Imported ethanol, for example, will have the benefit of 12.6c discount anyway, because that comes down from 38c per litre to 25c per litre. We believe that the way it was going to work was that they were going to gradually descend on an annual basis to 25c a litre and that would be their level. At the same time, we were rising to 12.5c a litre and there would be a 12.5c per litre buffer, representing those domestic benefits.

Senator ALLISON—Have you had a chance to confirm your interpretation of the bill with the department?

Mr Gordon—We sat down with the Minister for Industry, Tourism and Resources last Wednesday night. He was surprised that this interpretation was made and uncertain that it was correct, but his departmental officers confirmed that this interpretation is the correct one.

Senator ALLISON—After your meeting?

Mr Gordon—Yes.

Senator ALLISON—It is interesting that the group before us, biofuel producers, do not seem to have understood that that was the case. Would you say that is because the bill is unclear, to say the least, and because there has not been any consultation or explanation?

Mr Gordon—I can understand that, if the minister was unable to discern what the actual policy was, it certainly reinforces the fact that this is quite a complex bill and it is often difficult to read.

Mr Hill—With respect, I do not think the Biodiesel Association addressed the issue of imported biodiesel or imported ethanol.

Senator ALLISON—I am sorry—I did not quite catch that.

Mr Hill—The Biodiesel Association did not discuss imported biodiesel or imported ethanol.

Senator ALLISON—No, precisely. It was not in their submission. That is why I am saying it is interesting that a group which is—

Mr Hill—Sure.

Mr Gordon—Two of those sitting at the table, of course, are members of our association as well and are in support of the position of RFA on this matter. We cannot speak for others.

Senator ALLISON—Can you confirm for us the table which you have provided: attachment 1, ‘Impact of Treasury fuel tax credit reform proposal’? This is leaving aside all of the import questions. This is just the attachment; it is not a numbered page. You say that, once this reform is in place, the net cost to the heavy onroad vehicle operator is 81.9c per litre of diesel and, for biodiesel users, a higher figure of 25.2c per litre.

Mr Gordon—I do not have that in front of me.

Senator ALLISON—It is entitled ‘Attachment 1: Impact of Treasury fuel tax credit reform proposal’.

Mr Gordon—This was put together by ANZ Investment Bank. I will give that to Andrew, because he is the expert on these issues.

Senator ALLISON—I just wonder if you can run us through the make-up of those differentials and why it is that biodiesel will in effect be more expensive than petrodiesel.

Mr Hill—This has got to do with the phase-out of the Energy Grants Credits Scheme, which is proposed to start on 1 July. ANZ in this instance are supposing that the terminal gate price of diesel and biodiesel are each \$1. As of 1 July, the eligible user of a vehicle over 4.5 tonnes conducting business will be able to claim 18.1c per litre for regular diesel and, in the year 2006-07, will only be able to claim 14c for biodiesel and, in the subsequent year, 11c. Therefore, in simple terms, the cost for the end user will be 81c for diesel and 85c for biodiesel in the year 2006-07.

Senator ALLISON—That says it all, doesn’t it? It says that no-one will be interested in buying biodiesel.

Mr Hill—Yes. It will put more downward pressure on a product to reduce our margins or get out of the business.

Senator ALLISON—To be clear, that is what will happen by 2007?

Mr Hill—Yes, that is what will happen under the proposal for the financial year 2006-07.

Senator ALLISON—Does it matter whether it is biodiesel—B5, B20, or some other figure?

Mr Hill—It would take some time to go through the tables of how it is made up, but B5 is regarded as diesel under the fuel quality standard and, therefore, would be regarded as diesel.

Senator ALLISON—So B5 sits under that first category of diesel user—the cheaper—at 81.9c?

Mr Hill—Yes.

Senator ALLISON—Anything higher than B5—B10, B20, B50, B100—would fit under the biodiesel user example—

Mr Hill—Yes.

Senator ALLISON—and therefore attract 85.2c per litre?

Mr Hill—In simple terms, yes.

Senator ALLISON—We need this in simple terms.

Senator WEBBER—I do, anyway.

Senator ALLISON—That is amazing, Mr Hill and Mr Gordon. Can I, again, ask you whether you have shown those figures to the department? If so, do they agree that this is a likely outcome?

Mr Gordon—We have shared this information, as well as a brief, with a range of departments and advisers to the government.

Mr Hill—I would add that it is their table in the explanatory measures which outlines that fact. They actually wrote the document.

CHAIR—Have you shown it to Treasury?

Mr Hill—Yes, we have put that position to them previously.

CHAIR—Have you met with them?

Mr Gordon—We have met with them on a number of occasions.

CHAIR—What was Treasury's response to those figures?

Mr Hill—That our understanding is correct.

CHAIR—They said that to you, did they?

Mr Hill—Yes.

Senator ALLISON—If we go to 2011, when the excise begins to cut in, we have a differential of 18.1c per litre. I am looking at the figures in the box directly underneath that calculation we have just been talking about. What is the situation in terms of that differential? It will be 0.033c in 2007 and then it rises to 0.181c per litre by 2011. What is the figure for, say, 2015, when the full 12.5 per cent excise rate applies?

Mr Hill—I cannot answer that without a calculator and some time, but we are happy to provide that.

Senator ALLISON—It continues to go up; would that be fair to say?

Mr Hill—Obviously, it will go up. The point we are trying to get across is that we need more time to get the industry established before we can make a full and total contribution.

Senator ALLISON—I put it to you that the industry could never be established or grow under those circumstances when it is competing against diesel at a much lower price—a much lower end cost.

Mr Hill—I would agree.

Senator ALLISON—It is not time we need. We want a major fundamental change in this proposal.

Mr Hill—As it stands, the only way the industry would grow under this current format is if there were some regulation or requirement—a mandate, perhaps—for major oil company uptake of the production that exists and/or is proposed.

CHAIR—This bill is not about mandating the purchase of biofuels by major oil companies.

Senator ALLISON—Chair, I raise a point of order. The line of questioning is about the future of the industry, and the point that is being made by Mr Hill is that the oil companies are not prepared to take ethanol on board. They have been reluctant to do that and it is not unreasonable for him to then discuss the matter of forcing them to do so through a mandate.

CHAIR—Senator Allison, there is no point of order. I have, as is my custom, permitted you, Senator Murray and other senators to jump in to contribute to the discussion out of the order of the call in order to facilitate the free flow of the discussion, and I am applying the same principle to myself by asking a question arising from your question to Mr Hill—and I will proceed. Mr Hill, this bill is not about mandating the use or acquisition of biofuels by the major oil companies, is it? As I understand it, your complaint, and you may very well have a good point, is that the effect of the operation of the bill, as it is currently written, would be to deprive your industry of the benefits of the scheme put in place by the government a couple of years ago—in fact, as a consequence of the recommendations of this committee.

Mr Hill—That is correct.

CHAIR—That is your point?

Mr Hill—That is my point.

CHAIR—That is what I thought.

Mr Gordon—Chair, if I may just add something that may assist. The government has put in place an action plan process under which the oil companies have given commitments to voluntarily take up certain amounts of fuel. Our understanding is that, when that meeting took place between the Prime Minister and the oil companies, there was a choice between doing it voluntarily and the government looking at other mechanisms.

Senator JOYCE—How much ethanol are the oil companies actually using now?

Mr Gordon—Their target for 2006 is 89 million to 124 million litres, until December this year. There is some room possibly for dispute, but we try to follow this up quite clearly and regularly at least twice a month with potential producers. We do not see the evidence at this

stage that the oil companies will meet their 2006 target, but we do not know everything that is going on. We do monitor—

Senator MURRAY—Sorry, but when you say 2006, do you mean 2005-06 or the 2006 calendar year?

Mr Gordon—2005-06.

Senator MURRAY—So the financial year?

Mr Gordon—No, it will end in December.

Senator MURRAY—So it is a calendar year?

Mr Gordon—Correct. So we have yet to see that. If the target is not met, it will be a major issue because it will send a signal to the banks and other financial institutions that things have not changed. Now, I am not here to be critical of the oil companies or anybody else involved, except to say that is the situation that we are confronting. And we have more interest in this program being a success than anybody else.

CHAIR—Indeed. But the message that comes through loud and clear, at least to me, both from you and from the witnesses from the biofuels industry that we heard from before lunch, is that the complaint about this bill is that it would nullify the effect of a government policy which everybody seems to be very happy with.

Mr Gordon—Correct.

Mr Hill—Yes.

Senator MURRAY—That is right.

CHAIR—Does anybody have any more questions? Senator Joyce.

Senator JOYCE—The 2012 reduction in the excise is a crucial issue, and I have been trying to track that through but I cannot find that stated anywhere in the bill. Obviously, if you are going to call for an amendment or change to fix that issue, we need to know where it says that. Where is it?

Mr Gordon—I cannot tell you, and that is one of the problems with the bill. Our concern with respect to that is that, if the evidence is vague, it means you can interpret it in many ways.

Senator JOYCE—I am not vague. If I can find out where it is, I will certainly be making moves to change it. I put that categorically on the record.

Mr Gordon—Perhaps our Treasury colleagues will be able to help us there later on this afternoon.

Senator JOYCE—Do you feel that, in the last six years, the oil industry has been dragging the chain in meeting its objectives?

Mr Gordon—To be fair, I think it is too early to judge. We place a lot of importance on them meeting their targets as specified. The oil companies know their business better than anybody else, and, if they set a target and made a commitment to the government and the Prime Minister, you would expect them to be able to meet it. We have concerns about whether the target this year will be met, but nobody will be happier than us if it is met.

Senator JOYCE—Did you say 56 per cent of the trade account deficit is due to the importation of fuel?

Mr Gordon—It is 63 per cent.

Senator JOYCE—Do you feel that the implications of this bill as it stands, and as Senator Brandis has properly pointed out, run contrary to a government policy on what they were trying to achieve on this issue?

CHAIR—Senator Joyce, can I correct you before I am verballed. I did not point that out. I said that that is what I understand these witnesses to be pointing out to us.

Senator JOYCE—Fair enough. You believe the implementation of this bill as it stands would further exacerbate the problem of the trade account deficit?

Mr Gordon—This industry is at a very modest scale at this time but the biofuel industry is one of the fastest growing industries in the world because governments in countries such as the United States, the European Community, China, India, Japan and many others see that there is a vital role for alternative fuels, particularly renewable alternative fuels such as ethanol and biodiesel, to play a role in addressing these issues. President Bush has predicted that the United States has the capacity to replace 50 per cent of its current dependence on crude oil through biofuel development in that country.

Senator JOYCE—You and other witnesses believe that the effect of this bill runs contrary to the intent of previous government policy. Has anybody from any department given you any statement that that is what they intend to do—they intend to change a former government policy on this issue?

Mr Gordon—The clear message that we have got is that there will be no change in policy.

Senator JOYCE—You are basically saying it is a dilemma between the intent of this bill and the intent of what the government wanted to achieve.

Mr Gordon—All I can tell you is that the advice we have received from the Minister for Revenue and Assistant Treasurer, and Treasury, obviously, is that the government is not inclined to change this bill at this time. We hope to convince them otherwise that it is in the national interest to do so.

CHAIR—That is why we are here, Mr Gordon, having this hearing so that the parliament can consider the matter.

Mr Gordon—Thank you, Mr Chairman.

Senator JOYCE—And it is the proper course of the Senate too—and doing a very good job at it. Amongst the people that you represent, Mr Gordon, do you have any idea of the investment they have made in relation to that—the intent of the government policy as it formerly stood?

Mr Gordon—We think it could be in the order of \$600 million to \$700 million. I cannot be precise because the cost of setting up a biodiesel plant is significantly lower than for an ethanol plant. On average, the yardstick for an ethanol plant to produce one million litres is \$1 million investment.

Senator JOYCE—Would that \$600 million to \$700 million investment made in the Australian economy presently be stalled, reduced or destroyed by the intent of this?

Mr Gordon—I cannot say exactly but it could be one or all of those things. The box set up by the banks and financial institutions that many of our producers have been able to get a tick in in the past has been on the issue of, ‘Can you demonstrate that you can get your fuels into the marketplace?’ If there is uncertainty associated with this bill, if we do not see the take-up of the fuel commitments of the oil companies in this bill, then yes the risk is that the financial institutions and banks will not support the future development. With respect to biodiesel plants, they have picked up on the surge of international interest in investment in biofuels and there have been a number of very successful capital raisings in the public revenue market.

Senator JOYCE—To be more partisan, where do you believe the effects on the economy of the loss of the biorenewable fuel industry will be most keenly felt?

Mr Gordon—It will be felt in a couple of ways quite quickly. Biofuels have been demonstrated in the world as one of the few mechanisms to offer the consumer price stress relief for fuels. The real tragedy here in Australia, if we go through another period of policy uncertainty, is that we will not be able to get enough bank or investment interest for a number of years to start again. This industry may languish for the next 10 years in Australia while the rest of the world surges forward.

Senator JOYCE—A lot of that industry will be in regional Australia?

Mr Gordon—The majority of it will, for natural reasons. That is where the feed stocks are, so that is where you are going to set up your plant.

CHAIR—Thank you, Mr Gordon and Mr Hill. That is very helpful.

Senator JOYCE—I still have some questions for the Treasury. I was going to put them on notice because I have to leave at three o’clock.

CHAIR—Do you? That is a shame. Yes, put them on notice.

Senator JOYCE—I wanted to put that on the *Hansard*.

CHAIR—While we are having this discussion now can I indicate, in view of the very short time frames for reporting, we will have to ask the Treasury to have those answers to questions put on notice by Senator Joyce—and indeed anyone else—by the close of business tomorrow.

Senator JOYCE—I have sent them through to the committee now, so they should be on the way. Obviously they are in light of the questions we have been asked.

[2.52 pm]

HUMPHREYS, Dr Len, Chief Executive Officer, Australian Biodiesel Group Ltd

KENIRY, Dr John, Chairman, Australian Biodiesel Group Ltd

LOVELADY, Mr Craig Matthew, Director, Bioworks Australia Pty Ltd

IVERACH, Mr David, Chief Executive Officer, Investments, Transfield Holdings

CHAIR—The committee has received the written submissions of each of these three groups of witnesses. The submission from Australian Biodiesel Group Ltd has been marked confidential, so I propose, unless anyone has an objection, to follow the course that I recommended in the morning with a confidential submission—that is, to ask senators in framing their questions to take care not to expose any confidential material in the submission and for the witnesses from Australian Biodiesel Group Ltd, if they feel that a response to a question would require them to reveal any confidential matter, to indicate that to the committee in the first instance and we will consider the matter. I am also mindful of the time and the fact that two of the four witnesses I see before me have already given extensive evidence. So, having regard to that, can I ask honourable senators to limit their questions to matters that have not yet been canvassed by the committee to the extent to which they feel able. Mr Lovelady and Dr Keniry, we have not heard from either of you yet. Do either of you wish to make a statement to the committee?

Mr Lovelady—I am most grateful for the opportunity to present to you this afternoon our concerns with the fuel excise bill 2006. Bioworks is a company we formed last year to facilitate communities in regional Western Australia to get established with biodiesel production. We start by providing an education service for people to give them an understanding of the fuel. We supply equipment for the production, we provide processing materials and we support those activities by offering advice on the manufacture of the fuel. We also help with dealing with the regulations that confront the industry. Over the last few months, we have been to towns ranging from Morawa in the north-east wheat belt to Eaton in the south-west. There is substantial and widespread interest in biodiesel in our regional communities. We have ample raw materials, concentrated use of fuel and rising fuel costs. In theory it should not be hard to create a viable and prosperous industry throughout our regional communities.

In the current global environment of rising oil prices and global warming, any legislation that encourages the use of fossil fuels over renewable fuels should not be accepted, and that is what this legislation does. There are a number of areas of concern which we have with the legislation. Firstly, this bill is effectively a tax on biodiesel. Our customers in regional communities are not big fleet operators or big oil companies; they are farmers and small businesses operating a few trucks and heavy equipment. They get no special deals from big oil, and there are no fleet discounts or rebates for them; they pay bowser prices and they are struggling. For them, the opportunity to get a fuel that is 20c less is the difference between making a dollar and not. The customer pays a net price for fuel, and that is what they work on. By changing the treatment of the manufacturer's grant for biodiesel, users of the fuel will no longer be able to claim rebates. This will increase the price of biodiesel and this will be worn

by the manufacturer. It impacts directly on the viability of an industry that is in the formative stages of development.

Secondly, the bill adds a lot of complexity to the use of biodiesel. For a simplification bill, it is nothing short of disastrous for the suppliers of biodiesel. We are expected to ask our customers to track the underlying excise paid on fuel and claim their rebates based on a complicated method. There are no accounting systems capable of doing this, and it defies reality. There is a cost to this administrative burden, so, when considering whether or not to use the fuel, customers ask a very simple question: ‘What happens to my rebates?’ The proposed system is too hard. Small businesses are already struggling under the burden of compliance. They do not need further complexity.

Thirdly, the bill gives an unfair advantage to the suppliers of the five per cent blend. The inputs to biodiesel are basically traded as commodities. The advantage for our regional producers is that they avoid double transportation—that is, they are making the fuel where the raw materials are available and the fuel is consumed. If this legislation comes to pass, they will compete for raw materials against a central factory that has a 38c advantage. The transportation advantage will be lost, and the raw materials will be acquired by a supplier to a blend distributed as diesel. These central producers will be able to pay more for the same raw materials.

For our primary producers the position is worse. The changes in the bill make it uneconomic for them to use biodiesel, yet these people are the most affected by rising oil prices. For people living in metropolitan areas, fuel is a lifestyle choice. We manage rising costs by changing our living patterns: we downsize our vehicles, catch public transport and travel less. For regional people, they have no choice: crops need to be planted, harvested and taken to market; they cannot downsize their tractor or semitrailer. Under the proposed bill, biodiesel will be uncompetitive with petroleum products when sold to recipients entitled to a fuel tax credit.

This group has been broadened under the bill. This narrows the available market for the sale of biodiesel. As an industry, we must contend with the problems of fragmentation and disinformation. We are an emerging industry that lacks cohesion. These changes have been brought forward at a time when as an industry we are not capable of cohesive action.

In closing, I would like to quote from a letter that we received recently from John Hassell, a farmer in Pingelly with whom we have been working to develop a biodiesel facility. This was received after I advised him that the project would be on hold pending resolution of this legislation. Pingelly is a small community two hours south-east of Perth. In the last 30 years the community has lost 22 businesses, including machinery dealerships, stock agents, fuel distributors and the like. The most recent losses to the town have involved CBH’s decision to shut the wheat bin, requiring farmers to use the neighbouring Brookton bin 30 kilometres away, and the closure of the high school. In short, the community is in a negative spiral or decline. John Hassell wrote:

With the rising price of crude oil, it has put a lot of pressure on farming industry in our area, but there is a bright side. The bright side is biodiesel. It is already here because most of the farmers are already growing it in the form of oil from canola and tallow from the abattoir that we sell our stock to. The basic essentials of a new and really possible industry that would put some life back into our region,

biodiesel can actually compete with crude oil at present, providing better returns from the crop, lower fuel prices for everyone in the community and best of all for our region, employment in the many stages of production and distribution. We really have a chance to improve life in the bush because we are finally competitive with the major new industry. It is the chance to improve thousands of like communities across Australia. It is environmentally friendly and community friendly. Please, don't ruin the first good chance we have had in better than 50 years of putting little communities back on the map by changing the current legislation.

Dr Keniry—I have a few overview comments. There has been quite a lot of discussion this morning about the foreseeability of some of the changes in excise import/exports. People who read the biofuel task force report know that it is a complicated area, but there should not be any surprises that these things were coming. It was made clear by Treasury and so forth to the biofuels task force and then repeated in the document that these were the changes that were seen as consistent with the white paper.

CHAIR—Dr Keniry, remind us. You were a member of the biofuels task force.

Dr Keniry—I was a member of the biofuels task force. Treasury put out an explanatory note just before that group started, and caused a lot of consternation amongst some people who had made assumptions about how the rules were going to be interpreted. Then they were clarified—still, I would say, in a complex way. To the best of our ability we put them down in the report. They were predictable. I will come back to the impact of the changes on the viability, but I think they were reasonably predictable.

CHAIR—So you take issue with those who have suggested that the industry has been taken by surprise by government policy.

Dr Keniry—Some people, without a doubt, have been taken by surprise.

CHAIR—But that is not the government's fault.

Dr Keniry—I believe the information was in the public domain if you were prepared to sit down and analyse it and look at it. The one area that was not in any way envisaged in the biofuels report was the changes that were then made subsequently to facilitate this BP renewable diesel, or whatever people want to call it. That was certainly not envisaged. It is clear that that has been a change in the ground rules for this industry because it has provided something that is not biodiesel to be able to compete with biodiesel. That change has resulted in some changes in the bill so it can be incorporated. It certainly was not on the agenda in any way at all in the biofuels report.

CHAIR—Dr Keniry, just help me here. Are the changes to BP that are reflected in this bill consequential changes or are they legislated for by the bill?

Dr Keniry—I think the bill expands the definition of what can be included to get the excise concession to include, for example, having tallow go into an oil refinery and come out as a five per cent blend in diesel, and that was not even envisaged as a technology that might be applicable.

CHAIR—So it is certain provisions in this bill that give effect to these arrangements with BP which you say were not envisaged at the time the biofuels task force reported. Is that right?

Dr Keniry—Correct. That change has delivered a major competitive change, particularly in relation to retail diesel. That is where the excise concession is available in full to biodiesel, as compared to petrodiesel. But this BP diesel, if you like to call it that, based on tallow will now get the excise concession that we thought was originally going to be available just to biodiesel.

CHAIR—This point which, for shortness, I will call the BP point, is a completely separate point from the principal criticism that was being made of the bill from the point of view of the biofuels lobby—that is, that it sets to nought the effect of the producer grants scheme. You are saying that, allowing for that, there is an additional vice in the bill, and that is that it gives one of the major producers a benefit that it was not envisaged that it would enjoy but that would be enjoyed by the specific biofuel sector. Is that right?

Dr Keniry—Correct.

CHAIR—So we are dealing with two quite separate issues here, and you are not happy with either of them, I gather.

Dr Keniry—The first issue in relation to the changes is going to have an impact on the economic state of the industry.

CHAIR—Yes, that is about the economics.

Dr Keniry—The other issue in relation to the BP point, as you call it, has changed the ground rules quite significantly—

CHAIR—It changes the shape of the market, I suppose.

Dr Keniry—from the ground rules under which a lot of people chose to invest in the biofuels industry.

Senator MURRAY—I seek clarification, through the chair. Dr Keniry, did the biofuels task force look at the issue of renewable oils?

Dr Keniry—They looked at ethanol and biodiesel.

Senator MURRAY—No, the renewable oils issue?

Dr Keniry—No.

Senator MURRAY—Let me rephrase that; I have phrased it wrongly: recycled oils?

Dr Keniry—Used cooking oils, yes.

CHAIR—No. Dr Keniry, earlier in the day we had some evidence from witnesses from the recycled oil business.

Dr Keniry—This is recycled petro-oils. No, we did not.

Senator MURRAY—That is what I wanted to know.

CHAIR—Dr Keniry, did you finish your opening remarks?

Dr Keniry—No, not quite.

CHAIR—Please continue.

Dr Keniry—So the first issue was what was expected and what was unexpected. In my view, the unexpected bit is the quite significant change in the competitive environment. In terms of the economic state of the industry, in short, I think what has been said about unlikely future investment in the industry is quite correct. As a company director looking forward, investing in this biodiesel industry is much riskier now than we thought it was a few months ago before we saw the full extent of this bill.

The biofuels task force said that at the oil prices they were looking at, which were ABARE forecasts of around \$40, the biodiesel industry was unlikely to be competitive in the long run, having regard to where the government was going with subsidies. However, the oil price has gone up way beyond the \$40 that was on the table when this report was done, so people do expect that it is now commercially viable. It is at present, but if all these other subsidies are now lost—whether or not they were expected to be lost—then it is an extremely marginal proposition. Part of the reason for that is from within the industry. In getting a new product into the market, there are extra costs—you have to blend it, you are a small producer compared with big ones and you have to do a lot of your own distribution. So there are some costs that perhaps were not looked at, and a very significant factor among the larger potential users is that they want big discounts. In effect, they are saying, ‘If I am going to try this stuff then I want a discount.’ I think some of the earlier figuring was done on the basis that people would change their behaviour for half a cent while the reality is that they will not change their behaviour for half a cent.

There have been changes internally in the industry. However, there is no doubt that, if these shorter term subsidies are lost, there will be a serious diminution in investment going forward and perhaps even in the viability of investments that are occurring now. It seems to me that the government has spent \$40 million or so on encouraging the establishment of some plants. If the government continues to do what it is doing now, it will be walking away from the \$40 million of taxpayers’ money it has put into getting this industry going. I submit that there is a need for ongoing subsidies to help this get on its feet, whether you can see that need existing or not. Frankly, I think the government has made a mistake with the so-called ‘BP issue’. The government should undo that and restore the potentially competitive environment in the retail sector. That is the sector where excise concessions were always available and which should have been a good area for biodiesel producers to get into.

CHAIR—Anybody can answer this question: were there consultations with the biofuels industry in relation to the BP issue?

Dr Humphreys—There were not.

CHAIR—You would not necessarily expect there to be any, given the shape of the arrangement. But there were no consultations; is that right?

Dr Humphreys—No.

Dr Keniry—I am not aware of any. There were certainly no consultations with me.

Senator STEPHENS—Thank you for that submission because you have clarified very clearly for us some of the concerns we have had. I want to go to submission No. 7, which is from Bioworks Australia. Mr Lovelady, in this submission you recommend changing the wording of the legislation.

Mr Lovelady—Correct.

Senator STEPHENS—You suggest that, in section 43-10, reducing the amount of the fuel tax credit cleaner fuels grant, sections 1 and 2 be deleted. You then suggest that section 43-5(3) should read ‘a grant for on-road and off-road alternative fuels’ and that section C should read ‘a grant for petrol, diesel and biodiesel’. Would those changes address the concerns of your industry, other than the five per cent BP issue?

Mr Lovelady—I think there is an overrider in the legislation; it is a little hard to read. Off the top of my head, it is section 41-15. It says that, if you already have received a credit, no further credit can be payable on the fuel. It is a little hard to identify, but that is the problem section in the legislation as well.

Senator WEBBER—That section in the legislation reads, ‘No fuel tax credit if another entity was previously entitled to a credit.’

Mr Lovelady—Correct.

Senator WEBBER—And, ‘You are not entitled to a fuel tax credit for taxable fuel, if it is reasonable to conclude that another entity has previously been entitled to a fuel tax credit or a decreasing fuel tax adjustment for the fuel.’

Mr Lovelady—Yes. You will have to ask Treasury. I am not a lawyer and so I cannot speak for the legislative effect of how that operates.

Mr Iverach—This morning I was just sitting and listening, although I tried to enter some of the debate towards the end. But, as a recent investor in the industry, I would make some remarks, if I could be allowed the opportunity to do so.

CHAIR—Are these new points that you have not yet had an opportunity to make?

Mr Iverach—Certainly. Given what has been said already, I have changed what I was going to say to try to shed some light on some things and not repeat others that have been stated.

CHAIR—I will give you the opportunity to put some views on the record, but please try not to cover matters that have been dealt with already.

Mr Iverach—Transfield brings a slightly different perspective to looking at the industry because it was just a few months ago that we decided to invest about \$30 million in the industry. That was part of a deliberate move by Transfield to move into a new sector—the alternative fuels and energy sector. We wanted to participate in the development of these industries as we have in the past participated in the development of defence, construction, infrastructure and services. We think our decision makes us one of the largest investors in the industry and, obviously, we spent a lot of time looking at the industry and its prospects—trying to understand where it would go—before we did that.

You would have heard me say this morning that we were aware of white papers, the biofuels task force et cetera. But we were very influenced in the decision by the frequently publicised position of the government that it supported the industry, and that there was excise relief and this was going to be phased out in the future. That struck us as an appropriate policy for a fledgling industry—some help for a few years, and then a sort of a sunset clause, a

phase-down. You have heard, I think, quite amply, from a lot of us, that most of us took that excise holiday or relief as a form of subsidy—that it gave biodiesel a price advantage over conventional diesel.

If we made any mistake at all in looking at the future of the industry, it might have been to assume that, when we got into the detail of this bill, there would still be support for the biodiesel industry in that way. That is the position throughout Europe, Japan and North America; generally, it is recognised throughout the world that the biodiesel industry does not grow and survive without subsidies. As you have already heard, from 1 July that will not be the case in Australia; the excise benefit, or the lack of excise compared with everyone else, will suddenly be wiped away from about 90 per cent of the biodiesel that is sold in Australia. We do not have a problem with the excise relief given to business users. But we do have a problem with doing that and not having any compensating arrangements for biodiesel, because, as you have heard, biodiesel would thus have no competitive attributes that would mean that people would buy it.

CHAIR—Isn't this the same point that has been made by other witnesses as well—that is, that the effect of this bill will be to set to nought the benefit of the producer grant?

Mr Iverach—Yes. But in the remaining part of the market—in other words, in that 10 per cent or less of diesel that is used in what we call the retail market—biodiesel still has its competitive advantage, in the way, we understand, the new rules will work. We are still waiting for clarification, I think, of whether those rules cut out at five per cent biodiesel or something a bit more. That did feature prominently in our assessment of the reason to invest in the industry, because we could see there was a threat to a lot of it. We were hopeful that it would not be as dire as it now appears. But we could see that there was at least some retail part of the industry that could support a smaller biodiesel industry.

As Dr Keniry noted, the decision to give BP the same concession for putting the same feedstock in its existing refinery and making very large quantities of it has two very significant effects. First of all, it takes a very large fraction of the market that was not factored in. It was factored in as being a biodiesel market but not as being subsumed in that direction. Secondly, it puts pressures on the feedstock cost.

CHAIR—The growers are going to be pretty happy about that, aren't they?

Mr Iverach—The growers will be happy about that if we continue to compete for that, but I do not think anyone knows how the market, having been taken away and with production having been scaled back to meet that, is going to find its own level, except that it will certainly have an adverse impact on the biodiesel industry.

CHAIR—On your sector of the industry. But I suppose BP are going to say, 'We're players in the biodiesel industry too now.'

Mr Iverach—I do not think they claim biodiesel anymore, but you are quite right—

CHAIR—You might have let the genie out of the bottle by making this such an attractive proposition that some of the majors are now muscling in.

Mr Iverach—It is with considerable irony that we see that this bill, or its cognate bills—the amendment for the BP change is not in the fuel excise bill but in the cognate bills that come with it—

CHAIR—The consequential amendments bill.

Mr Iverach—Yes. It is with considerable irony that we see a very real threat to our investment in the biodiesel industry and a windfall of some \$200 million or so to BP as a result of the same bill. Yes, that is good news for them and bad news for us. As a company, we are accustomed to going with the swings and roundabouts of government policies et cetera. Our real interest is whether this is what the government and the parliament really intended to be the consequence of these bills. It is one thing for a government and a parliament to make legislative changes where there are winners and losers. Just about every bill does that, and we can accept that. In recent times, we have become both concerned and encouraged that the consequences of the legislation may not have been fully recognised. If that is the case, then perhaps there is some hope that there can be amendments that can rectify the damage that would otherwise be done to this industry.

CHAIR—To your sector of the industry. I remember sitting through a hearing of this committee a couple of years ago which recommended successfully to the government an extension of the phasing-in period for the biofuel excise—the tax-holiday period. Of the many arguments in favour of doing so, one was the argument from certain senators that it would give a boost to struggling rural communities. From the other side of the table—I think from our friends the Australian Democrats, among others—was the argument that it would be good for the environment. Both of those seemed on their own terms to be cogent arguments. What you seem to be facing now is that you have been too successful by attracting at least one of the oil majors into the biofuels sector. Those benefits—the environmental benefit and what you might call the parochial benefit—are still going to be felt, but they are going to be felt as a result of the participation of a big company in the biofuels sector rather than the development of smaller companies in a more specific market niche. What do you say about that?

Senator MURRAY—I would like clarification when you answer. I have become confused with your discourse. Are you still of the opinion that this bill is a terminal threat to the industry, because that is not what I have heard you say? If that is what you meant, it would be a threat to oil companies as well, because the industry must include everybody who participates in the industry not just your particular sector.

Mr Iverach—That is why I differentiated the market that can benefit from a product that could be marketed as diesel. That is the point I was making this morning about the level of biodiesel you can have in diesel and it still be diesel. That is an important issue. It leads to BP being able to take advantage of that and to have a windfall of a couple of hundred million dollars at the same time that most of the market for the biodiesel industry is in the long-distance trucking companies and off-road markets where the rules are different and you do not have that competitive advantage. As Senator Brandis pointed out, I do not think BP sees itself as part of the biodiesel industry, but this bill is certainly good for BP and for any other oil major which follows in their path.

CHAIR—If BP has decided that it can see a benefit for itself here, which it is entitled to do, then it probably will not be very long before the other oil majors make the same judgment. Parallel conduct is not entirely unknown among the oil majors.

Mr Iverach—The statement that the oil companies make is that the BP refinery in Brisbane is unique in Australia with its hydrogenation capacity and the availability of hydrogen—

CHAIR—I see.

Mr Iverach—and that other refineries would have to make discrete investment decisions to do that. There is nothing in this bill that prevents them from doing that and, when they so do, enjoying the same benefits.

CHAIR—They will just get their accountants to do a calculation of the cost of hydrogenating one of their refineries versus the benefit that the extra revenue—

Mr Iverach—I would assume the work has either already been done or is under way.

Senator MURRAY—Let us come back to some clear language. You say it is a terminal threat to your industry. I am going to translate that. That means it is going to kill your industry. Are you telling us that this will kill your industry and that the only people who will benefit are BP? Is that what you are saying?

Mr Iverach—I did not use the words ‘terminal threat’ or ‘kill the industry’.

Senator MURRAY—Are you Transfield Holdings?

Mr Iverach—Yes.

Senator MURRAY—Submission 24a—

Mr Iverach—I am going to be hung by some words, I think.

Senator MURRAY—Your submission says:

In conclusion, we see the Bill as a terminal threat to an industry which we believe is in Australia’s interest to develop.

Are you saying to me that you did not write that?

CHAIR—Well, you know—

Senator MURRAY—He just said to me he did not write that.

CHAIR—All right, Senator Murray. Mr Iverach, just tell us what your position is, having had the benefit of this discussion. I do not think anybody is going to make Perry Mason points about the language you used in your submission.

Senator MURRAY—I raise a point of order, Chair, and I would appreciate not having that kind of remark made. I have a difficulty because I had the impression—and it might be my fault, not yours, Mr Iverach—that overall, Mr Iverach has been giving us the curate’s egg kind of approach: this bill is good in some places and not in others, and so on and so forth. That is at odds with what I read to be his conclusion. He writes: ‘In conclusion it is a terminal threat to an industry.’ I thought it was important to discover whether, since you wrote the submission and since you heard the discussion—

CHAIR—Then let me rule on your point of order.

Senator MURRAY—I am still on my point of order.

CHAIR—Let me—

Senator MURRAY—Can I please complete my point of order?

CHAIR—I thought you had finished.

Senator MURRAY—I am entitled to do so. I want to know whether he has changed his position as a result of hearing evidence and so on or whether he remains of that opinion. That is why I pursued that point.

CHAIR—Obviously there is no point of order, but I think it is fair to say that we all want to know—all the senators want to know, from their different perspectives—what your position actually is Mr Iverach.

Mr Iverach—I think that the ‘terminal threat’—words which I used—is to the growth and further development of the industry. I would hope that the existing plants that are in operation or about to commence operation—of which there is about 300 million litres worth—will find a way to survive. They will not be as profitable as they would have expected and they will have to scramble in ways that industries often have to do. But this bill is a terminal threat to the expansion and growth of a viable biodiesel industry in Australia, and I exclude the oil majors from that.

Senator ALLISON—Dr Keniry, could we go back to the BP amendment, which I understand was put in the House of Representatives during that debate. You talked about this being something unexpected. Could you explain what the implications are beyond BP for this? Can you, or anyone on the panel, indicate what kind of biodiesel, if it is biodiesel at all, we are talking about here in hydrogenated tallow? What does that mean? Is it cheaper to produce? Has it just happened that BP has a ready source of hydrogen and it all comes together in a cheapish way? Is the whole industry benefiting from a shift from perhaps all the oil companies in this direction to take up the 350 megalitres promised to us?

Dr Keniry—I will go as far as I can with the science. I will probably have to ask Dr Humphreys to help me at the end. Basically, if you take what has been said this morning, biodiesel into the on-farm sector, if these subsidies go, is not much of a proposition. Biodiesel into the mining sector is not much of a proposition for the same reason. Biodiesel into the long-distance trucking business is not much of a proposition, if these changes go through. The retail sector, which only accounts for about 15 per cent or so of the total diesel, was the area, because it had excise concessions, where there was still significant financial reward for people to sell biodiesel into that industry. As things tiered down, that was an important sector for us to stay in, if the subsidies were removed.

By allowing BP into this business and supplying five per cent renewable diesel based on the same raw material, the external consequences will be increased competition for tallow because they will use a significant amount and inevitably the price will rise and that will adversely affect the viability of biodiesel producers. As all the alternate fuel suppliers have recognised, it is very difficult to break into the retail sector because the retail sector, mainly through the distribution, is controlled by the oil company majors. If they had the choice to buy

biodiesel or make it themselves, they probably would have bought biodiesel if there was some money to be made by adding biodiesel. Under this change, they can effectively produce a product that looks like diesel but gets the excise concession on five per cent of it.

In my opinion, the probability of BP now buying biodiesel from biodiesel producers to distribute to retail has almost disappeared. It is not just a question of allowing someone else into the industry and changing the rules after the race has been started; in effect, it has also delivered to a major distributor an ability to effectively go by themselves and therefore not have to deal with the biodiesel sector, into which, as I have said, the government has put quite a significant amount of money to set us up. For the technicalities, I think I would rather leave that to Len to explain. He is more of a chemist than I will ever be.

CHAIR—Do we need the technicalities?

Senator ALLISON—I think we do, yes.

CHAIR—I am fearful that at least one of us will not understand them.

Senator MURRAY—You can add me to that.

Senator ALLISON—I think we need to understand, Chair, whether this is an inferior product.

CHAIR—The point has been made loud and clear about the effect of the bill, and the point is either a good one or a bad one. We are straying a bit far but, since Senator Allison is so keen on having the science on the record, over to you, Dr Humphreys. Keep it as simple as you can.

Dr Humphreys—The science is quite simple. The globe has recognised biodiesel as being a methylestra of natural occurring fatty acids. That is what the world sees as a biodiesel. The environmental benefits of that have been measured to infinity—lack of carcinogens and a reduction of greenhouse gases. As somebody said this morning, many years have been spent on understanding what the output is from an engine using biodiesel, which is a methylestra of fatty acids. It is well defined and it is an isolated chemical that you can look at, and it has a standard which it has to conform to.

The thing about BP is we do not know what we do not know. They use tallow so that is a naturally occurring product. There is the first agreement. But with respect to the processing, the end product and the isolation of the chemical, there is zero information to say it has any environmental benefit. It is certainly not a methylestra of a fatty acid, which is what the world defines as biodiesel; therefore, it is definitely not biodiesel. It is significantly modified by putting it through the process, such that you cannot recognise it or identify it as a separate chemical. Therefore, you cannot say whether it meets the standard because there are no standards for this. So the answer is that we do not know, and that is one of the problems with the whole debate. There has been a complete distortion of the definition of the benefits of a biofuel, and tallow has been tacitly linked as a biofuel purely because it uses, as its feedstock, a renewable source. Everything else is a distortion of the fact from then on.

CHAIR—Are you saying that what BP is doing is not admixing a biofuel?

Dr Humphreys—Yes.

CHAIR—And the effect of this would be to give them the benefit which was designed for the biofuels industry by admixing the tallow, and you say that should not be counted as a biofuel? That is your point?

Dr Humphreys—That is correct.

Senator WATSON—Mr Lovelady, I would like to have another read of your opening comments because I was quite moved by them.

CHAIR—I forgot to ask. If your opening remarks are in typed form, would you be able to give a copy of them to the secretariat so that they can be distributed.

Mr Lovelady—Certainly.

Senator MURRAY—Thank you both for the comprehension of your opening remarks and your submission. Just one thing: I understand that 75 per cent or thereabouts of all diesel sales are off road? Is that correct?

Mr Lovelady—On road.

Senator MURRAY—About half and half?

Mr Lovelady—Yes. It is predominantly on-road diesel because it is on-road transport and then—

Senator MURRAY—It is just not through the retail sector?

Mr Lovelady—It is distributed wholesale bulk. In Western Australia we have about 16 wholesale distributors.

Senator MURRAY—Give me a rough feeling. If 25 per cent go through retail and 75 per cent is both on- and off-road sales by heavy users, how much of that is off road?

Mr Lovelady—About half of it. If you pick a town—

Senator MURRAY—Do not worry about that. If about half the sales are off-road, does this bill have a more negative consequence for you with off-road sales than on-road sales?

Mr Lovelady—Absolutely. Off-road users will never use biodiesel as a consequence of this bill.

Senator MURRAY—So if the committee were to recommend an area where the government should concentrate any remedial effort, it would be off road. Is that correct? If they did not want to go the whole monty—to use that expression—you would prefer them to concentrate on off road?

Mr Lovelady—I think it will be very hard to do that because you end up with complex distribution systems. It is already hard because you have to mix the fuels and at some point you have to blend in one way or another.

Senator MURRAY—I was thinking of the grant and subsidy schemes, because they have operated on an off-road basis before.

Mr Lovelady—The grant and subsidy schemes exist. Today we receive subsidies from the department of the environment which is the manufacturers grant.

Senator MURRAY—I understand that.

Mr Lovelady—We get subsidised by DOTARS to create regional services, regional development and now Treasury is taking those grants away.

Dr Keniry—The long-distance freight market is an important one; that is the one that has been most receptive up to now. When these subsidies go it is problematic whether that will continue.

Mr Iverach—The most attractive markets are the biggest users that take the highest proportion of biodiesel, because the logistics of transport, storage and blending are much simpler. At the other extreme, in the retail market of making a fuel that you can put in a family owned four-wheel drive diesel vehicle, distributing that to thousands of service stations is quite complex.

Senator MURRAY—That is why I assumed the highest users were likely to be off road.

Mr Iverach—The best users to target are in some ways the long-distance trucking companies, because they have a lot of their own infrastructure, they buy in bulk and they store their own fuel. Mining companies and some marine applications have the same things. The big farmers' cooperatives would have similar things. Delivering to a small farmer is probably as difficult as delivering to a small service station.

CHAIR—Thank you, gentlemen, that has been very helpful. The next witnesses on our list are from the Royal Automobile Club of Queensland, but as they are not here we will go straight to the National Farmers Federation.

[3.43 pm]

ARKLE, Mr Peter, Policy Manager, Rural Affairs, National Farmers Federation

FARGHER, Mr Ben, Chief Executive Officer, National Farmers Federation

CHAIR—Welcome. I invite one of you to make an opening statement.

Mr Fargher—I thank you for the opportunity to provide some comments to your committee today. By way of background, NFF did contribute to the development of the government's energy white paper. We provided a detailed submission in August last year. Comments with regard to fuel policy, fuel taxation and cash flow issues need to be understood in the context, well understood by you, I am sure, of an environment where fuel prices at the current levels being experienced are placing enormous pressure on farmers and regional communities. Farmers are very aware that we are not the only people in the community facing these high fuel prices.

Having noted that, the thing about the farming sector is that we are very pressured in terms of passing these costs on. We are at the end of the market chain. We cannot pass the costs on when we export 80 per cent of our produce. Given the global competitive nature of the marketplace and domestically, with two supermarkets controlling so much of the retail market, we find it very hard to pass on these costs. That does place significant pressure on our sector.

Notwithstanding that, I would like to give you one example from one of our members using actual data, April 2004 to April 2006. I asked one of our members the other day to look at his fuel bill so we could give you some context. He has faced an increase of 69 per cent for diesel fuel over that time and 36 per cent for fertiliser. Obviously, it is not just the fuel price, the business input of fuel, but it leads on to fertiliser. Obviously, freight charges have a significant impact which, as I said, we cannot pass on, particularly relevant in the cropping sector. Based on this pressure, and the pressure some of the sector has been under in regard to drought and therefore cash flow issues, we have been concerned in regard to the bill as it relates to cash flow around a move to claim the rebate only through the BAS system.

CHAIR—Is that your main point?

Mr Fargher—That is our main point.

CHAIR—Is it your only point?

Mr Fargher—No.

CHAIR—Go on.

Mr Fargher—I will be brief because I understand that changes have been made in the last few days. So we have issues with the bill. At large we have made those points and they related to biodiesel. They relate to the acceleration of fuel excise. But our major point here today was about cash flow in regard to the BAS. We stand by the fact that we supported the option to use the BAS but we wanted flexibility around that, because particularly the cropping sector may have cash flow difficulties if they could only claim the rebate through the BAS. We had that

feedback from our membership. We went to government with that. Government has made some amendments. We are pleased that the government has recognised those concerns.

CHAIR—This is a transitional arrangement for two years. Isn't that going to fix the problem?

Mr Fargher—That is what we are saying. It has been a concern to us. We have raised it with government. We are glad that they have recognised those points. Obviously we will need to talk with government over the next period of time because the issue of fuel prices does not go away. The issue of fuel policy does not go away and the issue of cash flow won't go away after that two years, but in the interim those discussions need to be had.

Senator WATSON—I am interested in the statistics about the increase in fuel prices. Can I have that?

Mr Fargher—Absolutely.

Senator WATSON—Thanks.

CHAIR—Now Mr Fargher, let's get this straight. To state the obvious, this bill does not set the price of petrol. We note your concerns about that, but there is nothing this bill can do about that.

Mr Fargher—Indeed.

CHAIR—I note your point that the cash flow issue will not disappear as a result of the two-year transitioning arrangements, but the two-year transitioning arrangements will go some way to addressing the concerns by giving your constituents the opportunity to arrange their affairs so as to deal with it over the two-year period.

Mr Fargher—Yes, that's correct.

CHAIR—Subject to that, am I right in understanding that the NFF supports the bill?

Mr Fargher—Yes, that's correct.

Senator STEPHENS—It seems to me that your satisfaction with the transitional arrangements announced by the minister does not cover the many issues that you raised in your submission. Were there other issues that you think could have given greater effect to the bill that are not included in the bill and the transition arrangements? You said in your submission to the white paper that your continuing discussions with Treasury and with the ATO have been, in many respects, disregarded. Were there other issues in that white paper that would have improved the bill?

Mr Fargher—There are other issues in regard to fuel policy that we will continue to advocate and fight on. There is absolutely no doubt about that. As an example, something that we raised in our submission that we will continue to negotiate with government on is the acceleration of the fuel reforms of the energy white paper itself. We advocated strongly for that. The government, at this time, has not chosen to accelerate them. We will continue to fight for those because farms are hurting from fuel prices now. But the main issue that our members have raised in regard to this bill, particularly recently because of the fuel price, is the cash flow issue. We advocated to government and there have been some issues resolved because of that. Are we still concerned about our biofuels policy? Yes. Are we still concerned

about accelerating the reforms? Yes. Will we continue to advocate on those issues? Yes. But the main issue that we had raised by our membership related to the eGrant transition arrangements cash flow BAS. That is why we are pleased that the government has seen fit to recognise that concern with the announcement last week.

Senator MURRAY—Do you represent the NFF national body?

Mr Fargher—Yes, we do.

Senator MURRAY—Have you given any thought to the issue of recycled oils, and did you hear the evidence given on it earlier today?

Mr Fargher—No. I think it would be fair to say that we have not considered recycled oils.

Senator MURRAY—I note that you have said you support the bill, subject to the changes the government has made. However, evidence emerged today that the recycled oils industry are seriously threatened by this bill. As you know, they take vast quantities of used oil from farmers. They think they will no longer be able to do so because the bottom will fall out of their market. That means that your members—if they are correct in their evidence—will be left with used oils which they will then have to decide whether to store or to have incinerated and destroyed, which is a cost to your members and is detrimental to the environment. Unfortunately, we have a very short timeline on reporting on this bill, but if you—

CHAIR—But a very full inquiry, Senator Murray!

Senator MURRAY—It is a lovely inquiry, Mr Chair, and I congratulate you on your witness list. What I would like to request is if you, Mr Arkle and Mr Fargher, would talk to the secretariat afterwards and have them get you a transcript of that evidence. If, as a consequence of that evidence, you wish to rapidly make a further submission—within the next two days—on the used oils effect on your members, I would be much obliged.

Mr Fargher—Okay, Senator. Thank you.

Senator WEBBER—I have one quick question. Accepting your support for the government's announcement last Thursday—about which I must say that it is amazing what a decision to have a Senate inquiry does to inform government decision making—I take it your organisation and your members have decided to support that in the transitional arrangements. In deciding to support the bill without needing any other changes, have you looked at the impact of the evidence we have had about the importance of the biofuels industry in developing small regional economies and in buying produce from your members, particularly from WAFF members rather than NFF members, in small regional communities in Western Australia?

Mr Fargher—Yes. We are certainly very interested in the biofuels industry in this country and very supportive of it. Our focus at the moment, outside ethanol and the support that government might give to the ethanol industry, is on biodiesel and discussions with government about regulation around biodiesel—about licensing and testing arrangements—as distinct from the focus that was articulated by the previous witness who appeared before your committee. That has been our focus to date, and of course that is outside the scope of the bill, which is why we have not focused on it—except to say in our submission that, if there was anything that was to the detriment of the biodiesel industry, we would be concerned to look at

it. Given the evidence of the previous witness, there are obviously concerns that need to be looked at. But our focus has been on how biodiesel is regulated—can farmers on-farm, small biodiesel producers, make biodiesel and, if they can, can they get a licence to do so; and is the testing requirement the same for them as it is for the major players or is there some flexibility they can be given in that regard. Yes, we are interested, but it is outside the scope of the bill. That is why we did not come forward in a major way on that point.

Senator WEBBER—Can I suggest that you look at some of the earlier evidence that we took as well. There was some quite forceful evidence given to us that this legislation will actually cause a lot of that industry to disappear.

CHAIR—It may, anyway.

Senator ALLISON—Did you discover the answer to those things that you just mentioned that the NFF is interested in?

Mr Fargher—In regard to biofuels?

Senator ALLISON—You said what you were interested in was licence arrangements, standards testing and so on.

Mr Fargher—No, we are still working with the government on those.

Senator ALLISON—It is my understanding that small producers do indeed have to test, be licensed and pay for doing all that and that, in fact, for some time now small-scale producers have pretty much walked away from that prospect, including your farmers.

Mr Fargher—We are certainly still in dialogue with the government, and we have advocated on those issues. With regard to long-term policy, I must say that these issues around biofuels are coming up through our membership more often. To be frank, I think our membership is becoming much more focused on long-term energy and fuel use in this country. Therefore, I suspect that the pressure from our membership will be such that we will have to advocate even more strongly in future on those issues.

Senator ALLISON—I am surprised that the NFF did not play a role at the time that those changes were made, but I am glad to see that you are now.

Mr Fargher—Which changes, Senator?

Senator ALLISON—The changes which required small-scale producers to effectively jump through the same hoops as the big-scale producers.

CHAIR—Thank you, Mr Fargher and Mr Arkle.

[3.58 pm]

HARDWICK, Mr Ross, Executive Officer, Economics, Farm Business and Transport, Western Australian Farmers Federation

Evidence was taken via teleconference—

CHAIR—Welcome. We have received from your organisation submission No. 13. Do you want to make some preliminary observations before we go to questions?

Mr Hardwick—The only observation that I did not include in our very short but succinct submission is one that has probably been dealt with, and that is the issue of payment and tax offset phase-in. I understand that has now been muted from the point of view of the e-payments and will be carried on for another year or two until people get familiar with the BAS process again.

CHAIR—I think what you are referring to, Mr Hardwick, is the fact that on Thursday, 1 June, the Assistant Treasurer, Mr Dutton, announced a two-year transition period for fuel tax credit claimants. Is that what you have in mind?

Mr Hardwick—That is what I have in mind.

CHAIR—I take it that your organisation welcomes that announcement?

Mr Hardwick—We do.

CHAIR—Do you have anything further to add?

Mr Hardwick—Not really.

CHAIR—With the announcement of the two-year transition period, may we take it that your organisation supports the bill?

Mr Hardwick—We do support the bill, other than those two points that I made.

CHAIR—Thank you very much, Mr Hardwick. We will start with questions from Senator Andrew Murray, from Western Australia.

Senator MURRAY—I understand there is no rain again.

Mr Hardwick—No. We are pretty dry over here. We have made the suggestion to farmers, particularly the northern farmers, that they stop seeding and wait for rain.

Senator MURRAY—Yes. I was talking to a farmer yesterday who said he can hold off planting for a little while but not too much longer. I want to ask you a couple of short questions. Have you had the opportunity to look at the submissions on the website?

Mr Hardwick—No, I have not. I have, up to a point. One or two of them I have read, but the short answer is: no, I have not been through all the submissions.

Senator MURRAY—Although we have a very good witness list today, we have a short reporting period and you might need to come back to us very quickly with a supplementary submission if you feel you need to. I would like to ask you, if you would not mind, to have a look through the submissions put by the various biodiesel and biofuel witnesses.

Mr Hardwick—Yes.

Senator MURRAY—In particular there are some Western Australian people there, like Bioworks and others.

Mr Hardwick—I actually have seen their submission.

Senator MURRAY—Could you have a look through them and, if you have any supplementary remarks to make to the committee, send them by email to the secretary?

Mr Hardwick—I will do.

Senator MURRAY—Thank you. You may not be able to find it on the website, but I will ask the secretariat if they can get the *Hansard* record to you if it arrives in time. Some issues were raised with respect to recycled oils which worry me a great deal, because large numbers of farmers have their used oils picked up and taken away to be recycled. The recycled oils people told the committee that, if their expectations are correct, this industry is likely to fall into a slump following the passage of this bill because of the pricing changes that result. That could result in very considerable aggravation for farmers in terms of either having to store used oil or dispose of it, whereas at present it is picked up from them by these recyclers and their collectors. If you could have a look at that evidence and let us know your views as well, that would be very helpful.

Mr Hardwick—I will do. Without having seen any of the evidence today, I can say that we would have an issue from the point of view of whole-of-farm environmental management strategy and systems if those oils were not able to be effectively picked up and either reused or recycled.

Senator MURRAY—I think it is a very significant issue from the perspective of the Western Australian farming community, so I would appreciate you having a look at it.

Mr Hardwick—I will do.

Senator MURRAY—Thank you they much.

Senator WEBBER—My questions are along similar lines to those of Senator Murray. I guess it is the joys of both being from Western Australia. You mentioned that you had seen the submission or had some discussions with the people from Bioworks.

Mr Hardwick—That is correct.

Senator WEBBER—They gave us very strong evidence that their investment process in the biofuels industry will be curtailed if this legislation goes through because the two-year transition package announced by the government does not actually impact on their concerns. Can I get any comment from you, either on notice or now, about what impact your members think that will have on them in terms of some of their product being consumed and the economic development of those small regional communities?

Mr Hardwick—I will add further to this through a written supplementary submission but, in short, given that the offset of any grant effectively negates the rebate that a farmer would get, we see that as counterproductive from the point of view of facilitating the siting of processing plants. The ones that we have seen at this stage—and you have probably been made well aware of them—are totally self-managed plants from Sweden that are computer controlled and can produce anywhere up to 10 million litres of biofuel. If they are not able to

be sited in a country area close to a feedstock source, we think that getting anywhere near self-sufficiency in biodiesel and/or ethanol as a strategic plan is not going to happen.

Senator WEBBER—Thank you for that. I welcome any additional comments you have.

CHAIR—Thanks very much, Mr Hardwick. The committee will take a break now. There is some confusion about whether the Royal Automobile Club of Queensland is meant to be here or is going to give evidence over the telephone. We will suspend proceedings to see what arrangements can be made about them and, if they do not appear, we will go to Treasury.

Proceedings suspended from 4.06 pm to 4.34 pm

FITES, Mr Gary, General Manager, External Relations, Royal Automobile Club of Queensland

WILLETT, Mr Ken, Executive Manager, Economic and Public Policy, Royal Automobile Club of Queensland

Evidence was taken via teleconference—

CHAIR—The proceedings are resumed. I understand we have on the telephone a spokesman for the Royal Automobile Club of Queensland. Is that right?

Mr Fites—That is correct. This is Gary Fites. I am General Manager, External Relations for the RACQ, and I am joined this afternoon by my colleague Ken Willett, our executive manager for economic and public policy.

CHAIR—Thank you, Mr Fites and Mr Willett. I do not understand any element of your submission to be confidential, but I should apprise you of the fact that these proceedings are public proceedings and there are other people, including journalists, in the hearing room who are listening. If there is anything you want to keep confidential, you should announce that before saying it.

Mr Fites—No, there is nothing we can envisage.

CHAIR—Thank you for making yourselves available. I am sorry, I think there might have been some confusion as to whether this was to be a teleconference or you were appearing personally. Anyway, now we have you. Would you like to speak to your submission or make any opening remarks before I invite my colleagues to direct questions to you?

Mr Fites—Yes, if I may.

Mr Fites—Thank you again for the opportunity to speak further to the brief submission that we made to your inquiry regarding the Fuel Tax (Consequential and Transitional Provisions) Bill 2006. By way of background, the RACQ represents directly more than one million Queensland motorists. As you may appreciate, that represents about a quarter of the state's population here in Queensland.

As far as advocacy is concerned, the RACQ's charter is to promote the legitimate and reasonable interests of our members as motorists. In terms of the thrust and direction of those advocacy efforts, they are broadly determined by, firstly, the policy set by the RACQ board, and that board is regionally representative of members across the state. They are determined, secondly, by research and analysis of issues of importance to motorists, and that is very much within Mr Willett's brief. Thirdly, we look at direct polling of representative samples of our membership to ascertain their views on issues such as this. Finally, we look at direct feedback from members in person or by phone, email or letter on motoring matters of concern to them.

When it comes to issues that do concern RACQ members, I can say without equivocation that there is no doubt that the price of fuel is most consistently top of their minds, even more so with the sharp rises in fuel pump prices that we have seen over the past year or so. That is why the RACQ has focused its submission on that part of the proposed legislation before the committee which we believe will impact negatively on the average private motorist not only

here in Queensland but throughout Australia. We are referring specifically to the proposed abolition of the Fuel Sales Grants Scheme covered under clause 3 in schedule 1 of the legislation which, as I say, in the RACQ's opinion, will see fuel prices across most of Queensland and indeed across most of Australia increase by between 1.1c and 3.3c a litre when GST is taken into account.

In Queensland that abolition will be felt even more because of the fact that around half the population in our decentralised state live and work outside the urbanised south-east corner of the state—that is, in regions inclusive of major provincial cities such as Toowoomba, Townsville and the combined cities of the Sunshine Coast where the grants scheme currently applies.

The RACQ is not in a position to state definitively whether or not the grant has been captured by the petroleum industry, as has been claimed, rather than having been passed on to motorists. However, our ongoing monitoring of pump prices in key centres around Queensland since the advent of both the GST and the Fuel Sales Grants Scheme in 2000 shows that, for the better part of the period post the year 2000, the differential between Brisbane and regional prices has in fact contracted.

In terms of the future direction of petrol and diesel prices, we do not believe it is particularly relevant whether some party in the supply chain has captured all or part of the applicable grant in any particular region in which it applies. To the extent that the grant may have been captured, it indicates that some relevant party in the supply chain has the market power to do so. In that case we would contend that they have the market power to defend that margin if the fuel sales grant is withdrawn and that would inevitably mean higher fuel prices for those people in regional Queensland and other parts of regional Australia.

If we take a scenario where the grants have in fact been passed on to motorists, parties in the supply chain there would be facing a reduction in an already smaller margin and in that case the imperative to protect those margins would be, we contend, even greater than if the market power was possessed. Again, we say that the inevitable result will be higher fuel prices if and when the grants scheme is withdrawn.

The federal government has consistently said there is nothing it can do about rising fuel prices. We have heard this in public statements from various ministers and the Prime Minister over the past year. To sum up this initial statement, the RACQ says that there is something the federal government can do to stop prices in regional Australia rising even further, and that is simply to retain the Fuel Sales Grants Scheme. That is basically an introduction to our case. Thank you.

CHAIR—Thank you. Have you done any economic modelling or obtained any expert advice from an economic consultant to support the claim that the effect of this legislation would be to increase the price of fuel?

Mr Fites—I will ask Mr Willett, who has considerable economic credentials himself, to answer that. That is where the analysis has been done.

CHAIR—Mr Willett, you are the economic analyst for RACQ, are you?

Mr Willett—Yes.

CHAIR—You have undertaken some study as to what you say would be the effects of the bill.

Mr Willett—It is basically intuitive analysis. We have not undertaken any modelling.

CHAIR—What does ‘intuitive analysis’ mean?

Mr Willett—Basically, it means thinking through the way in which the markets work. In this particular case we have looked at scenarios which involve possession of market power by various parties in the supply chain. We also looked at scenarios in which they do not possess market power. Our conclusion is that the effect would be basically the same: in either case we would see the abolition of the Fuel Sales Grants Scheme being passed on via higher retail prices.

CHAIR—The government’s view, supported by Treasury, is that the legislation is not going to have that consequence. We have witnesses from Treasury who are yet to give evidence to this hearing but they are listening to what you say. We will ask them the same question. It is striking that you are the first witnesses to have given evidence today to suggest that that will be a consequence of the bill when all the offsets and other provisions are taken into account. Are you sure you have not just looked at the repeal of the Fuel Sales Grants Scheme in isolation from all the other provisions of the bill?

Mr Willett—We have looked at the Fuel Sales Grants Scheme in isolation. What other provisions of the bill did you have in mind that provide an offsetting effect to the abolition of the Fuel Sales Grants Scheme?

CHAIR—The provisions concerning the levying of excise and the recoupment of the excise levied through the BAS scheme. And there are various others as well, but we will let Treasury elaborate on them.

Mr Willett—That relates to business use only, for a start, and I am not sure how on earth even that, in relation to business use, is going to hold down retail prices in the face of an abolition of the Fuel Sales Grants Scheme. The Fuel Sales Grants Scheme is applied at the retail level, remember, and it is inevitable that prices will rise because the parties in the supply chain will seek to protect their margins. If they have substantial market power they will have the market power to protect those margins. So if you argue—

CHAIR—That is assuming they do have substantial market power.

Mr Willett—It does not matter. If they had the market power to absorb the proceeds of the Fuel Sales Grants Scheme into their margins, as some members of the government have claimed, they would have the market power to protect those margins in the event that the fuel sales grant is abolished. We think there is prima facie evidence of the Fuel Sales Grants Scheme being passed on, at least partially. In that case we would believe that it will also be passed on, simply because there will be a stronger imperative for parties in the supply chain to protect their lower margin levels at that particular stage. If there is somebody else who has some evidence that prices will not rise, we would like to hear it. We have seen no-one present any significant evidence to indicate that prices will not rise. We have heard assertions only.

CHAIR—Indeed. But you are the only witness who makes that claim.

Mr Willett—It does not mean that—

CHAIR—We will see what Treasury has to say about that when we give them a go later on in the hearing. Can I invite you to comment on one other point? You criticise the government for not doing enough to keep petrol prices down. You do not seem, with respect, to have considered the effect of the government's decision of May 2001 to abandon the indexation of excise, the effect of which is a reduction, in effect, over time, of the price of petrol by 16c a litre. If the decision to forgo the indexation of excise had not been taken in 2001, the excise per litre in today's prices would not be 38c a litre; it would be 54c a litre. Have you not considered that?

Mr Willett—Of course we have, and the RACQ has acknowledged on numerous occasions that the abolition of the indexation has in fact meant lower excise and therefore lower petrol prices than would otherwise have been the case.

CHAIR—And the point I am at pains to make to you is that it is a continuing effect, so that, with the passing of every year, the proportion of excise drawn from the sale of each litre of petrol goes down.

Mr Fites—As Ken said, we certainly agree with that. Here is something more that the government can do to provide some relief from the high petrol prices which we have seen over the past year. Indeed, the proposal to divert the funds from this grant to roads spending in regional and outer suburban areas is a deal which we do not believe is satisfactory at all to motorists, in that the \$270 million a year that will be saved and diverted to roads funding will be something from which, we would contend, the average motorist in Queensland, or anywhere else in Australia, is going to see little benefit.

Senator WATSON—I think I agree with his rationale, in that people who have market power would have the strength to pass that on.

CHAIR—It was claimed, that, whether or not there is market power, in either scenario, the effect of the abolition of the Fuel Sales Grants Scheme would be to put upward pressure on prices. That was your evidence, wasn't it, Mr Willett? Is that what you say?

Mr Willett—Yes, it is a similar thing in that respect.

CHAIR—So are you not saying that this consequence that you predict is a function of the exercise of market power alone?

Mr Willett—No, we do not believe it is.

CHAIR—That is what I thought you said.

Mr Willett—Either way—regardless of whether the Fuel Sales Grants Scheme grants have been absorbed into the margins or not—we would argue that petrol prices will rise following the abolition of the scheme. I guess the proof of the pudding will be in the eating, won't it?

CHAIR—Yes, indeed. Thank you very much, indeed, Mr Willett and Mr Fites. You are excused. If you want to follow the evidence of Treasury, I think this is being broadcast on the parliamentary website. Anyway, you can inspect the *Hansard*. Thank you for your appearance.

Mr Fites—Thank you very much.

Mr Willett—Thank you.

CHAIR—At this stage we were going to go to Treasury, and we were going to take the evidence of the Australian Chamber of Commerce and Industry after Treasury, not because that is a good thing to do—usually it is best to have the government witnesses last—but because of the availability or otherwise of the ACCI witnesses. But I understand that we could, in view of the time, have the ACCI witnesses now. All right. We will have the ACCI witnesses now.

[4.51 pm]

GNIEL, Mr Peter, Director, Trade and Economic Policy, Plastics and Chemicals Industries Association

POTTER, Mr Michael James, Director, Economics and Taxation, Australian Chamber of Commerce and Industry

CHAIR—Welcome, Mr Potter and Mr Gniel. May I take it, Mr Gniel, that you have come along to support the ACCI's position?

Mr Gniel—That is correct.

CHAIR—Mr Potter, would you like to make an opening statement?

Mr Potter—Yes. Thank you for the opportunity to appear here today. The Fuel Tax Bill 2006 contains many very beneficial changes for business. I will not go into any detail about these; I will just mention that the expansion of the off-road and on-road grants scheme and the changes to claim systems will be beneficial for a lot of businesses. In my submission today I will be focusing upon those areas where we think there are concerns. As you would have heard from a couple of our members already, ACCORD and the Australian Paint Manufacturers Federation, they have some concerns over cash flow and compliance costs with the changes to excise treatment for fuel used in manufacturing activities. I am basically appearing here to underline and reiterate their concerns.

First of all, on cash flow costs, the fact that these businesses will have to buy fuel for 38c per litre more and claim it back later will obviously have cash flow costs. Our members have given estimates of the exact dollar cost that there will be for their industry. Secondly, there are compliance costs. Those members have particular concerns that the imposition of the excise and claiming it back later will increase compliance costs, compared to the current situation.

I might mention quickly some arguments that are used for the changes—first of all, that cash flow costs on these particular businesses will be offset by cash flow benefits upstream. Basically, this is because businesses upstream, like the paint manufacturers, currently have to sell fuel without excise. They will sell it with excise, and so there will be a cash flow benefit to those businesses, which it is arguable will be passed on. We think that there is a limited argument that that will occur. The same thing goes for compliance costs. Businesses upstream selling fuel without excise have higher compliance costs under the current arrangements. Under the new arrangements, we think it is unlikely that the reduction in compliance costs for the upstream businesses will be offset by the increase in compliance costs by the businesses downstream. In other words, we think that the net compliance costs in the economy will increase. The last point is tax evasion. You could argue that the changes will reduce tax evasion, but we have not seen any particular evidence that there is a lot of evasion and that this reduction in evasion will offset the costs of the measure. Mr Gniel, do you want to add anything?

Mr Gniel—Not at this point, other than to say that, as stated in our submission, PACIA's principal concern is the cash flow implications. We support the government's initiative to

simplify the fuel tax system but, as I understand it, there has been a long and arduous debate about cash flow today.

CHAIR—Yes, indeed. May we take it that, with the reservations that you have expressed, overall your position is to support the bill?

Mr Potter—Definitely. The bill has many good elements but, as with the nature of these inquiries, we are not inquiring into those things that are good.

CHAIR—We only hear the bad news at these hearings.

Mr Potter—Indeed, absolutely.

CHAIR—The fact that you so often deliver the bad news but today have had very little bad news to deliver gives us much encouragement.

Mr Potter—Yes. I might mention one other point. In fact, we do have a very wide membership. The New South Wales Farmers Federation is one of our members and you would have heard from the NFF today.

CHAIR—We have heard how happy the NFF are, yes.

Mr Potter—So we would be broadly supportive of what they are saying too.

CHAIR—Indeed, you would. I dare say that your happiness with the bill was made even more delirious by the announcement last Thursday by the Assistant Treasurer, Mr Dutton, of the two-year transition period.

Mr Potter—Overall, it has made the bill better, but still I consider that it only addresses a small proportion of the concerns of the manufacturing users of fuel. They will still have to buy fuel with excise included in the price and they will still have to claim it back. That means that it will have a smaller cash flow cost and it will have a smaller compliance cost, but there will still be a net increase in both those numbers. In particular, from the press release, it appears as though the claiming mechanism will be a written claim form, not the e-grant system that operates at the moment, which would have had lower compliance costs. So we recommend a continuation of the e-grant scheme, at least for the two-year transitional period, because that will have lower compliance costs than a system where you buy the fuel and then have to provide a claim form in writing.

CHAIR—We will ask Treasury whether that could be done administratively.

Mr Potter—Indeed.

Senator STEPHENS—That last point certainly forms part of the New South Wales Farmers Federation submission; they certainly encourage the flexibility of having both the BAS arrangement and the e-grants. With the diversity of your membership, I am just thinking about the compliance regimes for BAS and the suggestion in one submission—I cannot remember now which one it was—about aligning the compliance regime in this bill with the BAS regime. Would you see that as having any merit?

Mr Potter—I am not sure what particular alignment you are talking about.

Senator STEPHENS—I mean in terms of the size of turnover of companies and the reporting requirements of one month, three months or six months.

Mr Potter—Under the proposals, you would be claiming fuel rebates or grants on your BAS based upon the formula that I think currently exists in the legislation for when you put in a one-month, three-month or yearly BAS. So it would link in with what exists currently. Treasury could confirm this later, but I would assume that, with the proposal, there is an alignment there.

Senator STEPHENS—I do not think other people think that is what is scheduled to happen.

Mr Potter—You might have to ask Treasury about this one.

Senator STEPHENS—Yes, we will.

Mr Potter—I will make the simple statement that, if there is not alignment, there should be. You can ask Treasury about whether the bill will have an alignment. I hope that addresses your question.

Senator STEPHENS—Thank you. Do you represent the printing industry?

Mr Potter—Yes, the Printing Industry Association is one of our members as well. I do not think it has made a submission to this inquiry, but it has said verbally that it supports this concern. Its members use many solvents, as you might imagine. I guess they are downstream from paint manufacturers, so they would share those concerns. If a cost is imposed on the paint industry, it will flow through to the printing industry. Would it be helpful if I talked about recommendations for solving these issues?

CHAIR—Yes.

Mr Potter—I apologise if you have not asked a question—

CHAIR—Not at all. We are always open to helpful suggestions, and I see the Treasury officials in the back of the room are leaning forward eagerly.

Mr Potter—Very good. We think that the best idea is that you do not change things but you maintain the existing exemption for manufacturing users of fuel. Obviously, that is our No. 1 solution, but if that is not possible then there are a range of other possibilities which could be looked at. One of them is, as I have already mentioned, having the e-grant system continuing, where you can buy the fuel and get a refund of the excise immediately or nearly immediately. That would reduce both the compliance and the cash flow costs. Another thing you could throw into that mix is a threshold—having an easier claim below a certain threshold and maybe having the current bill's approach for companies above a certain threshold. For example, you might say that below a certain threshold you can prospectively claim for the excise for the fuel which you are planning to use in the future. That might be another approach.

Mr Gniel—Our submission raised very similar suggestions, with the view that it is for government to find the appropriate way that deals with these concerns.

Mr Potter—Indeed.

Senator STEPHENS—Mr Potter, your submission also recommends extending the e-grant system to businesses using fuel for non-combustion purposes.

Mr Potter—Yes. Manufacturing users of fuel do not need the e-grant at the moment because they can buy the fuel without excise. If you put the excise on, perhaps you should have easier claiming mechanisms for all businesses, including businesses that are manufacturing users of fuel.

Senator MURRAY—We have heard evidence today from a series of people who can be described as profoundly unhappy with the legislation. In no particular order, the groups are: recycled oils, paint manufacturers and solvent distributors, and what you broadly lumped together as biofuels, which represents a wide range of people. Apart from really practical issues, which is probably how you would view the paint people, that last group do not need to be in the excise system. They are very happy with how the system operates, and they are very small in number. They do not need to be dragged into it. The other two groups fall into a category of providing environmental and strategic benefits to Australia and of legitimately having been the targets of establishment cost subsidies—essentially, getting an industry going before you withdraw your subsidies and grants.

I was very interested in your analysis, because you listed a number of the major benefits from the bill. I thought to myself, ‘Many of those benefits could have been provided’—some people would agree with it and some people would not—‘without changing the existing rebate grants and subsidy system.’ For instance, you say in your submission:

The offroad grant will be extended to cover other offroad activities, including building, manufacturing and power generation ...

We do not need to do anything other than extend the existing system to get that benefit. Your next point is:

The onroad grant will be extended to metropolitan areas ...

We do not need to do anything other than extend the existing system. Your third point is:

The onroad grant will be extended to fuels other than diesel.

And I think the same applies.

Mr Potter—Yes.

Senator MURRAY—My concern with ACCI’s support for the bill holistically is that some of those things which attract you could be accommodated within the existing system. I am afraid that some of the unintended consequences—because I suspect they are unintended—do not justify the major overhaul that is under way. So, given that ACCI tend to be thoughtful about these things—we do not always agree, but I do agree you think about them—were you sufficiently consulted and were you made sufficiently aware of the downside, if you like, of this package—for instance, with the three groups I have outlined to you?

Mr Potter—First of all, I would say that there was quite an extensive consultation process on this bill, but there were a number of things which were what you might say specifically excluded from the consultations. These were particularly issues of policy. At a couple of points in the consultation—and Treasury might be able to speak to this—Treasury said that they were not able to have consultations on particular aspects of the bill. An example which I would use is the manufacturing users of fuel, but it could easily apply to those other areas. I am afraid I have not really looked into those particular other areas, such as—

Senator MURRAY—Recycled oils?

Mr Potter—recycled oils, yes. I have not really looked into those concerns. They might have some quite legitimate concerns there, but I am not aware of them and I did not specifically provide any input to Treasury on those.

Senator MURRAY—That is what worries me, because my impression of ACCI is that, if you are made aware of it, you will take a considered view of it.

Mr Potter—Indeed.

Senator MURRAY—With those things that Treasury could not discuss with you because they were policy issues, did you choose to take them up with the minister concerned?

Mr Potter—It is more like our members did. Peter, do you want to address that?

Mr Gniel—I must apologise: I have only been with the organisation for a brief period, so to comment in too much detail on the history would be a little remiss. However, my understanding is that we have certainly provided submissions to Minister Dutton and had various discussions with Treasury, ATO and other people in this building.

Mr Potter—I think you also provided submissions to Brough when he was Assistant Treasurer too.

Mr Gniel—That is correct, yes.

Senator MURRAY—My concern is that I have the impression that, like the farmers groups, who are also considered to think about a matter well when it is put before them, ACCI have almost been verbalised into supporting this bill. So you are being touted out there as being strongly supportive, but if somebody had said to you, ‘Actually, there’s a real issue for the following areas,’ you might have said you support it but you think those particular areas need to be addressed—which, frankly, is what you did with respect to the cash flow issue. You took that up properly.

We have had farmers groups appearing on the ether and they were not aware of the recycled oils issue. Neither was I before it was raised. They were not aware of the paints issue or sufficiently aware of the biofuels issue, which, if the evidence is accurate, will have a very negative effect on infant industries, on jobs, on import substitution, on farming viability and sustainability and on environmental considerations. And, as I said, all the benefits that you itemise could have been achieved without changing the system. So I am a bit concerned that government is going to wander out there and say, ‘Farmers groups and ACCI support it fully,’ and they have not spoken to you about policy and they have not told you about these other consequences that other people have been talking about.

Mr Potter—I guess I can blame our relevant members for not letting us know too. Not you, Peter.

Senator MURRAY—That happens, but you can see the danger. We will end up in the Senate chamber in two weeks time trying to stand firm against the negative side to this legislation, which you might agree with, and the government is going to stand there and say, ‘But ACCI supports it all and the farmers groups support it all.’ And I am not at all sure that they do support it all. They certainly support a significant slice of it.

CHAIR—But against that, if I may, Senator Murray, to put the position into the proper context, what that also demonstrates is that the objection of certain groups, such as the paint manufacturing industry or the oil recycling industry, for example, represents an almost infinitesimally small proportion of the economy that will be affected by the bill. What you represent because you are a peak body is the view across industry. Allowing for the fact that there might be certain industries that have legitimate concerns about the bill, the tininess of the sector of users overall that those industries represent against the overall view of industry which you represent does produce a conclusion of overwhelming net benefit in this legislation, doesn't it? The question for us is whether we should be recommending the excision from the effects of the bill of those relatively minor players.

Senator MURRAY—You are being verballed: he is telling you that you do not care about the little guys.

CHAIR—No more so than you, Senator Murray.

Mr Potter—I am being verballed by all, am I?

CHAIR—One can identify those industry participants who have legitimate concerns as to the effect, perhaps unintended, on them of the bill and can address their concern and lose sight of the big picture. The big picture, as I gather from your submission, is that from the overall point of view of industry this is a very welcome reform. Do you want to comment on that?

Mr Potter—I could make a number of points. First of all, we do not see that this as a black-and-white bill, that you have to accept it 100 per cent or that you accept it zero.

CHAIR—Quite. And as I said that raises the exemption issue for certain sectors that might genuinely find themselves in an anomalous position.

Mr Potter—I would also mention one other thing, going back to something that Senator Murray was talking about. You could change the existing system. My understanding is that the bill does make some administrative and other improvements that link in the fuel tax system better with the other systems that are in place for tax administration and compliance. You might want to ask Treasury about that in more detail. There are benefits in putting in place quite a substantial structure, and you might want to ask Treasury about that.

Going to the question of costs to smaller groups versus benefits to the larger groups, I always consider that the government and parliament should not just net out the costs and benefits of a particular bill and say, 'Well, overall, this is going to be of benefit to people,' and then just ignore the people who will lose. I think it is very important to look at the people who will lose.

CHAIR—Mr Potter, I think that is a very fair thing to say. But in this case the message that certainly came through to me from certain of the witnesses earlier in the day is that they do not challenge the policy merits of the bill. What they seem to be saying is, 'Bringing us into the system has an anomalous operation and, therefore, we are a proper case to be exempted from its operation.'

Senator MURRAY—Chair, I do have the call so I will continue.

CHAIR—Do you want to respond to that, first, Mr Potter, and then we will go back to Senator Murray?

Mr Potter—I do not think I have anything to add, Chair.

Senator MURRAY—The danger is that the government might say, ‘Never mind all that,’ and then just shove it through because they have the numbers. That is why I am concerned that you have not had the opportunity to have a look at the hard cases that I think should be addressed. You might be able to make suggestions, given your leading status in the business world, and the government might listen to you. My request to you—and we are on a short fuse with this inquiry; we have to report soon, so you would need to come back within a couple of days—is that you or some of your officers have a look at the submissions. I will ask the secretariat to provide you with the hearing evidence of the oil recyclers.

CHAIR—Senator Murray, if it helps, I have just asked the secretary about the availability of the *Hansard*, and I am told that it is likely that the *Hansard* for this morning will be available by early afternoon tomorrow.

Senator MURRAY—That is wonderful; thank you very much. She says she does not think so.

CHAIR—Perhaps that is not right, but anyway we will try to get the *Hansard* for the manufacturing users and the oil recyclers available as soon as we can.

Senator MURRAY—The secretariat has a hard copy of the non-confidential submissions there; it is also on the website. Could you look in particular at those three sectors and see whether there are any recommendations or suggestions you can make to the committee with respect to giving them relief? As far as I am concerned, in some ways they should not be caught up in what is essentially a modernisation, rationalisation and simplification of an excise and compliance system.

Mr Potter—We will of course take that on notice. I cannot guarantee that we will be able to provide you with much, because our policy development processes take longer than a couple of days.

CHAIR—That is because you are a consultative peak body.

Mr Potter—Indeed.

Senator MURRAY—Except you may be able to make some valid observations in a short form, which would assist us.

Senator WEBBER—Picking up from some of what Senator Murray had to say, I am also interested—either on notice or now—in your views. There are industry bodies, and paint is one but I am sure you have other members, that will be caught up in this regime that have never been caught up in before. The government brought out its package last Thursday, and as I have said before it is amazing what a Senate inquiry can do to inform government policy-making, so I think it is a very good thing that we are all here today. But my concern is that it has put together what it describes as a two-year transitional arrangement, and that in two years time we could very well find ourselves in the same position as we are in now. Is two years long enough for these industries that have never been caught up in this regime before to make the necessary cash flow adjustments and deal with being caught up?

Mr Potter—I am not convinced that two years is going to make everything fine. With the inclusion of the two-year transitional period, these businesses will still have to pay for fuel with excise; they will have to pay 38c a litre more for fuel and they will have to claim it back through a separate process. So both their cash flow and compliance costs will go up, but not by as much as they will at the end of the two-year period. So it is better than nothing, but I do not think is a vast improvement.

Senator WEBBER—Are there other suggested improvements that you can recommend?

Mr Potter—I have already answered that, I think. I do not know that I have any other ideas beyond those that I have provided earlier. Peter, do you want to add anything?

Mr Gniel—No, I think you have covered it quite effectively.

Mr Potter—Actually, there might be something. You have some numbers of your members who would actually be affected by this change.

Mr Gniel—Do I?

Mr Potter—Do you?

Mr Gniel—No; some of the subsets of our association you heard from this morning provided some pretty fair numbers. Obviously, plastics and chemicals is a pretty broad church—not quite as broad as ACCI, but fairly broad. The one observation I would make is that there would be a large number of our particularly smaller members that would not even be aware that these things are going on or have thought through the implications. There has been some difficulty for us in obtaining that data and engaging members. The bigger guys, whom you might expect have a capacity to deal with this more readily, have been able to lend some assistance in broad terms. It has been quite difficult to engage the ones we are particularly interested in, where the real impacts will be.

Senator WEBBER—One of the other cases that has been put to me, in addition to the industries that were here this morning, is industries like owner-operated prawn trawlers. At the moment, because of the way the regime is, the person that sells them the fuel gets the excise, they eventually pay their fuel bill and then they are away for months at a time. They are now going to have to pay the whole lot upfront and therefore borrow money to do so. They will be away for three or four months with their catch so they will be paying interest on the money they have borrowed and they are not going to get it back until they have done their BAS compliance, which you do not do from the middle of the ocean.

CHAIR—We did not hear any such evidence. Are you giving that evidence now, Senator Webber, on behalf of the prawn people?

Senator WEBBER—You could go and talk to WAFIC. They are concerned about the impact it will have on their cash flow and the additional cost in terms of having to borrow the money.

Mr Potter—I would not be surprised if there are impacts on the seafood industry but I am not in a position to comment.

CHAIR—Thank you, Mr Potter and Mr Gniel. You have been very helpful. You may take up Senator Murray's suggestion but if you are not in a position to respond—I am not trying to undercut you, Senator Murray—because you do not have time to consult your members, please do not feel obliged to respond. If you feel you are able to respond, that would be helpful.

[5.22 pm]

COLMER, Mr Patrick, General Manager, Indirect Tax Division, Department of the Treasury

FREE, Mr Anthony John, Manager, Excise Unit, Indirect Tax Division, Department of the Treasury

HARMS, Mr Michael, Fuel Credits Unit, Indirect Tax Division, Department of the Treasury

CHAIR—Welcome. Unless anyone has any objections, I propose to proceed as follows. Firstly, I do not generally invite Public Service witnesses to make statements. They are here to respond to what others have said and it is for us to put issues to them. Secondly, on my count there are eight discrete topics—I am not saying that there may not be others—which have been addressed by witnesses. I propose to deal with them sequentially and share the call around among senators in dealing with each of them.

The eight topics that I have made a note of, not necessarily in order of importance, are: the question of whether the abolition of the Fuel Sales Grants Scheme will lead to an increase in the price of fuel; the question of the cash flow effects and the extent to which they are mitigated by Mr Dutton's announcement last Thursday; the question of whether the E-grant scheme may continue either during the transitional period or absolutely so as to reduce the compliance burden; the question of whether non-fuel hydrocarbon users, such as the paint people who say they are not caught by the existing scheme but will be caught by the new scheme, should be caught by the new scheme or whether there are grounds to create an exemption in their favour; the question of whether oil recyclers who say they are not caught by the existing scheme but would be caught by the proposed scheme should be the beneficiaries of an exemption in their favour; the question of whether, in relation to the biofuels industry, the effect of the operation of the scheme would be to nullify the benefits to that industry of the government's producer grant system, which was introduced in 2003 in consequence of a recommendation of this committee; the question of what has been in omnibus terms called the 'BP amendment', that is, whether the provisions in the consequential amendments bill, which, it is asserted, will favour BP, is an issue and whether that is properly a matter for us to address; and, finally, the question of what has been called the 'greenhouse challenge', which goes immediately to what the oil recyclers had to say, that is, whether the environmental externalities of this legislation will be such that perhaps an exemption should be created for that reason in relation to oil recyclers. Is that a fair summary of the topics?

Senator WEBBER—Yes.

CHAIR—Then let us start with the first one: prices. It is said, although I note only by RACQ, that the effect of the repeal of the Fuel Sales Grants Act will be to increase petrol prices. What do you say about that?

Mr Colmer—We have not done any modelling of the repeal of the Fuel Sales Grants Scheme. It was a policy decision of government—a decision made about where their spending

priorities were. The Fuel Sales Grants Scheme, as you know, came in in 2000. It provides, in the main, 1c or 2c a litre to petrol sellers. There is not any real evidence about what its actual impact has been on prices and in that light there was a policy decision that the money should be redeployed.

CHAIR—And, as I understand it, the policy decision was to spend it on rural roads.

Mr Colmer—Yes, that is right. That was announced two years ago—I am not sure of the exact date.

Senator MURRAY—Is it about \$200 million?

Mr Colmer—It is something of that order; I do not have the exact figure but it is in the order of \$200 million.

CHAIR—Do you dispute the RACQ claim that this will increase the price of fuel? Do you say that there is no evidence for that? What exactly do you say, Mr Colmer?

Mr Colmer—The only thing that I can say on that particular point is that the Fuel Sales Grants Scheme was examined initially by the ACCC some time ago and it was subsequently examined again by the fuel tax inquiry of 2001. They were not able to provide any evidence around what its real impact was. I think it is a program that has been around and the government has taken a decision to redeploy that money on to things where there can be some harder and firmer results.

CHAIR—Would it be fair to say that you are not persuaded that the effect of this aspect of the legislation would be to increase petrol prices?

Mr Colmer—I am saying that we do not know. In some cases it may have impacts that are different from in other cases. It depends entirely on what the people who have been receiving this money do and what they do with it. For the most part it is 1c a litre. I do not know what the impact of that will be on fuel prices. You can make some theoretical assumptions about what it might do but I do not think we know. That is the short answer.

CHAIR—Do other officers wish to comment?

Senator WATSON—You could not refute the economic rationale of the point that was raised by the motorists organisation that those people who have absorbed the price will be in just as strong a position to pass that on and therefore there would be an increase in the price. Those in the past who have not been in that strong monopoly position to retain the benefit themselves and instead have passed it on will certainly pass it on. Either way, according to the motoring group, that 1c, 2c or even 3c will get passed on in the form of higher prices. The economics of the argument seem fairly sound to me from the motoring group.

Mr Colmer—All I can say is that we do not know what the impact will be. It is likely to be variable. It is likely that different recipients of that money have used it for different purposes. It was always intended that it should be passed on—in fact, that was quite clear.

CHAIR—But it may not have been. There is some evidence that it was not.

Mr Colmer—The ACCC, from memory, was not able to find any evidence that it had not been passed on—I think that was the conclusion they came down with.

Senator ALLISON—Has any other department bothered to look? What about PM&C or industry?

Mr Colmer—You would have to ask them.

Senator ALLISON—You have not.

Mr Colmer—I have told you: we have not done any modelling of this.

Senator ALLISON—I know you have not done any but has any other government department?

Mr Colmer—There was a government policy decision to redeploy the resources—

Senator ALLISON—So no department did anything?

Mr Colmer—into other—

CHAIR—Hang on, Senator Allison. Let the man finish his answer.

Mr Colmer—uses. The government decided that the money would be better off spent on other things.

Senator ALLISON—Without any department doing any modelling.

Mr Colmer—It is a policy decision.

Senator ALLISON—So no department did any modelling.

Mr Colmer—I am unaware of any modelling.

Senator ALLISON—You would be aware if there was some, presumably.

Mr Colmer—Not necessarily but probably.

Senator ALLISON—Really.

Mr Colmer—I am unaware of any modelling. I cannot say definitively that nobody has any modelling but I am unaware of any.

Senator ALLISON—We are unaware of any as well.

CHAIR—So we are unaware of any modelling.

Senator MURRAY—On the same point as Senator Watson, I think the nub of his question was that you could have a different view or simply not know. I think you are an economist, Mr Colmer, by memory.

Mr Colmer—No, I am not an economist; I am a sociologist by academic training, if that is helpful.

Senator MURRAY—His question was that it is a legitimate economic case that they put, which is arguable, but it is legitimate. Since you are not an economist, you will not be able to agree.

Mr Colmer—You can make a theoretical argument about this and that is fine, but I am not sure what you want me to do. All I can say is that we have no modelling on it.

CHAIR—You do not have a view on it.

Mr Colmer—My view is irrelevant. This is a policy matter for government.

Senator MURRAY—The point made by the witness, Senator Watson and me is that that is legitimate economic theory that he posited. It may not result in that because there are alternative theories or you may simply not know because of all the tangibles and extraneous matters that might influence the outcome. I just wanted to confirm that, from an economic perspective, it was legitimate theory that they were positing—that is all.

Mr Colmer—I think, as you are probably well aware, there are theoretical perspectives on this and there are things that you can point to on the ground. If you want to point to things on the ground, you can point to major variations in fuel prices on a very short cycle, and trying to see the impact of these things is very difficult at the best of times.

CHAIR—To make this as clear as it can be: it is your understanding, isn't it Mr Colmer, that when the government announced as a matter of policy that it intended to repeal the fuel sales grants scheme, the money saved as a result of the discontinuation of that program is to be spent on rural roads—is that right?

Mr Colmer—That is right. It has been redeployed into the AusLink program. This decision was taken as part of the broader consideration of the whole energy white paper. At that time there was a process being run through PM&C. There was an energy committee of cabinet. The decision was taken in that context and the money is to be redeployed into the AusLink program.

CHAIR—Was this a consequence of a recommendation of the energy task force?

Mr Colmer—I am not sure of that off the top of my head. It was in the white paper. That is a government document.

CHAIR—You might check that and come back to us. I propose, then, to go on to the second topic I identified—that is, the cash flow effects on businesses of these changes and the extent to which those alleged cash flow effects can be satisfactorily ameliorated by the two-year transition period. Mr Colmer, you have heard all the evidence that has been given from various stakeholders in relation to that. What do you say about that?

Mr Colmer—We have been discussing the issue around cash flow with various industry bodies over a very long period of time. I must say that some of the claims seem a little overstated to us. We are aware, for example, that very few farmers use eGrant and very few farmers claim particularly frequently under the existing scheme. Some of the cases that are put up for the cash flow argument have been chosen to maximise the impact and they are not necessarily representative of the reality of the situation as far as we can see.

CHAIR—But isn't it the case that the way this is going to work is that people are going to have to pay the excise up front and then claim it back three months later, assuming they are quarterly BAS lodgers, as a business input on their BAS? They are basically the parameters of this, aren't they?

Mr Colmer—That is basically the way that the current system works as well. People pay the excise up front and then claim it back. There are some exceptions to that and they are on your list of people that you want to deal with, but by and large the majority of people at the moment pay the excise up front and then claim it back under a specific, separate process.

CHAIR—What is the delay under the existing system?

Mr Colmer—They can choose to claim it any time up to four years later, I think, and the data that we have show that many of them do claim it annually or less often.

Senator WATSON—For the great majority it would be less. The point is that it is more than cash flow; it is extra working capital. In these times of rising interest rates et cetera, working capital is a significant issue. It is really more than cash flow. It is one of the consequences of cash flow, but we must not underemphasise the importance of extra working capital.

Mr Colmer—The working capital and cash flow are important issues—there is no doubt about that—but the experience of the existing schemes show that lots of people do not claim at less than three-monthly intervals. That is the current experience.

CHAIR—When you say lots, though, are you able to give us some figures?

Mr Colmer—I have to confess that we were not expecting this to be a major issue and so we have not brought all the data, I do not believe.

CHAIR—Do you have data?

Mr Colmer—We have data on claiming patterns and trends, and I guess we had thought that with the announcement last week that would largely have been dealt with.

CHAIR—It may well have been.

Mr Colmer—We believe that it probably has. It remains to be seen what happens with the two-year transition period. We announced this two years ago with a clear understanding that it would give people time to take it on board and adjust. Two years down the track, it seems that that perhaps has not been taken up, so we will wait and see what the next two years show. But we have done extensive analysis on this. We just did not bring it with us.

CHAIR—I am sure that extensive analysis would produce an answer to the question, which I think is what is on Senator Watson's mind and my mind, at least, and perhaps on others—that is, what percentage of users of the system claim the payment back within less than three months?

Mr Colmer—I am sure we can get something on that. We may not be able to answer that exact question, but I think we can come pretty close to giving you an answer to that.

CHAIR—Thank you.

Senator WATSON—Can we also have the letter that was sent out to claimants saying that the system that was changed two years ago was going to be subject to further revision? As a claimant, I was not aware of that.

Mr Colmer—I missed that. But we can tell you that for 2005—which I assume is the calendar year 2005—80.56 per cent of clients claimed between one and four times. I would say that means 80.56 per cent of clients claimed less than every three months.

CHAIR—So the cash flow effect will presumably, at most, effect 19.44 per cent of clients.

Mr Colmer—That is right. I do not have those sorts of figures with me, but a significant number of the other group are likely to be monthly BAS lodgers, in any case, because the larger companies tend to claim more frequently and they are ones that are on a monthly—

CHAIR—Could we disaggregate that 19.44 per cent between the monthly BAS lodgers and the quarterly BAS lodgers?

Mr Colmer—We will have a look and see what we can do.

CHAIR—You see, it may well be that you are able, with all the research that is being done, to largely eliminate this as an issue. If you are that would be good.

Mr Colmer—I think the position we find ourselves in is that it will be something that we will need to monitor over the next two years and see, in fact, how many people take up the transitional option and how that actually pans out over the next two years.

CHAIR—Sure. Your evidence, as I understand it, is that under current patterns this is not an issue for 80.56 per cent of people and, of the 19.44 per cent left, it is not going to be an issue for monthly BAS users. The question I am asking you to take on notice is to disaggregate the 19.44 per cent of people between monthly BAS lodgers and others.

Mr Colmer—Yes.

Senator WATSON—There is another factor that we have to take into account: a person may have three big fuel drops a year; therefore, that person will only lodge three claims. That is not to say that they are saving up all their claims until a third of the year has gone.

Mr Colmer—No, it is not to say that. What we are dealing with here, just by way of history, is what used to be the Diesel Fuel Rebate Scheme, which went back to 1982.

Senator WATSON—That is right.

Mr Colmer—There is a substantial history here and it may well be that, as economic times change, people's claiming patterns change. But, for a long time, there has been a pattern where people do not claim this as frequently as some people would lead us to believe. It may well be that that pattern changes over time, but it seems to have not changed particularly dramatically. It also incorporates the Diesel and Alternative Fuels Grants Scheme, which came into effect in 2000—that is the on-road scheme. There are differences in claiming patterns between those two schemes. The bottom line is that most people do not claim overly frequently.

CHAIR—I think it is clear to you what we are looking for, and you have obviously collected data.

Mr Colmer—We will see what we can find.

CHAIR—Are there other questions on the cash flow issue?

Senator MURRAY—Unless you have the answer to this question now, I would ask you to provide the answer on notice. We heard evidence today that, in the biofuels sector, the cash flow and working capital issues are not alleviated, it is my understanding, by the minister's announcement. So my question on notice is for you to look at that evidence with respect to the cash flow and working capital and come back and tell us whether they have a particular problem that is not addressed by the minister's announcement. From memory, Chair, I think it was Mr Grundell who said it would cost his company \$800,000 a week.

Mr Colmer—If you are referring to Mr Grundell, you are referring to the oil recyclers rather than biofuels.

Senator MURRAY—Mr Grundell represents Transpacific Industries.

CHAIR—Yes, he is an oil recycler. Senator Murray, I think he said that there are 40,000 places from which—

Senator MURRAY—Yes, it was 40,000 that he collected from, but one of them said it was going to require \$800,000 a week. But let us not argue about it.

CHAIR—I do not think that is right.

Mr Colmer—I think Mr Free can probably give you more detail on this. The argument made was that the oil recycling industry was going to be adversely affected because of the change to the excise arrangements.

CHAIR—Let us not deal with that now; I want to deal with that as a discrete topic.

Senator MURRAY—I am sorry, Chair, I would like to stay with the cash and working capital area. Mr Free, I think you said you would undertake to look at the evidence of witnesses who spoke to us today from biofuels and oil and talk to us about whether the minister's announcement will assist them. Is that correct?

Mr Free—When we come to oil recycling, cash flow is part of the oil recycling issue and we can certainly cover that in evidence and provide advice.

Senator MURRAY—Can you do that today?

Mr Free—I can do that now, or if the chairman wishes to discuss oil recyclers in an integrated fashion we can do it at that time.

Senator MURRAY—It means we will be picking up this issue then, but I will not worry about that.

CHAIR—All right.

Mr Free—I would add one qualification. Those figures given by Mr Colmer relate to cash flow issues where fuel is used as fuel. For example, where farmers, miners or the like use diesel, there are slightly different cash flow issues in relation to non-fuel users.

CHAIR—Do you have those figures as well?

Mr Free—No, they are in a different system, but we can traverse those issues when the time comes.

CHAIR—Can you locate those figures and give them to us on notice?

Mr Free—We can cover the non-fuel users in general terms.

CHAIR—Sorry, but can you find those figures and supply them to us in a written answer?

Mr Free—I will be able to give you the number of people who hold the remission certifications that we talked about earlier and describe how that system works and the changes.

Senator MURRAY—Yes, that is what I was after.

CHAIR—As there are no further questions on cash flow, the third issue I identified, which may be very similar, is compliance cost or, more specifically, the concern raised by some

witnesses—I think it was the farmers—as to why the eGrant scheme cannot continue either through the transitional period or absolutely.

Mr Colmer—This is an issue which to us has been quite overstated. Again, though, we do not have the full data because we were not expecting to discuss this today. I can tell you that, first of all, there have been some incorrect statements made about eGrant.

CHAIR—Why don't you take the opportunity to correct them now?

Mr Colmer—I am just about to.

CHAIR—Good.

Mr Colmer—The first one that springs to mind was the statement made by Michael Potter from ACCI, who gave evidence just before us. He said that eGrant allows people to get their money immediately. That is incorrect. All it does is replace a paper form with an electronic form, with the payment made in the usual sort of cycle. I am not sure of the exact timing, but it is not immediate. It is within whatever is the standard ATO processing time. That is one of the common fallacies about eGrant that is bandied about.

Senator MURRAY—Does it have a faster turnaround?

Mr Colmer—Not necessarily.

CHAIR—Okay, you have corrected that. While we are on that, though, at a time when there seems to be a movement away from paper to electronic lodgment—certainly a witness has said this—am I right in thinking that the electronic lodgment system will be abandoned and substituted for a physical lodgment?

Mr Colmer—The eGrant system is being abandoned in favour of the BAS system, which already provides options for electronic lodgment.

CHAIR—Is that all it is?

Mr Colmer—I am not sure exactly what you are referring to, but one of the key underlying rationales behind this whole program was to mainstream some of these programs. The ATO has a series of options available for lodging BASs, which includes paper lodgment, electronic lodgment, lodgment by a tax agent and a whole series of things.

CHAIR—So those who say that the eGrant system should be continued are merely saying that the old system should be continued.

Mr Colmer—That is absolutely correct.

CHAIR—Your point is that the whole point of this scheme is to introduce a new system which comprehends electronic lodgment on the BAS statement.

Mr Colmer—Amongst other options, but certainly that will be available to people. The other common fallacy around eGrant is that large numbers of farmers will be affected.

CHAIR—How many will be affected?

Mr Colmer—Something in the order of 300 nationally have used eGrant.

CHAIR—You obviously have those figures.

Mr Colmer—We have a more precise figure.

CHAIR—Can that more precise figure be provided, please?

Mr Colmer—Certainly; but it is of that order.

CHAIR—Are there any other questions on this topic?

Senator MURRAY—Are there any major politicians in that 300!

CHAIR—Getting on to other issues, which I think are more around substance than administrative method, the evidence of people who were described generically as non-fuel hydrocarbon users or manufacturing users, including the paint people and the suppliers to the paint manufacturers, say, if I understand them correctly, that the existing scheme does not apply to them, the new scheme will and, by implication, that is an anomaly of the new scheme. I hope I have put that fairly. What do you say about that?

Senator WATSON—And the complexities of claiming the credit will be enormous and that no accounting system could accommodate.

CHAIR—Let us deal with that next in this bracket, but first let us hear an answer to my question. What do you say about that—that its application to non-fuel hydrocarbon users is new and anomalous?

Mr Free—I think that is a fair representation of what they have said, but it shows a misunderstanding of the current legislative requirements.

CHAIR—Explain to us why it is not an anomaly.

Mr Free—The first thing I should say is that I am very pleased that some of the witnesses have talked about ‘using fuel’ rather than ‘as fuel’ because they recognise that the products that we are talking about are indeed actual components of fuel. One obvious example is the chemical toluene. That is used in large quantities in the paints and solvents industry. It also happens to be a component of petrol and, indeed, adds to its octane rating. The difficulty with petrol—as senators who have been on this committee for some time may remember—is that toluene, if left outside of arrangements for fuel tax, can be used very readily to extend petrol.

CHAIR—So capturing these people is essentially an anti-avoidance measure, is it?

Mr Free—Toluene has been excisable for a very long time. In instances where toluene is effectively excise free, you have to be very careful about those arrangements to ensure that, where it is excise free because it will be used as a fuel, you have a compliance and administrative mechanism so that that occurs.

In the late 1990s a system was brought in whereby fuels had to have added to them a chemical marker in instances where the fuels were not paid at the full rate because they were for use other than as fuel. Members of the paint and chemical industries made representations to the government at the time that they did not wish to use products like toluene with a chemical marker in them because they were concerned that that would interfere with the efficacy of the products when they were using them in industries. You have excise regulations which allow for a refund or a remission of the excise duty when the product is used other than as fuel.

The way the system works in practice is that a company that wishes to use a product other than as fuel will approach the tax office for a document colloquially known as a ‘remission

certificate', which effectively says that the tax office does believe that that company has a use for a product other than as fuel. They can then take that document to a supplier—normally one of the major oil companies or one of the intermediaries such as Recochem; a representative from there gave evidence earlier today—and there are legal conditions written into the permissions of the supplier governing the supply. So the claim that somehow there is an exemption is not actually correct, but—

CHAIR—It might be artless or imprecise to describe it as an exemption, but nevertheless whatever word we use the existing system does enable people in the position of Recochem or the paint manufacturers to whom they supply to be free of the existing arrangements. But they say that no such exemption will be available to them under the new system.

Mr Free—No, because, under the new system, rather than a remission of the excise duty otherwise payable by the supplier there will be excise paid which will then be claimed on the business activity statement by the user.

CHAIR—Are you saying that, under the existing system, they do not have to pay the duty because they get a remission but, under the new system, they will and then they will get it back?

Mr Free—Yes.

CHAIR—Given that they are not a user of fuel for the purposes of energy but in effect as a chemical component, and given that the existing system acknowledges that and provides a remission system for them, why shouldn't they enjoy an exemption from the new system which would reflect the same policy that presumably underlies the existing remission system?

Mr Free—Essentially, you have hit the nail on the head by referring to the fact that they use fuel. Irrespective of what they use it for, whether they burn it or use it as a chemical, as a solvent or as an input into the manufacturing process—

CHAIR—It is still fuel.

Mr Free—They have taken a product that is fuel, that has fuel tax applied to it and that is in many cases an actual ingredient of fuel—in some cases, such as kerosene, it is directly fuel. So the opportunity has been taken to align them with the fuel tax credits system as is the case for all users of fuel.

CHAIR—I know that an opportunity has been taken, but they lose the benefit of a remission, which they get under the existing system. My question is: why should they not enjoy an equivalent benefit under the new system?

Mr Free—It depends what you mean by benefit. If the benefit is—

CHAIR—At the moment they do not have to pay up front if they have a remission, do they?

Mr Free—No, they do not have to pay up front.

CHAIR—But under this system they would have to pay up front and then claim it back on their BAS—correct?

Mr Free—That is correct. Their compliance obligation is effectively the initial application. Our understanding from tax office figures is that there are about 600 such remission

certificates and that the total amount of product covered by those remission certificates is in the region of 170 million litres, and I think Mr Hambrook in his evidence referred to the paint manufacturers using about 42 million litres. They do have to make an initial application—

CHAIR—The remission certificate?

Mr Free—and that is all the compliance burden they bear. Curiously, I note that these mechanisms were described as ‘simple’. Previously Mr Hambrook has described them as ‘complex’, ‘time-consuming’, ‘expensive to implement’ and—

CHAIR—Everyone complains about compliance—

Mr Free—he also said they were not foolproof.

Senator WATSON—That was to get the credit back.

CHAIR—The point is, Mr Free—and what you have just said only affirms it in my own mind—these people under the existing scheme have a particular compliance burden and under the new scheme they are going to have a different and more onerous compliance burden. That is right, isn’t it?

Mr Free—It depends what you mean by ‘more onerous’.

CHAIR—It means that they are going to have to pay upfront and claim back on their quarterly BAS—whereas at the moment they do not have to pay upfront once they get one of these remission certificates, which they only have to apply for once. That is right isn’t it?

Mr Free—I agree with you on the cash flow effect where they have a quarterly BAS. I do not necessarily agree where they have a monthly BAS.

CHAIR—The evidence was that most of them have quarterly BASs except for the big three and the paint industry, for example, and it is not just the paint industry that is affected. So as it seems to be an incidental consequence why have we in introducing this new fuel tax scheme changed the compliance obligations of a particular and relatively small sector of industry?

Mr Free—The government took the view when considering those fuel tax arrangements that they would move all fuel tax relief across to a credit system and that when these arrangements were implemented they were anomalous with the general processes for claiming, which is a movement to the BAS.

CHAIR—But they were anomalous, did you say?

Mr Free—Yes, these are arrangements that were set up at the time the chemical marking scheme came into place in 1998. You have mentioned that in separating out cash flow effects in terms of the administrative cost there is a one-off application per year for the person seeking approval for the remitted fuel. That is not the case of course with the manufacturer because the supplier of the fuel is bound by legal instruments governing their behaviour as an excise manufacturer and they are legally obligated to pay the excise which is remitted to them so they can pass on that effectively excise free fuel provided they meet the obligations of the permissions that are given to them. They include things such as keeping records of their supply to the people using remission certificates and keeping a copy of the remission certificates for five years. In an instance where a person with a remission certificate comes to

a supplier and says, 'I want remitted fuel,' the supplier is then in a position where, if they do not check the bona fides of that remission certificate and ensure that they meet the conditions that are in the permission, they are the ones legally responsible for paying the excise. So you are correct in that there are fairly low compliance costs for the parties that get the benefit of that remitted fuel but there are significantly higher compliance costs for the suppliers of the fuel, who obtain no benefit whatsoever other than a remission of duty to pass on to their customers.

CHAIR—Except that the suppliers of the fuel are going to be the big oil companies, aren't they?

Mr Free—In some cases they are. In some cases they are intermediaries.

CHAIR—Like Recochem? Recochem were here today to support essentially the same proposition that their customers were advocating.

Mr Free—Recochem is not—and let me use toluene because it is the common example used across the chemicals and paint industry—a manufacturer of toluene. As a branded affiliate of Shell, it will obtain its toluene from the Shell Co. The comment that we have made in our various discussion papers—and we have never tried to hide the fact that there will be cash flow adjustments—is that the cash flow effects for any individual business will vary considerably depending on the terms of trade they have with their fuel suppliers, how frequently and when in a BAS reporting cycle they purchase fuel, how frequently they lodge a BAS and whether they operate on a cash or accruals basis.

CHAIR—I am sure that is all true, Mr Free, but only the wearer knows where the shoe pinches. You have a particular industry saying: 'There is a compliance burden under the existing system. We would be prejudiced or our industry would be damaged if that compliance burden were changed in the way contemplated by this scheme.' You have said it yourself that the existing compliance arrangements for this industry sector are an anomaly—that is, from the tax department's point of view. But they say, 'It is specific provision for our industry and we want to keep it that way.' My question to you is: if an exemption were created so as to maintain the existing arrangements for that sector, would it be revenue neutral or would it involve a cost to the revenue?

Mr Free—The objective in both cases is that the fuel, whether it is used other than as a fuel or not, is effectively excise free, with the exception of any cash flow effects because of changes in the first year. It would ultimately be revenue neutral in the impact on the effective excise.

Mr Colmer—This whole process is part of a fairly major approach to trying, as I said earlier, to reorient some old tax systems and realign them with more modern ones. The Excise Act, as I am sure everybody around here knows, is originally a 1901 act; a lot of the arrangements in it are very old and antiquated. We took the view, and perhaps it was wrong, that as part of all of this we needed to streamline a lot of arrangements. I cannot remember exactly, but there is something like half a dozen pages, possibly more, of remissions, refunds and similar arrangements in the regulations in the Excise Act; it is a not insignificant compliance problem for excise manufacturers. We took the view that the better approach was to have the people who were receiving the benefit of the fuel tax credit, as it will be, bear the

compliance burden. We understand that there are cash flow implications. As I said earlier, we do not think they are significant in the long term. It is something like 0.6c a litre. We are bringing in an expanded system of fuel credits which is providing \$1.5 billion over the next four years. The benefits will be a lot—

CHAIR—You do not need to persuade me about that, but these people have come along and said, ‘This is going to have an anomalous effect on us.’ You answer them by saying, ‘In fact, you are the beneficiary of an anomalous exemption.’ Those are the parameters of the discussion. You then tell me that if we do not change the arrangements it is going to revenue neutral—no cost to the revenue—and they say, ‘Whether it is an anomaly or not, if you change the arrangement, it is going to send a lot of us out of business.’ I think, on a simple, utilitarian test, the merits are with them.

Mr Colmer—As I have said on numerous occasions today, we believe that those costs are overstated. The minister has now announced that they will have the benefit of a transitional arrangement. I would say—

CHAIR—Yes, but they are losing what you say is their anomalous special treatment. The transitional arrangements are not going to fix that up, from their point of view.

Mr Colmer—No, they probably will not. But whether or not that proves to be the issue that they currently think it is is something that we will find out over the next two years.

CHAIR—Colleagues, I am sorry for dominating the discussion.

Senator MURRAY—You did that exceptionally well.

CHAIR—Does anyone want to ask any questions on this issue?

Senator MURRAY—The only observation I would make, apart from the fact that you carried all our arguments, is that it seems to me, from the response of Treasury, they are looking for consistency, which, as I understand it, results in the removal of six-odd pages of regulations from the tax act and a changed system for suppliers. I do not know that all suppliers are worried about that. It seems to me that—

CHAIR—They have a lot to say to us, so it seems that they are.

Senator MURRAY—It seems to me from your utilitarian remark at the end about a cost-benefit basis that they have a good case for an exemption.

CHAIR—You do not need to respond to this if you do not want to, Mr Colmer, but it seems to me that if these people were in a position no different to that of anyone else then there would not be a lot of merit in their argument. But I am rather persuaded that, because they are a manufacturing user rather than a user of fuel in the ordinary sense of the word, they are in a genuinely special position and the desire—which I understand from a point of view of Weberian, bureaucratic rationality—to impose a uniform system on everyone should admit exemptions in special cases where there is a genuinely different and special case. I am rather persuaded that this is one. There it is. I said you did not have to respond, and you did not.

Mr Colmer—We will see how it pans out. We obviously took the contrary view when we were looking at it, but there you go.

CHAIR—You did. The next topic is the oil recyclers. They say the same thing as the non-fuel hydrocarbon users about cash flow. I do not think we need to traverse that again. But they also say that there will be an environmental externality. I will give the call to Senator Murray to pursue that. They also say they are being taxed twice. We will let Senator Murray deal with the environmental externality issue and Senator Watson deal with the ‘taxed twice’ assertion.

Senator MURRAY—Gentlemen, I am not sure if the full nature of the industry was explored with you in their discussions. There are 40,000 collection points: suppliers of this dirty oil for recycling, which includes many small suppliers like farms and so on. It seems to me that the present system works very effectively, from an environmental perspective, in sweeping up used oil that otherwise would have to be destroyed or stored—and may in fact be stored dangerously by a minority of irresponsible people. So we have a system which seems to work very well and is in the public interest to maintain and sustain.

It also seems to me that changing the existing system in a way which would make them less competitive does not have a good cost benefit rationale to it and does not go to the heart of what you are trying to achieve through your legislation. In other words, it is a minor area which we could attend to without damaging your overall intent. If we deal with just the environmental area, their evidence was that you implied in negotiation that you could not deal with environmental externalities, that your job as Treasury was to focus on the intent of your scheme and the costs of your scheme and how to deal with that. Our attitude has to be broader; therefore the question to you must be: do you accept that those externalities should be taken into account?

Mr Colmer—I think the case of the oil recyclers is a little different. The reason that it is different is that, prior to 2000, there were quite a large number of special remissions, concessions and all sorts of arrangements in the excise legislation to promote oil recycling. Most of those went back to the nineties. In 2000 the government established a specific oil recycling program, the Product Stewardship for Oil Program, which in part depends on—

Senator MURRAY—You might remember that was negotiated between the government and the Democrats.

Mr Colmer—Indeed it was.

Senator ALLISON—We do remember.

Mr Colmer—I am glad. I have in the past done significant work on that myself, but it is no longer part of my particular area. However, the aim of the product stewardship program was to provide a detailed, effective working framework to deal with oil recycling. As part of that, there were very overt statements made that we were going to unwind the existing excise concessions and replace them with the product stewardship arrangements. That was always part of it, and this is the end point of that process.

The issues raised by the oil recyclers today are ones that we actually think are nonexistent. I will get Mr Free to explain these to you in more detail, but the issues that they are complaining about are not ones that are going to specifically disadvantage them. They are more general ones around the use of burner fuel. You can complain about that again if you wish—it is all part of this related cash-flow compliance matter—but it has no specific impact on recycled oil over and above non-recycled oil. The policy, though, for oil recycling is part

of the environment portfolio, and that is run through that product stewardship program. We have been saying all along that it is inappropriate for us as a tax policy area to be involved in that area, and we have been withdrawing and that should not be of any surprise.

CHAIR—You cannot really comment. For that reason, I feel some sympathy for your position, Mr Colmer. I do not think you can really comment on the environmental policy consequences.

Mr Colmer—We would not try.

Senator MURRAY—Sorry, but can I continue with our interchange? As you know, Mr Colmer, throughout the revenue system it has been government policy—and, in many respects, still is government policy—to use different excise levels and tax regimes for social policy outcomes. It does not matter if it is in the welfare area or with low-alcohol beer or whatever. We have always regarded the tax side of it, the revenue side of it—and, by we, I mean the parliament, not just my political party—as being a key part of the incentives which allow for an efficient and effective oil recycling program. We do not see you as having some kind of policy purity and these issues being that of the environment department. I presume you did not mean that in your response, that you see the two as integrating.

Mr Colmer—I am really glad that you mentioned low-alcohol beer, because not only is that going to be discussed tomorrow or later tonight but it is also a perfect example of government policy development. As you would recall, the government made some significant changes to low-alcohol beer—

Senator MURRAY—And you did a wonderful job on that, let me tell you.

Mr Colmer—in order to replace existing spending programs on low-alcohol beer that were in place in the states. In the oil recycling arena the government took the other view: ‘Let’s pull away from these hidden excise concessions which are difficult to run and let’s put in place an overt spending program.’ That is what has been happening over the years, but the key thing that joins them all together is that the government have said, ‘Let’s have one unified, open system here.’ In one case, on the excise for beer, we brokered an arrangement with the states and removed a whole series of complicated, little bitty state-run schemes and replaced them with one national excise scheme.

Senator MURRAY—If you recall, my party strongly supported you in that effort.

Mr Colmer—Thank you. In oil recycling we have done exactly the same thing except that we have chosen to run it the opposite way and replace a range of complicated, hidden—in this case—excise arrangements with a spending program. But in each case what we have done is round up a series of small, complicated programs to try to replace them with one clear overt arrangement.

Mr Free—I want to give an example of one of those excise regulations that was in place prior to the product stewardship scheme that was not targeted very well and that legally allowed waste oil that was recycled and minimally treated to be mixed in with diesel. That occurred during the 1990s because of a fairly poorly targeted excise measure. Clearly, that is inconsistent with national fuel standards for diesel.

Senator MURRAY—But that was sorted in 2000, wasn’t it?

Mr Free—Yes, that was removed. I would like to talk briefly about where this bill does affect recycled product and that is that the principal activity of oil recyclers in Australia is selling their product, treated to various levels of cleaning it up, for what is loosely known as a burner fuel. One of the witnesses talked about some of their customers for that. They are businesses like cement operations and brick kilns—and I think drycleaners were mentioned. That fuel is used essentially for burning as a source of external heat. The fuel tax credits relevance to that is that fuel tax credits work with fuel tax, and all fuels, irrespective of whether they are recycled or whether they are from conventional sources, would be paying 38c per litre. Then, if someone uses those in their business, they are eligible for a 38c per litre fuel tax credit.

Senator WATSON—I understood it was 30 cents.

Mr Free—That is a slightly different matter. In general terms, where you use a conventional petroleum product, such as fuel oil, or where you use a recycled product, such as waste oil which has been recycled and cleaned up, the new system has exactly the same effect. Where you get relief from the excise, that will be obtained through a fuel tax credit from the person who uses it in their business.

There is an effect on recyclers because of fuel tax reform, and that is that one of the levels of assistance in the excise arrangements is that, while the conventional fuels currently pay 7.557c per litre excise, because of the excise tariff and some quite complicated provisions, where they come from recycled sources they do not pay anything. So that 200 million litres of burner fuel from recycled sources implicitly is getting \$15 million a year in tax assistance because they are not paying 7½c that their competition from conventional sources pay—

Senator MURRAY—But their point is that was excised when it was original new product and it should not be excised again.

Mr Free—That is a separate matter, which I will come to. And the government put in a budget measure that completely offsets that in the first year and phases down. So in terms of that 200 million litres that is being used as burner fuel for cement factories, brick kilns and the like, effectively in the first year of fuel tax reform they continue to get that 7½c advantage over conventional competition. They face exactly the same cash flow issues as the conventional competition does.

The issue you raise, where they do not pay the same tax or they say they have paid tax, relates to where product is diluted into sumps. It is not something that is covered by this bill. It relates to the excise tariff changes which are not in these bills, but if it is within the scope of the inquiry I am happy to talk about it.

CHAIR—I think you should, Mr Free. Basically, as I understand Senator Murray's point, there are broader social policy issues engaged here. And we have had evidence from a spokesman for the industry, whose evidence I think has to be taken at face value, that a large proportion of this industry would go out of business or cease to trade in particular smaller sectors of the market were these changes to be introduced. That would have the result that there would be a large quantity of oil not recycled or recovered but buried or otherwise disposed off, with consequent environmental hazards. That is the point, I think.

Mr Free—That point was made in terms of customers for this recycled oil at the moment facing a price that goes up by 38c because the users can then use it in their businesses and claim a fuel tax credit. I would make the point that exactly the same will be happening to the conventional products that are sold from non-recycled sources. So if the competition in those is heating oil or fuel oil or diesel, exactly the same applies: a 38c charge applies to the product that is used and it is reclaimable by fuel tax credit.

Senator MURRAY—But you miss the substitution point. If there is a substitution from used, recycled product to new product, that new product is imported and, once used, then becomes used product. You are just going to get an accumulating amount of used product because of the substitution effect and the creation of this product. It seems to me that it is not worth taking the risk and that, at least until the main system is settled down, we should have a period in which this particular area can be reassessed. I understand what you are saying, but I am also, like the chair, inclined to take at least at face value what the industry have told us. We are aware that the system since 2000 has been very effective. It has been a great success from the social and environmental perspective; maybe not from your tax and complexity perspective. I am just concerned we are taking unnecessary risks with the assumption you are outlining and that those risks have not been properly evaluated.

Mr Colmer—I think I should say that we have been working with the environment portfolio on this. They have not raised that as an issue. Frankly, the position put by the oil recyclers seems to be a bit of misunderstanding of what is actually going to happen. We have been trying to clarify that their claim that there is going to be a specific impact on them is not correct. It is going to be a more general impact. It is not going to be a specific impact on them as oil recyclers.

Senator MURRAY—Do you believe that there will be no slump, no effect, on their business whatsoever from these changes?

Mr Colmer—As I said, and as Mr Free pointed out earlier, there is a difference in the application of the excise and we have been discussing that with the environment portfolio. We have met with the oil recyclers on this on numerous occasions as well. Never saying never is always a useful position, but we do not believe that there is going to be an impact that cannot and will not be managed. What we are saying is that we believe that the product stewardship program is the appropriate way to deal with that and, as I say, we have been talking to the department of environment on those matters.

Senator WATSON—Quite strident statements were made by the witnesses today, particularly in the oil recycling area, that, quite simply, the increased cost by virtue of paying an excise of 38c and getting back 30c will be a cost imposition and the combined effect of these changes, in terms of who they sell their product to, will be such that they could well go out of business and the big users will just convert over to gas. To say, from your point of view, that there will be no impact just worries me. As politicians, we have to face the realities in our electorates of companies going out of business as a result of changes in policy, yet the advice from Treasury is: 'It remains to be seen whether that will really happen. There is some doubt about this because it can be managed.' The only people who will be managing it will be the liquidators.

Mr Colmer—I am not saying it remains to be seen; I am saying that we have been working with the environment portfolio. This is a program that has a different framework and we do not believe that there is a problem here.

Senator WATSON—Won't it be dumped on the farms, if they cannot get an outlet for it?

Mr Colmer—Why won't they get an outlet for it?

Senator WATSON—If the business for the recyclers is not there, where will the outlet be?

Mr Colmer—I do not believe that there is any reason why the recyclers are going to disappear.

Senator WATSON—I have already given you a case where a differential between what they can claim back and what they pay. That is one reason.

Mr Free—If they are reselling recycled product as a fuel for burning, they will pay 38c. Their customers will get 38c and, quite separately, as a result of the measure announced in the budget, the recyclers will get a benefit under the product stewardship oil scheme to reflect the fact that they currently get 7½c implied assistance and that will continue for one year at least.

Senator MURRAY—After the year, they will have no competitive advantage. What you are talking to us about is a transitional provision, whereas what we are talking to you about is maintaining a system which works.

Mr Free—I think you mentioned about imported lubricating oils—the activities that we are talking about currently are not re-refining that lubricant oil into lubricant oil again, it is simply cleaning it up and burning it. I know there is a strategy by the department of environment to actually encourage re-refining. While I would not be an expert on the levels of all the grants made under the Product Stewardship for Oil program, I know that for producing re-refined oil the benefit rate is 50c per litre. And, if you take lubricating oil and re-refine it to produce further lubricating oil, the excise does not apply in that case because you have gone back to lubricating oil and, should you set up to do so, you will be paid 50c a litre.

There are variable grant or product benefit rates that are paid for various activities. I know what the department of environment is moving towards—in the budget papers it has alluded to where oil recyclers adjust to new market conditions it was to take account of some of the excise changes, but also the government wishes to use that program to encourage recycling activities that are probably environmentally more beneficial than simply burning the oil.

CHAIR—You just want these incentives out of the tax system.

Mr Free—It is not just us who want it out of the tax system, Mr Chairman. The government has made decisions along these lines to take them out of the tax system because the Product Stewardship for Oil program is in place, and you can actively target those activities that are considered to be environmentally beneficial. The example I have just given is that, for re-refining of lubricants or waste oil back into lubricants that you can use again, the grant rate is 50c per litre. I think I heard the witness from Transpacific say they are actively working towards building a plant to do that, and that is certainly consistent with the government's environmental policy in relation to waste oil collection.

CHAIR—I understand that. Your position is the typical one and I am not criticising you for it. The typical position of the Taxation Office is that, to the greatest extent possible, you want simplicity and uniformity in the application of the tax system, and you do not like the system being used to incentivise certain outcomes in other areas beyond fiscal policy. That is understandable.

Mr Colmer—That is a government decision, Senator. The government set up the program with an expressed view that they needed one program for oil recycling.

CHAIR—What about the assertion that was made that this product is being taxed or excised twice?

Mr Free—Again it is not in this bill under inquiry but it is a result of changes to the excise tariff, the alcohol provisions of which are under inquiry also by this committee. During the 1990s there were provisions put in the excise tariff where diesel or petrol, which was taken to already have had excise paid on it and recovered, had an excise-free rate. The theory of that was that if you operate an engine then some of the fuel internally will leak into the sump. As practical example, if you take the oil out of a car or a truck the argument was that there was some fuel—diesel obviously in a diesel powered vehicle and petrol in a normal motor car—that had leaked into the sump. Conceptually that could occur but there are some difficulties with the argument because it is probably in very small quantities.

CHAIR—Just cutting to the chase, Mr Free, do you say that when the oil is recycled or reprocessed it is a new product and therefore should, for that simple reason, attract an excise charge?

Mr Colmer—I do not think we do say that, Senator. I think what the oil recycling industry argue is that they are able to extract already taxed diesel or petrol from sump oil.

CHAIR—Yes, but you argue the contrary.

Mr Colmer—No, not necessarily. I think what we say is that, if you can do that, then that is very interesting. As a basic theoretical position, I am not convinced that the fact that excise may or may not have been paid on that petrol or diesel before it found its way into the sump oil is of any relevance at all. We quite happily charge GST on second-hand goods and we quite happily charge GST on second-hand cars. That is taxing an already taxed product. I do not see that there is any absolute theoretical bar depending on whether it is new or old or whatever. It is a political argument.

CHAIR—If it is resold, it is resold.

Senator MURRAY—Excise is not a value added tax. I am not sure that is a good—

Mr Colmer—It does not really matter whether it is a value added tax or not. The argument that is made is: it is already taxed, so how can you tax it again? That does not bear any relationship to the particular type of tax that it is. It is a political argument that has been made in the past, but I do not know whether that has any fundamental merit. It is an argument you can make and it is an argument you can reject.

CHAIR—What you are saying—and in a different way the High Court looks at this every time it considers section 90 of the Constitution—is: that which attracts excise is the

transaction and, if there is a multiplicity of transactions in relation to the same good, nevertheless one looks at the transaction, not the essential nature of the good.

Mr Colmer—I am not even sure that I am saying that, and I am not sure that that is what the High Court would say. But I would have to bow to your better knowledge of constitutional law.

CHAIR—I am actually not sure what the High Court says these days, but that is one of the issues that is always confronted whenever section 90 of the Constitution is argued.

Mr Colmer—I think that the argument that I would make if I were going to make such an argument is that there is a product which is being sold which is some sort of fuel.

CHAIR—So you look at the transaction, not the thing which is the subject of the transaction?

Mr Colmer—If you wish, but I do not think that you can actually make any very tenuous link between some fuel that is sitting in a barrel and some fuel that was sitting in a barrel six, 10 years ago—who knows?—and say, ‘It was taxed then; it has been taxed already.’ I think that is an extremely tenuous link. But that is a theoretical argument. The position we find ourselves in is that the oil recyclers made that argument back in the late nineties and won the day at the time. So that is what we are dealing with now. It is all very jolly—we can talk about tax theory till the cows come home, but it might not help us in this particular circumstance.

Senator MURRAY—Don’t tell me you’re becoming cynical, Mr Colmer!

Mr Colmer—No, Senator.

Senator WATSON—Currently most of the product that the recyclers use comes under the definition of specified product or a similar name, for which the end user attracts a rebate of 30c. Mr Free earlier said that that rebate will no longer be 30c but will be 38c. Can you confirm that? The submissions that have come to me suggest that they will now be paying 38c and will attract a rebate not of 38c, as you say, but of only 30c, which is the specified oils category of rebate. Who is correct?

Mr Free—Both of us are correct. I was referring to the product that is sold as burner fuel. The product that you are referring to is actually claimed to be diesel recovered from sump oil. That, because of the provisions in the current excise tariff, has a zero rate, and yet, as you have just mentioned, users can claim 30c for using it.

Senator WATSON—So they are going to be 7c worse off per litre, aren’t they—they have to be—in this category that I am referring to, not the ones you are referring to?

Mr Colmer—There is actually a further twist to this particular tale—

Senator WATSON—The category of specified—

CHAIR—Hang on, Mr Colmer. Senator Watson, you keep developing that thought.

Senator WATSON—For this product called specified diesel, you say, ‘Yes, I’m right.’ So they will now pay 38c and get a rebate of approximately 30c, so there will be a 7c differential that the companies will have to pay, which will make them less economic. Is that not right?

Mr Colmer—I think you are referring to light fuel oil under the current arrangements.

Mr Harms—Is this under the Energy Grants (Credits) Scheme?

Senator WATSON—That is right.

Mr Harms—Certain off-road users of diesel and like products get a credit of the excise. In the case of specified diesel, which is also known as light fuel oil, instead of getting a 38c per litre credit, they only get a 30c per litre credit. So they pay an effective tax of 7.557c per litre, which is the burner fuel rate, rather than having an excise free product, which other users get.

Senator WATSON—They have to be worse off, haven't they?

Mr Harms—In future, they will get a credit of 38c per litre, because the government's intention is that burner fuels are free of excise under this reform. There will not be a separate rate for specified diesel in future; it will pay 38c in excise, the end user will get 38c in credit, so the end user will pay no effective tax.

Senator WATSON—Earlier, Mr Free said he was right and I was right.

Mr Colmer—I think we are all right on this one.

Senator WATSON—Somebody must be worse off.

Mr Colmer—This is a classic example of the complexities that we are trying to cut through, and I am afraid we are shaving some people's heads on the way past.

Senator WATSON—I just want to make sure that people are not worse off; that is all I want. I obviously have a little chink somewhere where people feel they are going to be worse off, but if you can assure me they will not get a rebate of 30c, I will be delighted.

Mr Colmer—The situation you are referring to now is a special situation under the current arrangements, which will disappear on 1 July. Under the current arrangements that you are talking about, people pay 38c excise and get a 30c rebate, with a few decimal points. After 1 July, they will pay 38c and get a 38c rebate, because the burner fuel rate, which is currently 7.557c, goes from an effective rate of zero.

CHAIR—Are you saying that, in effect, the witnesses from the oil recyclers only said what they said because they did not understand the way in which the scheme would operate?

Mr Colmer—As far as I could see, I think there was some misunderstanding.

CHAIR—If there is nothing more on this topic, the oil recyclers, then we are going to press on.

Senator WATSON—This is an important point.

CHAIR—Yes, it is. Is there any thing more to say about it? Do you have any more questions?

Senator MURRAY—Our difficulty is Treasury have one view and recyclers have another one.

CHAIR—Yes. I am not trying to attenuate the discussion, but are there any new questions, other than chewing the cud on this issue? All right, we will go to the next topic, which I thought was the one that exercised most of the controversy today in relation to biofuels. There are two quite separate issues. The first was the claim made by all of the biofuels witnesses that the effect of this scheme on them would be to nullify completely the benefit to the

industry of the Energy Grants (Cleaner Fuels) Scheme Bill 2003 and, more specifically, the offsetting of the excise payments by producer rebates. What do you say about all of that?

Mr Colmer—I think the best thing I can do about that is to read to you from the letter that Dr Humphreys tabled earlier today, which sets out the government's intention around the cleaner fuels scheme. This is a letter from Mr Mal Brough, the previous Assistant Treasurer, dated 15 June 2005. It is addressed to Dr L Humphreys, chief executive officer. I quote:

The cleaner fuels grant was not intended as a stimulus package for the biodiesel industry.

CHAIR—Well, it was. Mr Brough might have thought that, Mr Colmer, but I chaired the inquiry of this committee, and Senator Webber, Senator Murray, Senator Stephens and Senator Watson—everybody you see before you—were participants. Mr Brough might think that; but, if he does, he does not know, because it was. The recommendations this committee made to the government—which were accepted by the government and which I wrote—were for that specific purpose.

Mr Colmer—Can I also quote from the explanatory memorandum of the Energy Grants (Cleaner Fuels) Scheme Bill 2004. It states:

The grant will offset the excise and customs duty payable on biodiesel from 18 September 2003 and continue the current effective excise rate of zero for 100% biodiesel until 30 June 2008. The grant will also be payable on fuel blends containing biodiesel, extending an effective excise rate of zero to the biodiesel component of fuels blends for the same period.

There is nothing there that says that the package was intended to be a stimulus for the biodiesel industry. The stimulus for the biodiesel industry—

CHAIR—Mr Colmer, let us not kid ourselves. The whole point of the package was to provide a stimulus.

Mr Colmer—The whole point of the package was to continue the pre-existing treatment of zero effective excise—

CHAIR—And to extend the time during which that benefit was able to be enjoyed by the industry.

Mr Colmer—Yes, until 30 June 2008—now 30 June 2011.

CHAIR—That is right. And, as we have heard from the witnesses, that policy decision of the government to support the industry in that way has been extremely beneficial and has been a good policy. Do you have anything further to say about that issue, Mr Colmer, Mr Harms or Mr Free?

Mr Harms—I think the issue is—

CHAIR—You will not win my heart or mind by telling me that the purpose of the scheme was not to support the industry, because it was.

Mr Harms—I think the issue is the interaction of the outcome of that legislation—which is to make biodiesel excise free—with the government's policies announced in the energy white paper, which were essentially to remove the tax on business inputs. So where you are trying to sell a tax-free product into a marketplace that pays no tax, that tax-free product does not have any competitive advantage by virtue of its privileged tax treatment.

CHAIR—All right. I think we have heard what you have to say about that. Does somebody want to ask some questions about the BP amendment issue? I know that is a bit unfair to BP.

Senator STEPHENS—Where is it?

Senator WEBBER—Where do I find it? What is it?

Mr Colmer—You will not find it in these bills, because it is not in these bills.

CHAIR—I did not think so.

Senator WEBBER—Where will I find it?

Mr Colmer—You will find it in the Excise Laws Amendment (Fuel Tax Reform and Other Measures) Bill.

CHAIR—Which is the other bill that this committee is inquiring into, with respect to alcohol. Then we might defer any questions to that inquiry.

Senator MURRAY—Except, if I may suggest, Chair, we got evidence on it because it was integrated with the issue. We should at least summarise the evidence that was given to us.

CHAIR—Correct me if I am wrong, colleagues, but the argument as I understood it—and I am not adopting this; it may be completely wrong—was that the definition of what constitutes biodiesel for the purposes of attracting the beneficial treatment has been expanded so as to enable BP and potentially the other oil majors to obtain that benefit as a result of the admixture of a product called tallow into diesel; and the biofuels people say that is not properly a biofuel. Isn't that what it amounts to?

Mr Colmer—Yes.

CHAIR—I know that is not in this legislation, but do you want to comment on that?

Mr Colmer—Your summary is almost correct. The one distinction we would make is that we are not defining what BP is making as 'biodiesel'. It is being defined as 'renewable diesel'. That may be neither here nor there at the end of the day.

CHAIR—But it is an issue of definition, though. They say it is not cricket to include tallow as a biofuel. That is their point, isn't it?

Mr Colmer—I think that is what they were trying to say.

CHAIR—That might be complete rubbish, for all I know. But that is the discussion, isn't it?

Mr Colmer—That is what the discussion is. Certainly, the discussion I heard earlier today was that they did not know whether it met the biodiesel standard. My understanding is that it will not necessarily meet the biodiesel standard. BP have said that it will meet the diesel standard.

Senator MURRAY—Which is why it is called 'renewable diesel', I assume.

Mr Colmer—Which is why it is called 'renewable diesel'.

Senator MURRAY—Is there a definition of 'renewable diesel' in the legislation?

Mr Free—Yes, it is in the excise laws amendment bill.

Mr Colmer—There are a number of benefits from biofuels and we have heard them all today—the renewability factor, the energy security factor, the greenhouse impact, tailpipe emissions and regional impacts. There is no doubt that renewable diesel meets at least the renewability, energy security and greenhouse criteria in exactly the same way that biodiesel does. I do not know what the tailpipe emissions are and I do not know off the top of my head what the regional impacts are, but again that is going to vary substantially. In this case, it will have flow-through impacts on regional industry by increasing the value of tallow as a product, and that will presumably flow back into local rural communities.

CHAIR—It will also benefit BP and whichever of the other oil majors use hydrogenation in their refineries so as to enable them to produce this product.

Mr Colmer—I think the government’s biofuels policy is about biofuels; it is not about—

CHAIR—Privileging one sector of the industry over the other.

Mr Colmer—That is right. Essentially, the arguments made today were competition arguments, as far as I could see.

CHAIR—I agree with you. I think that is dead right. And you have nothing more to say?

Mr Colmer—I do not think there is anything more to say.

Senator STEPHENS—I want to put an issue on the table that was raised by the New South Wales Farmers Association in their submission, No. 14. They say:

... the Association believes there needs to be clarification on what constitutes “vehicles used in carrying out a primary production business”. The current explanation raises questions on whether using a vehicle for agricultural related activities such as carting fertiliser from point of purchase to the farm constitutes use in a primary production business and whether primarily refers to time of use or distance covered.

Would you like to make any comments about that? It would be helpful if you could respond to that.

Mr Harms—Both of those things may be factors in determining whether something is primarily used in agriculture. I think that the activity that they quote, about carrying fertiliser to their property, is clearly part of their primary production business. The ATO ultimately will be putting out guidance as to what vehicles are covered by that. I can think of some circumstances where time would be a factor, where the vehicle was mostly used on the farm, and other circumstances where other things may be factors. I think it would be a combination of a number of factors in determining what ‘primarily’ meant.

Senator STEPHENS—So it will be the ATO’s responsibility to define this?

Mr Harms—Interpret the law, yes.

CHAIR—There is one last issue that I omitted to mention. One of the complaints of the non-fuel users of hydrocarbon products or what you would say are the manufacturing users of fuel is that, if they reach the appropriate threshold, they get caught in the government’s Greenhouse Challenge rules, or whatever they are. The threshold is \$3 million, and they say because they do not burn fuels—they use these hydrocarbons not as fuels but as ingredients—there is no logical reason why they should be caught in the web of the Greenhouse Challenge.

I hope I have not put that wrongly. What do you say about that? You do not have to say anything if you do not want to.

Mr Colmer—I would just make the observation that—and perhaps Michael can give more details if you wish—basically, the Greenhouse Challenge is about managing the energy use of individual businesses. They may not burn the fuel, but I dare say they use energy and if they are getting \$3 million worth of credits then they are going to be a reasonably decent sized business.

CHAIR—No I, think it is about burning fuel.

Mr Colmer—The Greenhouse Challenge is more generally about use of energy, as far as I understand. Is it not?

Senator MURRAY—Page 44, paragraph 2.98, of the EM says:

Receipt of fuel tax credits by large energy users is conditional on those entities being members of the Greenhouse Challenge Plus Programme.

Later on it says:

Membership of the Greenhouse Challenge Plus Programme signals an expectation that large energy users will participate in an active partnership with government to address climate change.

In my own view that is unexceptionable and to be admired.

CHAIR—Thank you very much, Mr Colmer, Mr Harms and Mr Free. You are excused. I remind you that the answers to the questions taken on notice should be provided by email to the secretariat by the close of business tomorrow and the committee will consider the matter.

Committee adjourned at 7.03 pm