



COMMONWEALTH OF AUSTRALIA

# Official Committee Hansard

## SENATE

ECONOMICS LEGISLATION COMMITTEE

**Reference: Energy Grants (Cleaner Fuels) Scheme Bill 2003**

TUESDAY, 7 OCTOBER 2003

CANBERRA

BY AUTHORITY OF THE SENATE



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## **WITNESSES**

<b>BLACK, Mr Kevin Raymond, Managing Director, Natural Gas Vehicles Group Pty Ltd .....</b>	<b>37</b>
<b>ELLIOTT, Mr William Raymond, Spokesman, Australian Coalition for Ethanol; and Ethanol Project Manager, Dalby Bio-Refinery Ltd .....</b>	<b>17</b>
<b>FLETCHER, Mr Les, Director, Manildra Park .....</b>	<b>1</b>
<b>FREE, Mr Anthony John, Manager, Excise Unit, Indirect Tax Division, Department of the Treasury .....</b>	<b>45</b>
<b>GORDON, Mr Robert, Executive Director, Australian Biofuels Association.....</b>	<b>1</b>
<b>HARMS, Mr Michael, Acting General Manager, Indirect Tax Division, Department of the Treasury .....</b>	<b>45</b>
<b>HARRISON, Mr Christopher, Spokesman, Australian Coalition for Ethanol; and Director, Dalby Bio-Refinery Ltd .....</b>	<b>17</b>
<b>MACPHERSON, Mr Ewen Duncan, Deputy Director, Australian Institute of Petroleum.....</b>	<b>14</b>
<b>NEILSEN, Mr Warring John, Manager, Corporate Affairs, Elgas Ltd.....</b>	<b>28</b>
<b>NORTH, Mr Raymond, General Manager, Australian Liquefied Petroleum Gas Association .....</b>	<b>28</b>
<b>PRESTON, Ms Kate, Policy Analyst, Indirect Tax Division, Department of the Treasury .....</b>	<b>45</b>
<b>ROSE, Mr Griffith Frank, CVC Reef Ltd and Australian Biodiesel Consultancy.....</b>	<b>42</b>

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**SENATE**  
**ECONOMICS LEGISLATION COMMITTEE**  
**Tuesday, 7 October 2003**

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

**Substitute members:** Senator Allison to replace Senator Murray for matters relating to the Resources portfolio

**Participating members:** Senators Abetz, Boswell, Buckland, George Campbell, Carr, Cherry, Conroy, Cook, Coonan, Eggleston, Chris Evans, Faulkner, Ferguson, Ferris, Forshaw, Harradine, Harris, Kirk, Knowles, Lees, Lightfoot, Ludwig, Lundy, Mackay, Marshall, Mason, McGauran, Murphy, Payne, Ridgeway, Sherry, Stott Despoja, Tchen and Tierney

**Senators in attendance:** Senator Brandis (*Chair*) Senator Stephens (*Deputy Chair*), Senators Allison, Chapman, and Webber

**Terms of reference for the inquiry:**

Energy Grants (Cleaner Fuels) Scheme Bill 2003

**Committee met at 4.35 p.m.**

**FLETCHER, Mr Les, Director, Manildra Park**

**GORDON, Mr Robert, Executive Director, Australian Biofuels Association**

**CHAIR**—Welcome. I declare open this public hearing of the Senate Economics Legislation Committee, the purpose of which is to receive evidence on the Energy Grants (Cleaner Fuels) Scheme Bill 2003 and the Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003. On 17 September 2003, the Senate adopted the Selection of Bills Committee report No. 11 2003 and referred the provisions of those bills to the Senate Economics Legislation Committee for report by 16 October 2003. The bills provide a framework for the payment of grants for the importation and manufacture of cleaner fuels. The Selection of Bills Committee report directs this committee to examine particularly the definition of cleaner fuel in the legislation and the subsidy arrangements applying to those fuels.

Before we begin taking evidence, I remind you that all witnesses appearing before this committee are protected by parliamentary privilege. Parliamentary privilege refers to the special rights and immunities necessary for the discharge of parliamentary functions without obstruction or fear of prosecution. Any act by any person which operates to the disadvantage of a witness on account of evidence given by that witness before this committee is treated as a breach of parliamentary privilege. These privileges are intended to protect witnesses. I also remind you that giving false or misleading evidence to the committee may constitute a contempt of the Senate.

The committee prefers all evidence to be given in public but should you at any stage wish to give any part of your evidence in private you may ask to do so and the committee will consider your request. I now invite you to make a brief opening statement and then we will proceed to questions.

**Mr Gordon**—Thank you. The Australian Biofuels Association is the peak body representing the commercial biofuels industry—namely, ethanol and biodiesel production in Australia. Our membership represents current biofuels producers and prospective new biofuels industry entrants. We represent independent fuel companies, distributors and sellers of biofuels, which effectively provide the backbone of competition in markets largely dominated by major oil companies.

We see a future where common interests between biofuels and petroleum fuels will dominate and dictate the establishment of a fair working relationship in the future. As we speak, there is between \$400 million and \$600 million in new ethanol and biodiesel refineries on the drawing boards. We are confident that, if the government delivers on its election promises, we can meet the projected government target of 350 million litres of biofuels used in Australia within five years—at least two years before the 2010 target set by the government.

We are concerned that future biofuels expansion has been put at risk by the politicisation of biofuels and the rough and tumble of competition at the federal level. This is in stark contrast to the position adopted by the Queensland and NSW governments on biofuels and the benefits they offer in terms of the environment and mitigating the risks of petroleum fuels, air pollution, the risk to human health, reducing greenhouse gas emissions and in terms of economic and employment growth in rural Australian communities.

We have been particularly concerned that factually based information about ethanol has taken a back seat to ambit claims that have been fabricated or are unsubstantiated or both. We hope that the deliberations of this committee will assist in depoliticising the ethanol debate and concentrate on factual information and data based on 22 years of safe and reliable on-road use with 10 per cent and higher ethanol blends and biodiesel in the United States, Brazil and Europe, in Australia over the past 10 years and now recently in New Zealand. Today, there is a clearly discernible movement in countries such as India, China, Japan, Mexico, New Zealand and Thailand to biofuels as a means of ameliorating the impacts of petroleum fuels and developing future energy security options.

We do not claim that biofuels alone represent the future fuel mix of Australia or represent the saviour of the Australian sugar industry, for example. We do, however, have a role to play in addressing both of these issues. We participate in today's hearings in the hope that the overall national interest of Australia and factual information will form the basis of a forward-looking policy, not only for biofuels but for other alternative fuels including LPG and CNG.

**CHAIR**—Would your colleague like to make any additional remarks?

**Mr Fletcher**—Not as an opening statement.

**Senator STEPHENS**—Thank you for your submission, gentlemen. I would like to pick up on some of the issues you raised in your submission and ask you, first of all, whether there have been any independent performance reviews of the industry.

**Mr Gordon**—Our industry has probably been the most studied industry in the fuel business in Australia, and the studies continue. As we understand it, the government has set in train more studies about the likely viability of our industry and this will just build on a number of earlier studies that have been done by ABARE and others. In respect of the actual trials of ethanol blend fuels in the Australian vehicle fleet, Australia conducted in New South Wales what were probably the largest trials in the world of a 10 per cent ethanol blend. The steering committee of those trials involved: the Federated Chamber of Automotive Industries, representing the automobile manufacturers and importers; the NRMA, representing Australia's motoring associations; the Australian Institute of Petroleum; and a whole range of other technical organisations that contributed to that \$250 million trial program.

The results of those trials essentially replicated the results of similar trials conducted in the United States over the past 20 years and indicated that there was a commonality of experience, not only with the Australian vehicle fleet but also with the experience in the United States with a 10 per cent ethanol blend over the past 20 to 22 years. There have been very extensive trials; there is very little that is not known on the use of biofuels, particularly ethanol, in the marketplace as we know it today.

**Senator STEPHENS**—Can you just elaborate a little on the argument in your submission? You argue that exemption from the fuel excise has provided:

... a sound basis for investment in alternative fuels, and offer renewable fuels (ethanol and biodiesel) a sound platform for future expansion ...

Then you claim that there is no evidence to support:

... Government claims that the proposed changes will provide a sound basis for future investment in alternative fuels.

Can you just elaborate on that argument that you present?

**Mr Gordon**—Perhaps it was not so much an argument as the position that we see exists today. As we understand it, the government has basically put forward a framework bill on an energy scheme which entails significant changes to a regime associated with the use of fuel excise over the past 20 or 22 years. It is 22 years when you look at the treatment of LPG, for example. It certainly has permitted the LPG industry to establish an infrastructure within Australia, particularly in Victoria, which I think most Australians would be pretty proud of, and it gave that industry the opportunity to establish solidly its foundations in this country. We stand on a platform which offers significant future expansion of biofuels production in Australia; that is, ethanol and biodiesel. We are confident that, if we can secure long-term policy certainty from the government, we can readily achieve those targets, particularly if the promises the government has made in terms of long-term policy security are met.

**Senator STEPHENS**—Can you talk to us a little bit about the take-up rate of biofuels?

**Mr Gordon**—The take-up rate with biofuels in Australia has been fairly slow, mainly because production has been limited to essentially two producers. The main producer of ethanol, for example, has been the Manildra Group. They have been followed, with smaller amounts of ethanol fuel production, by CSR distilleries, which has an ethanol distillery located in Sarina, near Mackay, in Queensland.

Biodiesel production is genuinely at an infant stage in Australia. We represent the potential future commercial producers of biodiesel. There was a small biodiesel plant in Moama, which is no longer producing commercially. But there has been the establishment of a biodiesel production facility near Newcastle, and that is starting to supply commercial scale biodiesel to the New South Wales transport fuel market, mainly for use in diesel engines in mines underground and for council fleets. Like the ethanol industry, it is looking forward to the implementation of the 350-million-litre government program. We are confident that not only will we see a significant increase in ethanol production in Queensland, New South Wales, Western Australia and Victoria but also we will see an expansion in production projects with respect to biodiesel in those states as well.

**Mr Fletcher**—I am a director of a company called Manildra Park Petroleum. We have a partnership with the Manildra company that has been running for some two years. I first started buying ethanol from Manildra in 1992. I found that, basically from the day I first purchased ethanol from Manildra, I was shut out by the oil companies. Shell went to one customer and said: 'If you're going to continue buying blends of this, we'll take our sign away. It adulterates our fuel.' This story continues today. Today I still cannot buy petrol from a major oil company to blend with ethanol. If I can buy the quantity I want, I cannot buy it at a price where I can resell it. From 1992 until today, I have subsidised petrol with ethanol to sell it. What worries me greatly is that the Manildra plant recently put off 50 people because we could not sell the ethanol. I currently have 10 million litres of ethanol stored. I do not know what I am going to do with it. Manildra has a plant at Nowra on which it has spent close to \$30 million. Its main function was to treat effluent and we were to get ethanol from our part of that effluent. That plant cannot be started up and run at its full capacity today because we do not know what we are going to do with the ethanol.

The federal government has appointed a facilitator to go to the oil companies and see what has to be done. It would be wrong for me to pre-empt what will happen there, but there have been meetings with two of the companies. I believe that tomorrow there will be meetings with two more of the companies. The facilitator will report to the government on how successful those sales may or may not be. It does not seem to matter what we do—we cannot buy petrol to blend with the ethanol nor sell ethanol to these companies. That is my experience of the ethanol side of biofuels in this country.

You are probably all aware of the politics of things. I was at one meeting with Mr McMullan, who at that time was the shadow Treasurer for the opposition. He said to us: 'We're all for ethanol but, when the politics come into it, we're more interested in getting the Prime Minister.' I just thought how disgusting it was.

**CHAIR**—That was an ungracious thing to say.

**Mr Fletcher**—That is what he said. Sure, have your politics and do what you want to do, but why destroy an industry? Why let people lose their jobs? We seemed to run into problems with Environment Australia. They wanted 10 per cent. Since 1994 we have been selling 20 per cent blends in Sydney. We supply most of the independents. We are probably responsible for keeping the price down some 3c to 6c a litre per week. As you probably all know, in Sydney you pay 10c to 14c a litre more at the oil company sites on Wednesdays than you do on Tuesdays. I believe that that was part of the reason for conducting the war against the 20

per cent. We had a meeting with Greg Bourne, who at the time was the CEO—he may still be—of BP. He said to Dick Honan and me: ‘Gentlemen, congratulations on getting where you’ve got to, but tonight I’m off to have dinner with the General Motors people and I think that’s where we might get you.’ We had lunch with Tony Blevins at the Hyatt Hotel. He was the CEO of Caltex before the last one. He said exactly the same thing: ‘We’ll fix you guys and you will not be able to blend your 20 per cent.’ The result of that is, as you all will have seen, the no ethanol signs at all the major company sites. Before we go anywhere, I think we have to ask why these companies will not take up ethanol.

**CHAIR**—It is because they want to sell more petrol, of course.

**Mr Fletcher**—Exactly.

**CHAIR**—But surely a supplier—Shell, Caltex or BP—is entitled to protect its product from being what it considers to be adulterated by admixture with another substance which it claims—and I know this is a controversial claim—will degrade the product. If Shell supplies to a Shell-badged site, why isn’t it entitled to say to its distributor, ‘You are only to pump Shell petrol through your pumps’?

**Mr Fletcher**—Granted, and I agree with that. I would be the last one to take that right away from anyone. But what I do not understand is how they can run a campaign against ethanol when every one of those companies buys and blends hundreds of millions of litres of ethanol a year in the US and other countries around the world. Why run the campaign to destroy it? In my experience—with the hundreds of millions of miles that we have sold ethanol to drivers for—there is no problem as was made out. They were just put out there and it was a campaign to stop ethanol.

**CHAIR**—But they are selling their own commercial self-interest. They are entitled to do that, aren’t they?

**Mr Fletcher**—I do not think I would go down and say, ‘Shell petrol is bad and this is bad’—not when I was using the same petrol myself and selling it. They are doing the same thing. They are buying ethanol in every other country in the world.

**CHAIR**—As I hear you, your criticism of them amounts basically to an allegation of hypocrisy—that is, they are condemning as bad policy in Australia what they are happy to do in other nations. Is that what it amounts to?

**Mr Fletcher**—Exactly, yes.

**CHAIR**—Sorry, Senator Stephens.

**Senator STEPHENS**—I have lost my train of thought. I will pass to Senator Webber for a minute.

**Senator WEBBER**—I want to return briefly to your statement earlier where you were outlining your confidence in the future of the industry. I want to explore how firmly attached that confidence was to the passage of this legislation and whether in fact the delay in the introduction of this legislation had caused any anxiety. I know it was part of the budget process and was meant to have a start-up date of 18 September or something, but here we are in October going through the processes.

**Mr Gordon**—My response to that is in two parts. As far as the contents of the bill are concerned, at this time we know as little as you do about what the actual government policy will be on future excise rates by moving to an energy content framework and these issues. It is very difficult to give you a clear and precise answer. I wish I could, but I cannot.

**Senator WEBBER**—Fair enough.

**Mr Gordon**—In terms of the wider issues, there is a genuine concern about the early movement and passage of this bill. As you are aware, the introduction of the grant scheme was proposed for 18 September. That was to include a producer subsidy for biodiesel and to reconfirm, effectively, a producer subsidy that had been confirmed for ethanol in production and the marketplace. The importance of that was in part because of concerns about the introduction of imported fuels, particularly highly subsidised ethanol from countries such as Brazil, which currently produce anywhere between 12 and 15 billion litres of ethanol per year. They are the largest producers in the world and effectively control not only the price of ethanol internationally but also the price of crystal sugar. They do this very effectively. When the sugar is delivered to the sugar mill or the refinery, it is graded. If it does not meet a certain quality standard that is suitable for the production of A-grade crystal sugar, all of it is moved into ethanol. What the industry has done in Brazil is give that country the capacity and flexibility to move the price of crystal sugar or ethanol as it suits them and as is reflected by the demands of seasonal factors.

The Brazilians regularly visit Australia. They have been closely following events here. Our concern has been that, if highly subsidised ethanol were to enter this market in high volumes before the foundations of an Australian domestic industry were established, the prospects of actually establishing a domestic industry and all the benefits that it brings not only environmentally but economically, including new jobs growth in rural Australian communities, would be lost. We believe that is the case also with biodiesel. We were surprised that the bill does not propose similar cover for biodiesel.

We object to that because we believe that the case that was made for ethanol that was accepted was equally applicable for biodiesel. We believe that it also provides Brazil with a chance because, if Brazil were to take up the opportunity to invest in the Australian industry, they would also have access to the producer subsidy for which that date of 18 September has some significance. So, for these reasons, we would hope that the bill can go forward. At the same time, we would like to say we were in a better position to evaluate the details of how alternative fuels will be treated under a new energy based system which, as we understand it, would be a theoretical, calorific energy based system which would not reflect real world conditions and performance not only of petrol and diesel fuels but also of alternative fuels. We see real complications in adopting that approach—indeed, no other country in the world, as far as our knowledge goes, has adopted this approach. So, yes, we have concerns about it. We would hope that the Senate could deal with this matter fairly efficiently and that we could move forward, but I am sure that, in a similar circumstance, you would like to have more detail.

**Senator WEBBER**—Indeed. That is partly what this afternoon's hearing is about. In your view, was there adequate consultation by government with industry in the development of this legislation?

**Mr Gordon**—The government has established an energy task force, which has been looking into these issues. Our industry and others have sought them out, have had engagements with them and have made presentations to them. With respect to ethanol, associated with the energy task force has been a restoring confidence to ethanol working group, which we have been part of, as has the AIP, the AAA, the Service Stations Association of Australia, the oil companies and anybody who has a vested interest in it—including, most importantly, prospective new entrants into the industry. So there has been consultation. We would like to have seen more give on the other side of the table, but we have done what we can with the opportunities we have had.

**ACTING CHAIR (Senator Stephens)**—Let me take you back, just so I can understand your industry a little better. I then want to talk to you about the issue that you raised quite specifically in your submission about moving to an energy content basis. Just so that I do understand the size of your industry and its make-up, I would like to ask you very bluntly: is your industry sustainable without government assistance?

**Mr Gordon**—No alternative fuel industry, as I understand it, is fully sustainable on the basis of competing economically with petroleum fuels. Part of that is complicated by the fact that the price of petroleum fuels, whether it be oil or gas, is not set by the free market—oil is set by the oil cartels, and gas is set by Saudi Arabia.

Our industries have to compete for their feed stocks and products in the open and free market, so it is difficult to be precise in how competitive we are. We do know that as the price of oil increases we become increasingly competitive and we know that, once our industry has the capacity to grow and we have the advantage of economies of scale, we will become increasingly competitive over—we believe—the next 10 years. We would hope that within 10 years we will be close to being competitive with petroleum fuels, particularly if not only Australian but also international estimates about the sustainability of existing domestic oil and gas reserves are met.

One thing is certain, however, and that is that in every country in the world new industries of this kind have required and received some sort of support from government. The oil industry, for example, does not accept any responsibility for the externality impact of its fuels—whether in terms of greenhouse, air pollution or health risks and other impacts associated with the use of those fuels. All alternative fuels—whether LPG, CNG, ethanol or biodiesel—play a role in addressing and reducing those costs to both the taxpayer and the community. I cannot provide you with a simple answer, but it is the real world that exists out there. Over the past 10 years the United States industry has reduced its costs by about 50 per cent. We would expect that we could achieve similar targets in Australia.

**ACTING CHAIR**—So you are suggesting perhaps a 10-year horizon for being able to be as self-sustaining as any of the other energy industries.

**Mr Gordon**—Yes.

**ACTING CHAIR**—In your submission you recommend that the entitlement and payment of the grants be deferred for five years.

**Mr Gordon**—For biodiesel.

**ACTING CHAIR**—Yes, for biodiesel. What would the five-year threshold deliver for your industry?

**Mr Gordon**—A five-year threshold makes it very tight for our industry. When the government announced its biofuels cleaner transport fuels initiative in the lead-up to the last election, the clear inference was that our industry would be provided with a 10-year excise period. That was close to what the oil companies, as well as the financial institutions that we need to support industry growth, were proposing. Our preferred position would be a period of 10 years of excise exemption before moving to the proposed phase-out. We believe that would give us the opportunity, and would obviously give LPG and CNG that additional opportunity, to become stable and to become competitive in the marketplace here.

**ACTING CHAIR**—In five years time, how much growth do you anticipate in your sector?

**Mr Gordon**—We are very confident we could quickly achieve the 350 million litre target. We believe we could exceed that if the promised long-term policy certainty announced by the government in the lead-up to the election is adhered to. We believe that by 2020 our industry would have the capacity to supply 10 per cent of transport fuel—that is, petrol and diesel—used in Australia. That may sound optimistic, but it would closely reflect the rapid expansion that is going on in the United States. But we first of all need a foundation upon which to provide a jump-start for that growth. If we do not have that, we are not going to go anywhere. Currently, our industry produces between 130 and 150 million litres of ethanol and biodiesel a year, so it is very small in the international arena by any measure.

**ACTING CHAIR**—I am conscious of going over time, and I am sorry to the other witnesses for doing that, but I want to take you to that other issue about the theoretical calorific value. Can you help me out a little bit more with that? You touched on it briefly and suggested that it is not being used anywhere else. Have you any sense of why it has been introduced here?

**Mr Gordon**—It is so difficult. Because it is a theoretical measure of energy, it does not necessarily reflect its actual use in vehicles. It is very difficult to use as an accurate measure to balance out what other benefits may flow or, in particular, what benefits may be attributed to alternative fuels such as our own.

**ACTING CHAIR**—Do you think this shift has come from the energy task force?

**Mr Gordon**—No, it was in the budget. The movement to an energy based scheme was set out in the budget papers. There should be recognition of the environmental and other benefits of alternative fuels. The task of trying to establish and set a value on those benefits is as complex for a theoretical energy based system as it is for our fuels, but we believe and are very confident that the return the government gets in terms of flows of revenues and taxes back to Treasury from the operation of an ethanol plant, for example, which is one of the measures we have used, and the impacts on the wider community would represent around 28c per litre flowing back to government. When you add up the environmental benefits—for example, our fuels are natural octane enhancers, which we provide to petroleum fuels and which are going to become important with new fuel standards by 2005-06—we are confident that we would exceed, in returning benefit back to the government, the 38.143c a litre we currently get from the government as a producer's subsidy.

**ACTING CHAIR**—This is my final question. Do you have any observation to make about why ethanol is being treated separately with respect to the production subsidies and is not actually captured in this bill but in an appropriation bill? Do you have any comments on that?

**Mr Gordon**—We have seen no explanation whatsoever. We would be as interested as you in anything that officials may be able to provide on that issue later.

**ACTING CHAIR**—Thank you very much, Mr Gordon.

**Senator ALLISON**—At the risk of asking questions that have already been answered or asked, Mr Gordon, could you comment on the E10 blends and on the perception of the public that ethanol is somehow an inferior additive to petrol? Could you explore for the committee the environmental advantages of that blend?

**Mr Gordon**—We touched briefly, but not specifically, on that issue earlier, and I am happy to elaborate on that. This has been one of the more disappointing aspects of what we have all seen as the ethanol debate over last year and longer. One of the tasks set for the working group on restoring confidence to ethanol was to have the Federated Chamber of Automotive Industries go to the automobile manufacturers and importers and conduct what was thought to be a fairly simply and straightforward task. As you will recall, during the debate on what the most appropriate ethanol blend levels were, all parties openly acknowledged that a 10 per cent blend was a safe, proven and reliable fuel, as demonstrated in America and elsewhere. In the United States, for example, it was not only warranted but recommended for use by all of the car manufacturers that produce cars in Australia and by all of the companies that import vehicles into the Australian market.

What was even more disappointing was that the facts associated with the largest trial of an E10 blend in the world, which was conducted in New South Wales in 1997-98, which cost the Australian taxpayer around \$2.5 million and which involved some 60 cars, clearly replicated other trials and demonstrated that the use of an E10 blend in the Australian vehicle fleet posed no technical, compatibility, engine wear or other associated problems. That related to all vehicles—both pre- and post-1986 vehicles. In saying this, we acknowledge that with some older vehicles there could be a build-up of rust in the fuel tanks and gums in the fuel lines and that if they are not operating efficiently it may be advisable to visit a mechanic to have your vehicle inspected before you use an ethanol blend fuel for the first time. But the experience in New South Wales over the past 10 years has confirmed the results of the Australian trials in 1997-98 and trials that have been conducted over the past 20 years by the US Department of Energy and other government agencies in the United States. If the facts were the determining factor here, there would not be a debate on the use of a 10 per cent ethanol blend in this country. There is not such a debate in New Zealand, which some two weeks ago decided to go to a 10 per cent ethanol blend. They provided cautionary advice on the use of ethanol for the first time in some older vehicles, but that is all.

We have and can provide the committee with lists of those automobile manufacturers and importers in the United States who not only warrant the use of an E10 blend but claim that it is safe and reliable in all vehicles. There is an email in our submission from the California Energy Commission that reflects that advice more recently—that all vehicles over the past 20 years have been able to use a 10 per cent blend efficiently. Unfortunately, there have been

claims that millions of vehicles cannot operate effectively on E10. This frankly is rubbish. There was a claim that there was a secret report on which this was based. Again, that is rubbish. There was no such secret report. There was a working paper that is still in progress by the FCAI. Based on an initial report, the FCAI recommended they go back to the automobile manufacturers in Australia and the importers of vehicles into Australia to deal with the inconsistencies of some of the responses. There was no indication that millions of vehicles could not operate effectively on an E10 blend. Indeed, when you looked closely and analysed the responses in the initial FCAI report, it quickly became obvious that a number of those pre- and post-1986 vehicles were actually tested during the 1997-98 Australian trials of E10 and were proven to operate very efficiently on an E10 blend.

**Mr Fletcher**—I would just add that every one of the newspaper articles on the claims of damage was followed up and, to date, we do not have one vehicle that was run on an ethanol blend that was claimed to have had problems. Bob Gordon followed those claims up through the Biofuels Association, and I think he could provide the committee with evidence of those follow-ups.

**Senator ALLISON**—Towards the end of your submission you talk about the five-year period after which the producer subsidy will be available to Brazilian producers—and, presumably, producers from elsewhere. What do you see the viability of the industry in Australia being in five years time? Will we be competitive with heavily subsidised Brazilian imports of ethanol by that time? If not, what do you think is likely to happen to the industry in anticipation of that five-year changeover?

**Mr Gordon**—If we do not get that, we will not go anywhere. If this market is flooded with cheap, highly subsidised ethanol, whether it is from Brazil or elsewhere, or, equally, biodiesel—not necessarily from Brazil, but from other sources—it will make it very difficult for financial institutions or anybody to support the development of a domestic industry. The five years at least gives us the opportunity to establish a foundation for domestic biofuels production in this country. So we will start off with a chance. What happens from then, we will see. Five years is a long time. If we can demonstrate that there is a large number of benefits—as it has flowed for Brazil from the establishment of a domestic biofuels industry—perhaps this issue will be revisited. At least we have five years—so we are grateful for that. If we could have more, we would be even more grateful. If we had 10 years, we would be better established. But we have learnt to take what we can get and be grateful for small mercies.

**Senator ALLISON**—So would you expect the government to have done some sort of analysis of the likelihood that five years was going to be the right period of time in which to allow the industry to develop? Did you see any evidence that the government has actually done this work?

**Mr Gordon**—No, we have not. We have seen no evidence of that. In fact, as I mentioned before, we would be very interested to see what information is provided in that regard by officials later tonight.

**Senator ALLISON**—So if I can just make this clear: you would like to see the Senate perhaps amend the legislation to change the five-year period into a 10-year period. Would that be a good outcome for your industry?

**Mr Gordon**—It would give us time to set an industry of a scale that would have greater efficiencies of scale in terms of production and will be more competitive. We would hope that the Senate would also consider extending this benefit to biodiesel. As I mentioned earlier, the case for providing biodiesel protection against imports initially is as compelling as it is for ethanol.

**Senator ALLISON**—It goes to another piece of legislation that another committee will deal with in a few days time, but there is a question of labelling at the point of sale. Is it your view that instead of ‘no ethanol’ labels, we should be saying ‘no toluene’ or no other substance which ethanol might be a substitute for and a cleaner substitute for? What is your recommendation on labelling—which you describe as discriminatory?

**Mr Gordon**—As it is judged important enough to label the contents of food, we believe that it is equally important to label the contents of fuel. Looking at the pervasiveness of food items, it is a very wise step to take. Most people forget that the use or take-up of transport fuels is also substantially pervasive throughout our community, but the average Australian is pretty much ignorant of what is in their fuels. The reality is that those fuels have had a great influence on our society, our freedom to move and all these things, but they also carry risks in terms of air pollution and associated risks to human health. We believe that it would be in the interests of the public to have sensible uniform labelling of the contents of all fuels. We are concerned that, while the current ‘no ethanol’ anti-ethanol campaign is being waged throughout Australia, if ethanol alone were required to label, the situation for our industry would be highly discriminatory and potentially damaging.

**Senator ALLISON**—Would you prefer to see the actual content of petrol in this case or, given that most people would not understand what benzene or toluene means in terms of emissions, would it be better to have a kind of clean fuel rating system that could be judged by another body?

**Mr Gordon**—That is certainly a possibility. It is perhaps instructive to look at what is happening with the major oil companies in certain places. For example, in the United States there is not uniform labelling with fuels. In California, there is no requirement for labelling ethanol content in fuels. But in places like Nebraska, for example, there is a limited simplified label of E10: effectively ‘this fuel contains 10 per cent ethanol content’—and that works. If you get into the detailed chemical contents or the compound contents of fuels, it can become very complex; there may be a requirement to give some general warning of some of the health impacts.

We would prefer that we start off with a common simplified labelling process that makes the consumer aware of what is in their fuels. During the ethanol debate there was a lot of emotion based on what, as recalled by Mr Fletcher, were proven fabricated claims of ethanol-related engine damage not only in New South Wales but also in Victoria; none of those were found to be substantiated. Indeed, in the case of the *Sydney Morning Herald* article that started this off on 18 December last year, that paper issued a retraction and an apology for that article acknowledging that it was a fabrication. But in the heat of all of that we had quite emotional claims that ethanol should not be used in aircraft. For God’s sake, ethanol is not used in aircraft. With aircraft there is no room on the forecourt to land or park for the aircraft to be loaded with fuel.

But it is clear that all transport fuels—whether petrol, diesel, ethanol or biodiesel—are designed for automotive use. That said, there is a wide range of nonautomotive applications—whether with whipper snippers or small engines—that are built around the use of transport fuels and that generally require an additive of some kind, perhaps two-stroke oil, to operate. Like E10 blends, those fuels are generally recognised in the United States as being compatible with a 10 per cent blend. We can provide you with lists that indicate that. Probably commonsense would dictate that not only ethanol or biodiesel but also regular and premium fuels in Australia should carry an equal warning to the consumer that: ‘If these fuels are used in nonautomotive applications, please contact your manufacturer or refer to your user manuals.’ That would be a sensible thing to do. This business of having a whole range of symbols saying ‘Beware, don’t use this fuel’ really is over the top; and we believe it has more to do with emotion than factual information that is available readily not only here but elsewhere around the world.

**Mr Fletcher**—At a recent meeting with the New South Wales EPA that Bob and I attended, they were very concerned with the amount of benzene allowed to stay in our fuel, which is up to five per cent. They were considering testing New South Wales fuel for benzene content and maybe even banning the amount that there was because of the carcinogenic effect of benzene. So they are quite worried about it.

**Senator CHAPMAN**—I have no questions.

**Senator WEBBER**—In listening to that exchange, a question occurs to me. I accept what you were saying earlier about your confidence in the industry to develop the required capacity should the legislation go through. But isn’t one of the challenges for the industry to develop consumer confidence rather than the capacity to deliver? In fact, one could mount the argument: why should we subsidise a product that consumers do not want to buy? They have demonstrated that they do not want to buy it. Shouldn’t the government put the money elsewhere?

**Mr Gordon**—I would not necessarily agree that the government should put the money elsewhere. Certainly one has to acknowledge that, over the past year, serious damage has been caused to people’s perception about the use of ethanol blends in fuel. As I said earlier, there was general accord politically and across the board from all interest groups—whether it was the automobile manufacturers and importers or the petroleum industry—that a 10 per cent ethanol blend was a safe and reliable fuel; yet almost simultaneously with that fabricated article in the *Sydney Morning Herald* about ethanol damage in Sydney the major oil companies launched a national ‘no ethanol’ campaign, which was a carbon copy of a campaign launched by their parent companies in the United States 20 years ago. And it had the same impact in the United States. ‘No ethanol’ implies that something is wrong, but there is no explanation of why they say ‘no ethanol’ at the point of sale. This sense has been accentuated by the range of exaggerated claims about damages associated with ethanol.

We have been part of a working group that is designed to deal with restoring confidence to the ethanol industry. The first step would be the removal by the major oil companies of their ‘no ethanol’ signage. What they are doing is totally at odds with what their parent companies are doing in the United States every year. In the photographs we have given you and in the brief on California, for example, the major oil companies and our industry in America are

working together on a renewable fuel standard which will see an increase of ethanol production in the United States from somewhere around nine billion litres a year now to about 20 billion litres by 2012. What concerns the oil companies in Australia is understandably market share, and they wish to protect that. But they do have needs for alternative fuels—for natural octane enhancers and oxygenated fuels—to meet future fuel quality standards. So we look forward to the time—and we hope it will arrive quickly—when we will give up this current sort of activity we are going through and, working together, get on with the business.

**Senator WEBBER**—Does the industry have any plans to do something positive about restoring consumer confidence? We will get to talk to the petrol companies a bit later on.

**Mr Gordon**—Yes, we do. We are looking at advertising campaigns and at engaging the consumer at the point of sale. We are looking at a range of measures. For example, as Les has just mentioned to me, some of that activity is going on. BP sold some 10 million litres of fuel in trials in Brisbane. That represents about 100 million litres of a 10 per cent ethanol blend fuel in Brisbane in all vehicles representative of the Brisbane fleet, with no difficulties being demonstrated technically or otherwise. Currently Caltex is running trials in Cairns and is extending them to Mareeba south of Cairns. So some bright spots are on the horizon but, yes, there is a big challenge that we have to overcome and we know we have to make a big commitment in that regard.

**ACTING CHAIR**—Gentlemen, thank you for your submission and for your evidence today. No doubt you will follow the inquiry's proceedings with interest.

[5.36 p.m.]

**MACPHERSON, Mr Ewen Duncan, Deputy Director, Australian Institute of Petroleum**

**ACTING CHAIR**—Welcome. The committee prefers all evidence to be given in public but, should you at any stage wish to give any part of your evidence in private, you may ask to do so and the committee will consider your request. I now invite you to make a brief opening statement.

**Mr Macpherson**—First of all, we fully support this bill and we urge that it be passed as soon as possible. We support strongly the general intent of the bill to give a framework for the payment of grants for all cleaner fuels and biofuels. But our main interest at present regards the incentives for the early production of cleaner petrol and diesel. AIP and its member companies are fully supportive of the government move to introduce cleaner fuels to Australia and the mandatory fuel standards which underlie that move. We have worked closely with the vehicle industry to ensure that the vehicle technology necessary for the desired better air quality output from vehicles and increased fuel efficiency is matched by the availability of the cleaner fuels necessary for that to happen. We believe that this will certainly have important benefits in terms of air quality in our cities, fuel efficiency and general health.

The bill as it stands is focused partly on reduction of sulfur in petrol and diesel, in line with Euro standards. As an indication of the benefits, we have outlined in our submission that the US EPA has noted in a cost benefit study that the benefits were of the order of 16 to one in favour of lower sulfur. In Australia we already have some mandatory lower sulfur standards in place. The major change for petrol and diesel will come in in 2005-06, and there will be a further round in 2009 approximately.

One of the key issues which we have worked on with the vehicle industry is that, while we are matching on timing for the 2009 lower sulfur petrol and diesel—which effectively means zero sulfur for diesel and 50 ppm sulfur for premium petrol—a part of the new vehicle fleet, particularly imports, would benefit from having those fuels earlier than 2009. That does cause a problem for our refiners. We are still working on putting in place the investments necessary to meet the 2005-06 standards, and the cost of these alone is close to \$1 billion.

The refiners need to bed down these investments, and when you start looking at the further investments necessary for lower sulfur, again in 2009, there is a logical sequence of investments necessary to reach that goal. We also need about three to four years to put it all in place. Any departure from that time frame will lead to a major increase in costs. We certainly argue that the mandatory standards should not start before 2009, which is in line with the announced government policy.

As I have said though, part of a vehicle fleet could benefit from some early availability. We believe the incentives program outlined by government would be a most important step to achieve this. We also understand that, if this is available, there will be benefits from the existing vehicle fleet as well. The incentives outlined will give your suppliers much more flexibility to be able to bring forward part of investments so part of that supply can be made available. We urge that this be put in place as fast as possible to provide certainty for investment.

**ACTING CHAIR**—Thank you, Mr Macpherson. Your submission is succinct and to the point about the final point you made about certainty of investment. You have suggested and reiterated here today that there would be an investment requirement of at least \$1 billion to the refineries with a further \$1 billion down the track.

**Mr Macpherson**—That is correct.

**ACTING CHAIR**—That is fairly significant. One of the things that struck me in the explanatory memorandum of this bill is how does one define clean, cleaner and cleanest. Do you have any comments to make about what is ‘clean’ petrol?

**Mr Macpherson**—Let us look at the progress in fuel standards over the last three to four years and see where we are going. The key focus has been benzene, which is effectively to be removed from petrol. By 2006, we will be down to less than one per cent maximum. At present we are running at about 2½ per cent. That is a major investment that is already in place. The next measure is to move the base fuel from 91 octanes to 95 octanes, which is quite necessary for the new engines.

But perhaps the most important change, which affects both petrol and diesel, is to remove sulfur or reduce it as low as possible. If you look at the Euro 4 and Euro 5 standards and where they are getting to, we are now at the point where—certainly with Euro 4 and possibly Euro 5 too—there is not much more benefit to air quality coming out from improving the standard of fuel. What that would ultimately mean, as I said, is 10 ppm of sulfur in diesel from 2009, which we certainly support. We have yet to be convinced of the need for petrol to go to 10 ppm of sulfur in petrol. That depends upon the engine technology and we have yet to see it put in place. We certainly support a move to 50 ppm of sulfur in petrol for premium petrol. There is no need to do it for the base fuel at present because the current car fleet cannot use high grades. Where we are heading to is probably clean fuels.

We have also analysed the relative benefits or performance of the 2009 fuels against biofuels, LPG, CNG and so on. In our view, by the time you get to those standards of fuel there is in fact not much difference. There are a few positives and a few negatives on each of them. We are certainly confident that by about 2009-10, we will have a sterling performance in terms of fuel standards, whether it is biofuels or standard fuels.

**Senator CHAPMAN**—I have one question. Do you believe that the regulations provide sufficient flexibility to potentially add in a timely manner additional alternative fuels?

**Mr Macpherson**—Our stance on both ethanol and biodiesel is that we fully recognise the government’s targets in this respect and we would be working hard to put that in place. I think Mr Bob Gordon mentioned the working group on confidence building. We have been fully involved in that. We are currently producing an AIP guideline, endorsed by the ABA, on storage and handling of ethanol fuels. Caltex and BP also have been involved at times in trials of ethanol. We certainly see this as an ongoing process. The key points are, firstly, to build confidence in the consumer. We have certainly made a promising start in that one. From our point of view, the key thing was to get in place a cap on ethanol blends which is in line with what is recommended by the vehicle manufacturers, and they say 10 per cent. I think that was a major step.

We think labelling is a major step required as well, for consumer information. We certainly found at the start of this year that a large number of motorists were fronting up to console operators at service stations and asking questions about ethanol which, quite frankly, those people are not capable of answering. Some companies, not all, decided to put in place those 'No ethanol' signs. So we think the first step is to rebuild confidence. Secondly, supply must be reliable on a long-term basis. Finally, it must be competitive in price. How the five years matches into that I cannot tell you, particularly on the last point. We are not producers of ethanol, so really I think Mr Bob Gordon is better served to answer that question, but as it stands at present with current oil prices we certainly think they will need assistance for a fair period of time. Whether it is five years I just cannot tell you.

**CHAIR**—As there are no further questions, thank you very much, Mr Macpherson.

[5.48 p.m.]

**ELLIOTT, Mr William Raymond, Spokesman, Australian Coalition for Ethanol; and Ethanol Project Manager, Dalby Bio-Refinery Ltd**

**HARRISON, Mr Christopher, Spokesman, Australian Coalition for Ethanol; and Director, Dalby Bio-Refinery Ltd**

**CHAIR**—Welcome. Is there anything further you would like to say about the capacity in which you appear today?

**Mr Elliott**—I am a spokesman for the Australian Coalition for Ethanol, which is a grouping of about 50 local government organisations, chambers of commerce, ethanol proponents and independent fuel organisations, overwhelmingly in Queensland. I am also the project manager for the Dalby bio-refinery.

**CHAIR**—Would either of you gentleman like to make a short opening statement?

**Mr Harrison**—Thank you for the opportunity. I will be brief. As I have previously said, we are here as spokespeople for the Australian Coalition for Ethanol but unashamedly we also represent Dalby Bio-refinery. We will try to talk on an industry basis but on anything specific we will be talking about Dalby Bio-refinery. We have worked with most of the major proponents and we believe that our project, if not the most advanced, is certainly up there with the most advanced, and I think that when we talk about the needs and requirements for the Dalby Bio-refinery we generally talk about the needs for the industry.

We have taken a fair bit of time on our presentation, and our covering letter pretty well states our case. We have listed the journey so far—the steps we have taken, and where we and the industry find ourselves. We ask that this legislation not go through, probably for slightly different reasons from what we have heard so far. We believe that the announcement made in the budget—the five by five offer—will not allow renewable fuels to go forward. The five years is totally inadequate for any investment in Australia. The second part is a little difficult because we do not know what the final excise is on renewable fuels, so it is very hard to say whether post 2008 we will have a viable industry. But, having been involved in the energy task force—I spent what seems like a lifetime in Canberra talking to whomever would listen to us—it would seem that the final excise on renewables will be energy based, probably with very little offset. On that basis it will not be sufficient to go forward. What we are saying is that enabling legislation that allows the five by five package to happen will not allow a renewable fuel industry to go forward.

**CHAIR**—Mr Elliott, do you want to add anything?

**Mr Elliott**—No.

**Senator STEPHENS**—Thank you, gentlemen, for your presentation. It is quite comprehensive. I want to be quite clear. In your submission you said:

All projects are currently unable to proceed due to the current uncertainty and will not proceed if the excise base foreshadowed in this year's budget is not implemented.

Is that because of the delay in passing the legislation or is it to do with the issue around ethanol?

**Mr Harrison**—It is really to do with our not knowing the final excise rate. We do not have enough information to go forward—and we do not have enough information to pull the pin, to be perfectly honest—because there is an outside chance that that final excise will demonstrate the benefits that we spent months trying to convince people of. The government policy in late 2001 said that renewable fuels would have a zero excise, but I do not think by any yardstick you could say that the announcement in the budget reflects that. So we have a five-year window to 2008, and it is rapidly reducing. It is not five years anymore. Five years will not allow investment. If that final excise is on a straight energy basis, which it seems that it will be, it will not be an environment that you can invest in post 2008 either. We have tried to provide some financials and our assumptions to demonstrate that simply will not work.

**Mr Elliott**—We speak also on the basis of some of the other proponents, particularly the proponents that have a Queensland element in their proposals. They have also said the same thing. Multiplex said that their proposal cannot go ahead on the existing basis. CSR have already made it clear in letters that are in the public domain that, under what was proposed in the budget, they would not put a single dollar into ethanol even into their fully depreciated plant in Sarina much less the plant they are planning to build in the Burdekin. That has been communicated pretty widely.

We are disappointed because we were in the situation of having gone to tender for the Dalby plant in November last year, and we had to put it on hold in February this year when the banks came back seeking certainty from the government, following the withdrawal of BP from their trials. Up until then we had seen it as having a strong element of certainty. There was a very well prepared and laid out policy on biofuels for cleaner transport at the last election. In fact, I would have to say that, up until 12 months ago, we used to use it actively and hand it out as a demonstration of the benefits of the industry, because it is a well prepared policy.

Unfortunately, what is in the budget has moved a long way from that policy. We went forward on the basis of that policy but, acknowledging that promises at elections sometimes are not all they seem, we got a commitment from the relevant minister that the policy would be implemented and that a zero excise would be maintained and we went ahead and spent a considerable amount of money preparing to go forward with construction. This is a \$79 million project. Its direct employment is not high—it is 34. But, in a town like Dalby, that is significant. It involves 186 permanent indirect jobs and about 465 jobs in the construction over a period of a little more than 12 months. So it makes a significant impact in a regional area. That is the same for other ethanol projects. They all involve similar amounts of money and make a considerable impact in regional areas. There are not many developments that you can say really impact in the regional areas as opposed to the cities. These do not work in major cities; they do work in regional towns in sugar areas and grain areas.

**Senator STEPHENS**—I note and understand, then, your concern about the uncertainty and obviously the regional benefits of the program. The several stages that you outline provide a strong argument. When the whole ethanol issue blew up around the Manildra proposal, there was quite a lot of information provided, particularly from the feed industries, about the raw materials that would go into this expanded ethanol industry and production. Do

you have any comments about the availability of the feed stock? To what extent has that been factored into your proposal—for example, the estimated cost of importing feed stock?

**Mr Elliott**—Speaking for the Dalby project, we see that there is an adequate supply of grain in the Darling Downs area. In fact, even when there has been a very poor year, sorghum has been exported out of the port of Brisbane in quite considerable quantities—more than we would require. We have been working with a lot of the grain traders to try to stop a lot of those exports and to take product that would otherwise be exported to Japan and elsewhere.

The reason that is exported is that the feedlotter and others who are normally the users of a lot of that grain are unable to provide long-term commitments to take grain. Because we are building a plant that will run for around 360 days a year and we will use the same amount of product month in and month out for 20 years or more, we have the capacity to commit to taking grain over a long period of time and to do forward contracts. Until we had to put the project on hold earlier this year, we were actively canvassing six-year price contracts, with an escalator year by year, in our contracts with farmers, and we were hoping to sign up about 25 per cent of our grain supply with farmers in that way.

I think there is a lot of misinformation on the attitude of the feedlotter. We have five of the major feedlotter in the Dalby area who have given us letters of support. Far from being opposed to what we are doing, they have actively supported it. A new feedlotter recently presented to the Dalby Chamber of Commerce and the Dalby council and, when they were asked whether they had any concerns about the ethanol project, they said that they saw it as having absolutely no impact on them. In part, that is because the by-product of the project—high-protein distillers grain—is very much in demand for animal feeding.

In the US, where they are moving to the renewable fuel standards—which will, in effect, require, by 2012, 10 per cent ethanol in probably 80 per cent or so of all the gasoline used in the US—Senator Harkin, when he was the chairman of the Senate agriculture committee, asked the US Department of Agriculture to look into the effect on meat production pricing. They found that it had a neutral effect on feedlots for beef production but actually had the effect of reducing the cost of production of poultry and pork because it supplied a lot of high-protein meal.

In Australia we import most of our protein meal from the US. In fact, last year, 403,000 tonnes were imported on the east coast of Australia, plus other amounts from other areas. So we have a deficit in that high-protein feed and it would be well received. That is why we are getting support from a lot of the local feedlots that have the opportunity to access that product should we be able to proceed.

**Senator STEPHENS**—I have one final question. You make it very clear that the projects are not able to proceed, and will not proceed, unless there is some certainty. How long can you wait?

**Mr Harrison**—Not long. We have been treading this course since September last year. Decisions were going to be made late last year, earlier this year, prior to the budget and in the budget. We have now had the budget and, in my opinion, the budget announcement actually created more questions than provided answers. We are a family company and we cannot

continue the expenditure that we have incurred over the last 24 months, and particularly in the last 12 months, for much longer.

**CHAIR**—Following on from that last answer, if you wind back to when the policy was announced—we have heard your misgivings about the policy and the commercial difficulties which it presents to you—if you had a blank sheet of paper and you could start again, what would be the principal policy adjustments or changes that you would contend for—in summary and in some sort of order of priority?

**Mr Harrison**—I do not know that we would change a lot. I think the government announcement and the work we did at that point in time to get comfort that that was what was going to happen, I do not think anyone could do much more. We have read the *Biofuels for cleaner transport* document 1,000 times and we have had some of the best minds in Australia look at it. I fail to see how you could come up with any other interpretation than what we have in our presentation. I have to be honest, I think there has been a shocking lack of leadership on this. I think there has been point scoring from both the government and the opposition. To put a policy like that out, I would like to have seen some leadership. I would like to have seen the federal government actually running some vehicles on biodiesel and ethanol. It would have been very easy to do, to get it on the right-hand side of the page and do what they said they wanted to do and make this industry happen, instead of allowing it to lurch from disaster to disaster as it has over last 12 months.

**CHAIR**—Is the biggest issue the five by five excise?

**Mr Harrison**—It is. We started this journey believing that ethanol and renewable fuels would remain excise exempt. When it became apparent that that was not going to happen, through what was called the Brazilian import in September last year, we realised that we could not go right back to the status quo, so we said, ‘If we cannot have the intent of the policy then we have to at least put a minimum on that.’ It was pretty simple. With any of the lending authorities in Australia, you need 10-year certainty. Ewen alluded to it before. He does not know what the time period is, but it is pretty simple maths. At about \$22 and \$23 a barrel, this industry needs support. At some other figure it does not. To come out in the budget and put a line in the sand and say, ‘We want a renewable fuels industry; but, in five years time—whether the sky is falling in or the planet is tilted on its axis—you are going to pay this sort of excise,’ says to me that you do not want a renewable fuels industry; they just do not mesh.

**CHAIR**—Your evidence to us is that the economics of the five by five phase will not stack up.

**Mr Harrison**—Exactly.

**CHAIR**—There is a division. We will have to suspend the hearing.

**Proceedings suspended from 6.05 p.m. to 6.14 p.m.**

**CHAIR**—Sorry, Mr Elliott, please continue.

**Mr Elliott**—Going back, we had gone ahead on the basis of the policy at the last election. We saw that as a good basis. One of the things spelt out clearly in the *Biofuels for cleaner transport* policy why an ethanol or biofuels industry had not developed previously was the

uncertainty in investment. The policy identified the fact that there had not been any period of time put on the excise-free period and clearly enunciated the need for a commercial period to allow investments to go ahead. That is really the way we proceeded—based on the policy, on the zero excise and the subsequent commitment we got that that was going to be honoured, and the recognition in the policy that the requirement was for a commercial period to allow any constructor of a plant to get a return on capital and also for the banks to be able to lend to get their money back.

Regarding the reference Chris made on the \$23 a barrel, while clearly the price of oil is running much higher than that, \$22 to \$23 a barrel is the sort of level the banks are requiring that all investments be considered upon, and that is the basis that we have done all of our project work on.

**CHAIR**—Thank you.

**Senator ALLISON**—Mr Elliott, to clarify a point in relation to another submission, what, roughly, is likely to be the production cost of ethanol for you once your industry is up and running?

**Mr Elliott**—That is a moving target, frankly. To be able to answer that question is very difficult. Very roughly, something in the mid to high \$50s. That will decrease over time with technology, but, like any production, it depends on inputs. About 62 per cent of our costs for operating the plant are associated with the purchase of grain. We have used ABARE figures for the outlook for grain and graphed those forward but, like any outlook, they are fundamentally flawed, because somebody is looking at the past and trying to guess what the future is going to be.

In the same way, if you look at it from the other direction, one of the things the grain farmers say is, ‘What is our capacity to pay in terms of grain?’ You can only answer that in terms of what the oil prices are going to be. The reality is that we have tried to go ahead on the basis of what the banks are looking for, which also links in very clearly with what the Energy Information Agency, part of the US Department of Energy, says. They are probably the premier forecaster of long-term oil prices. The banks are picking up figures that are very close to those sorts of numbers. We have used that and we have used ABARE numbers looking back and then carrying those forward, looking at what they see as the future grain prices. We have used PricewaterhouseCoopers to do all our financials, which we believe are very robust. So we believe that the numbers we are working on are very accurate, well based and well analysed.

We have also communicated with other proponents—people like Multiplex, CSR and others, including Primary Energy. Primary Energy, for example, has a Gunnedah based plant proposed using identical technologies to those we are using. They have all come up with very similar cost structures. It is an interesting fact that, while there are some higher costs associated with producing from grain, that is offset by producing a high-value protein feed that is saleable. The sugar industry, perhaps, has a lower production cost but does not have a by-product that can also be sold. At the end of the day, the production cost for our plant and for most other plants coming from either sugar based feedstocks or grain based feedstocks are

relatively close to one another. That is associated with the fact that most of it is the primary commodity that you are working on.

**Senator ALLISON**—You have argued for a 10-year minimum effective excise-free period. Can you for the committee's sake describe where you think the industry from your point of view would be in five years with a five-year period and how different it might be in 10 years time with a 10-year period that would suggest that we need 10-year rather than a five-year period?

**Mr Elliott**—I think that if there were only a five-year excise-free period, there would be no more industry than there is at the moment. There would be no development of it because nobody could get a payback in a five-year period. Let us face it, at the moment the five years is from 1 July 2003, so by the time we build the plant—even if it were well advanced—and re-engage the banks and get all that squared away, it is probably going to be the best part of two years before we can commission. Other projects are well beyond that. CSR are suggesting for their Burdekin project that it will be three to 3½ years before they can commission, even if they get a favourable decision right at the moment. The advanced projects are somewhere in that sort of time frame. If you are talking about two years from now, you have only got three years or less of the excise-free period. There is no way anybody can get a payback on that.

As Chris said before, the situation we face at the moment is that there is not even enough information to properly walk away because we do not know what the final excise is proposed to be. If it is low, it might still be workable as long as it was for an extended period. We would argue for an effective 10-year excise-free period and then a phase-in of some form after that or at least a process that makes sense so that you are not going to a bank or asking investors to invest in something that is likely to be shut down after 10 years. No country town wants to have a big investment and then have it shut down again. Nobody wants to invest in anything like that.

**Senator ALLISON**—Speaking of country towns, are you sensing a disappointment in the area you have set up in from farmers and the community generally about this development, or are they not aware that there is such a risk?

**Mr Elliott**—They are very aware of it at the moment. In our area they see it as putting a floor under grain prices and taking some of the ups and downs out of prices and allowing them to manage their businesses. Certainly with the long-term grain prices that were operating until earlier this year when we had to put the project on hold, there was a lot of interest in being able to use it as a tool for managing their businesses. The other side of it is that in the Dalby area there is a lot of cotton grown as well, and a lot of cotton growers saw it for the first time as providing them with the ability to manage their grain production in the same way that they manage their cotton. With cotton they can go out and take futures contracts and plan five years ahead by committing their cotton; in grain, they have not been able to do that. By offering six-year contracts, which we were doing, they had the capacity to lock in the price in the way that they could lock in the price on cotton and to move away from cotton and have a greater amount of grain. It would have put it on the same business basis; whereas, at the moment they really cannot plan more than six or 12 months ahead, if that.

**Senator ALLISON**—You referred earlier to technology which might bring down the cost of producing ethanol in the future. Could I invite you to expand on that? It is my understanding that waste streams offer opportunities with by-products and so forth. Could you let the committee know what you see on the horizon in terms of technology?

**Mr Elliott**—The US industry now has 74 operating plants and, as Bob Gordon said before, they will produce about nine billion litres of ethanol, which is half the petrol produced in Australia. They will produce that amount this year. They are basically all in rural and regional communities throughout the USA. There was a big move to the biotechnology or the biorefinery concept of producing not only ethanol but also a range of other products. I personally see the opportunity for us and for other ethanol plants to become centres of rural chemistry. There are a lot of other things that can be produced—for example, we have thoughts of producing biodiesel in the future. With biodiesel there are a lot of mineral oils that get used as crop sprays. Those can be produced from vegetable oils that can be grown in rural areas. A lot of those are being imported from the US, Britain and parts of Europe at the moment because we are not producing those as clarified oils in Australia. So there is an opportunity, not just in Dalby but in towns right across regional areas of Australia, to enhance the skills base. I do not believe there is a lack of skills in country towns but they tend to be the same skills.

I think that in the US, where you have industry spread much more widely and not concentrated in two or three major capitals, you have got that much more interaction between the country and city and much more development of industry and chemical technology along the way. There is a big move towards a whole range of biotechnology projects to be linked in with ethanol plants—and, for that matter, biodiesel plants as well—and they are some of the opportunities we see for the future.

In terms of the technology, the US, particularly the Department of Agriculture but also the Department of Energy, has been funding a lot of research on driving down the costs of cellulosic enzymes to be able to convert cellulose into starch and then from starch into sugars. All fibres, whether in paper, bagasse, grass, whatever, are essentially lots of sugar atoms joined together. The US Department of Agriculture has just spent something like \$45 million over a three-year program to drive down tenfold the price of what are at the moment quite expensive enzymes to be able to convert cellulose. So looking down the track—and in practical terms we are probably talking at least 10 years before that, but something in that sort of time frame—you are going to start seeing that some of the fibre that comes in with the grain or the bagasse that comes in the sugar cane is going to be able to be converted into ethanol itself.

At a conference that was held last year we sponsored somebody from the Natural Renewable Energy Laboratory in the US to come over here. At the conference in the US they had done a lot of work on sugar bagasse and found that it was the most attractive source of conversion of cellulose into ethanol—much more so than corn. If you are based in the US and you are sitting in a corn state, that is the wrong answer to come out of your research, but that was the reality of it. They see bagasse in the future, probably in the 10-year time frame, and converting the bagasse into a combination of ethanol from the cellulose, with the lignons that provide the energy that they burn at the moment still there and available for burning. It was

expressed as a case of having your cake and eating it too. So there are a lot of different changes that concur.

Finally, running from that, it fits well into a future hydrogen economy. In fact I saw a quote just a couple of days ago from the chief research scientist of Volkswagen. Volkswagen's policy is that they believe that the future of fuels is into hydrogen—hydrogen for fuel cells—but they are very emphatic in saying that it has to come from renewable sources. There is no point in going ahead with a hydrogen economy if you are not doing it from a renewable base. That is where we see ethanol fitting in, because ethanol has a high ratio of hydrogen in it. There are a number of fuel cells already on the market that can convert ethanol into hydrogen and you can therefore use the sunk costs in terms of logistics and in terms of fuel stations. You do not have to put a lot of investment into—

**Senator ALLISON**—Are you saying that you can use ethanol in hydrogen fuel cells? The cells themselves converted to—

**Mr Elliott**—Yes. The preferred method at the moment is either methanol or ethanol because of the high ratio. Otherwise you have got to have a lot of investment in actually producing hydrogen and holding hydrogen close to the site. They are even now selling in the US some ethanol based fuel cell where you actually put ethanol in and it can charge your batteries on your laptop. In fact it has just been approved for use in aircraft in the US. You can recharge your batteries in-flight by using a fuel cell powered by ethanol. It is on sale right at the moment. There has been a lot work done in the US on exactly that. Therefore you come up with a renewable hydrogen economy to meet that sort of standard. But that is looking at 20 years or more.

**Mr Harrison**—It is actually one of the cornerstones of the Renewable Fuels Association of America: exploring ethanol's relationship with hydrogen. It is one of the four or five major mandates.

**Senator ALLISON**—Coming back to 2003—

**Mr Elliott**—Sorry, I am going a little far ahead.

**Senator ALLISON**—it has been suggested in some submissions that we should be satisfied that our approach to cleaner fuels is about ultra low sulfur diesel and ultra low sulfur petrol. You may have already done this; if you have, do not answer the question. What advantages does an ethanol blend in fuel provide in terms of clean air?

**Mr Harrison**—I would answer that one very simply. I just go back to the government's policy of 2001. The benefits are clearly articulated. If you really thought ultra low sulphur diesel was the way forward, that information was available prior. Why on earth would you release that sort of policy?

**Mr Elliott**—In the US, for example, since the Clean Air Act of 1990, which was sponsored by George Bush Snr, they require in the major cities, in other words in the major pollution areas, the use of oxygenates in fuels. An oxygenate can be something like MTBE or ethanol. The reason you are doing that is that when you burn anything, whether it is out in the open or in the car, you need a fuel, an ignition source and oxygen. In the combustion of fuels in an automotive sense you are always short of oxygen. That is why you get a lot of the partly burnt

unstable components being thrown out, like carbon monoxide and others. If you put enough oxygen there you get a much more complete burn. You do not get unburnt hydrocarbons being ejected from the tailpipe. You get a more complete burn of the fuel that has been put in there. That is the advantage and that is why they have done it in the USA. They initially went with MTBE; they have subsequently found that there are issues associated with that and there is now a strong move towards ethanol. There is always a parallel process. Really you are trying to put oxygen in there to get a more complete burn. If we set fire to something right here you are not going to have a problem—there is plenty of oxygen. In your engine you do not have plenty of oxygen. That is the simple reason you use it. As a consequence you get far less pollution and all the health consequences that come from that.

**Senator ALLISON**—What currently is in use as an oxygenate?

**Mr Elliott**—We do not use oxygenates in Australia.

**Senator ALLISON**—When you put ethanol into petrol, what is it that you do not need to put in instead?

**Mr Elliott**—I am not sure it is a case of not needing to put in something. As the AIP said before, with the move to the 95 octane Australia is facing a double whammy effect. We are moving with our new Australian design rules to require a 95 octane, which is quite a demand for extra octane. At the same time, moving to the Euro 3, and in particular if we move to Euro 4, there is a big reduction in the allowable amount of aromatics. Traditionally in Australia we have got our octane boost from aromatics. If you are constraining the amount of aromatics that can be used in your fuels you have to find your octane from somewhere else. That is a big enough problem—just moving ahead with reducing your aromatics—but if you are also boosting your octane as a way of getting better fuel economy, which is prescribed under the new design rules, you have that double whammy effect.

I can really understand from the oil companies the need for an enormous amount of investment. As they have found in the US, using an oxygenate, and particularly using ethanol, has allowed a lot of oil companies to reduce, postpone or otherwise delay the requirement for investment and make a substantial contribution so they can produce a gasoline in US terms that has a lower octane component coming out of the refinery and then blend in ethanol to make the octane up to the final level.

**Senator ALLISON**—This might be a difficult question: why is it that petroleum companies are not embracing ethanol as an additive?

**Mr Elliott**—I think Ewen laid that out. I can understand a certain caution but I think his comments—I hope I quote him correctly—were that there was the need for an assured supply and the need for competition. Unless a renewable fuels industry develops, which means really an environment that allows new producers like us, other members of the Australian Coalition for Ethanol and other proponents around the country to proceed with those, we are not going to have a competitive situation and we are not going to have a guaranteed supply. I do not know that there is as big a gap between ethanol proponents and the oil companies as some people might suggest. I think that, like a lot of these things, there is sometimes a perceived gap and when people start to talk to each other then there is a lot more common ground. Certainly at the moment it seems like there is a gap. It does not have to be there.

**Mr Harrison**—The lack of the final excise also impacts on that because, as an ethanol proponent but also as a fuel marketer, a major oil company or another large independent, I cannot do a contract with a customer at the moment because I cannot tell them what the price of ethanol will be because I do not know what the final excise will be.

**Mr Elliott**—The other thing I was going to say is that out of our total production, which is 80 million litres, we actually presigned contracts prior to the budget—well before the budget. We signed contracts for 65 million litres on a five-year take-or-pay agreement. We are in a good position. We did not go to the major oil companies. We saw the opportunity to work with some of the independents, primarily in Queensland. We had our market in place. Of course, those contracts were dependent on the excise environment prevailing at the time they were signed, so at the moment they are very much in question, but they are take-or-pay contracts, very solid contracts which were well regarded by the banks, which is why we got a good response from the banks until the perception was that there was a change in government policy occurring.

**Senator ALLISON**—You point out that there is a serious loss of confidence in ethanol blended petrol. What would you like to see the government do to restore confidence or do you think it is a job for your industry to tackle alone?

**Mr Harrison**—With the greatest respect, I think the industry is so battered, and we have spent so much, that it is very hard at the moment to pull your socks up and go out and do some positive consumer confidence building. Most of us here have participated in the ethanol confidence-building and labelling workshop or committee that was formed just after the budget. I would have to be brutally frank and say that I do not think that has achieved a hell of a lot. I thought we were there to build confidence and try to go forward, but what I think we have actually done is try to please everyone in the room. That is not building confidence in trying to go forward. I think I started to answer Senator Brandis before when I said that, if the government announces a policy saying it wants a renewable fuel industry in Australia, it needs to demonstrate that faith. A very obvious way would be for the huge federal fleet to start to use some serious quantities of biodiesel and some ethanol—for the government to get behind it and say, ‘This is what we want to happen.’ If I was in their position, that is exactly what I would do.

**Senator ALLISON**—Finally, if there is time, do you have a comment on labelling that you have not already made?

**Mr Harrison**—We would endorse what the ABA said. In relation to the level of labelling that has been suggested, the proponents and the producers have tried to be proactive and tried to support it. I know I speak for them all when I say that we think the labelling is, frankly, a nonsense. It was done and dusted internationally 10 or 15 years ago.

**Mr Elliott**—If I could add to that, we had Larry Johnson out here recently. He has been involved for more than 20 years in the US and developed the ethanol industry in the US. He drew those direct parallels—the no-ethanol signs and things that went up. One of the ways they solved that issue was to get everybody around the table and come up with positive ethanol signs—‘10 per cent ethanol in your fuel for cleaner air’ and those sorts of positive

responses. They were still labelling, but giving it in a positive frame rather than a legalistic type frame.

**Senator ALLISON**—‘Guaranteed no ethanol’?

**Mr Elliott**—‘Ten per cent ethanol to support your community’ and things like that in the farming communities. There can be that sort of flexibility. But in the US there are now no states that require the labelling of E10. The last state that mandated the labelling was South Carolina, and between three and four months ago they removed that requirement. They were the last ones to require it. Some places, like Nebraska, mark it as E10, but that is a voluntary program. Iowa does it the same way. Minnesota, which is one of the biggest states, does not have any labelling at all for it; it just mandates it as 10 per cent, and that is what happens.

**CHAIR**—Thank you.

[6.39 p.m.]

**NEILSEN, Mr Warring John, Manager, Corporate Affairs, Elgas Ltd**

**NORTH, Mr Raymond, General Manager, Australian Liquefied Petroleum Gas Association**

**CHAIR**—If either or both of you would care to make a brief opening statement, please feel free to do so.

**Mr North**—I appear here to represent the interests of the members of the Australian Liquefied Petroleum Gas Association, the major Australian liquefied petroleum gas producers, distributors, marketers, service companies, wholesalers and retailers.

**Mr Neilsen**—I am here to represent just Elgas.

**CHAIR**—Welcome. The committee has before it submissions from each of your organisations or in your case, Mr Neilsen, your company. Would you each like to make an opening statement?

**Mr North**—Our purpose in making a submission to the committee was to enable us to participate and draw the committee's attention to the interrelationship of the legislation that you are reviewing with a wider policy framework for alternative transport fuels. We are pursuing a dialogue with government in asking you to reconsider the imposition of excise on LPG in combustion engines specifically for automotive use. We believe there is a strong case to be represented there. Australia is self-sufficient in LPG and the use of LPG has been encouraged by government for 25 years as a clean, environmentally beneficial fuel compared to some of the other alternatives. Australians have been encouraged by government to use LPG as an automotive fuel, and it seems incorrect to us to have a policy initiative which then penalises that.

There could be an impact on jobs in Australia. The LPG business is about 60 per cent LPG used as an automotive fuel and 40 per cent used in what we term traditional use—as a heating source and as a source of power in remote areas, and in agriculture and in industry. Even though the proposed excise will not be introduced until 2008, and then progressively, the impact on the industry has been profound. Automotive manufacturers are noticing fleet managers and large fleet owners cutting back on orders for LPG powered cars because of the uncertainty. Even though the government has been quite honourable in its commitment in giving industry five years notice, which it said it would always do, it did come as a bolt out of the blue. It is having an impact on consumers, both in the traditional and autogas areas, who do not understand that the excise would only be applied to internal combustion engines, although that still needs clarification that it will only be internal combustion engines in the automotive sector. Flow-on could be wide in rural and regional Australia. There are over one million people in rural and regional Australia who depend on LPG as an alternative fuel. It is a traditional fuel and the use of LPG is quite widespread as an automotive fuel in rural and regional areas—particularly in Victoria.

The LPG industry would like to ask government to consider an excise of no more than 8c a litre and a capital cost reimbursement of \$1,200 over a period of time, which would enable us

to put into process the plans that we had before the announcement was made to develop the autogas industry in conjunction with the automotive manufacturers.

We also would like to draw the attention of the committee to the opportunity to use the Energy Grants (Credits) Scheme. The Australian taxi industry will be representing the government separately on this, but there is an opportunity to use that mechanism to promote the use in the commercial sector of LPG as an automotive fuel. The recommendation there would be to extend that type of encouragement down to vehicles of below 4.5 tonnes gross vehicle mass. In summary, that is the interest that we have in putting some of those facts before your committee in the context of a policy review in alternative fuels.

**CHAIR**—Thank you, Mr North. Mr Neilsen, would you like to make a statement?

**Mr Neilsen**—Yes, I will. On the basis of the Elgas being the largest single purpose marketer in LPG, our company has taken a fairly committed approach to LPG and in recent times we have completed a \$200 million underground gas cavern at Port Botany. Mainly that was to ensure longevity, security of supply, for the growth of the industry, in particular the autogas industry. We also operate probably one of the largest independent networks of auto sites throughout Australia—with Kleenheat we have a joint venture called Unigas—and therefore we have quite a significant interest in the viability of the industry.

I would like to make a couple of points from our perspective. The alternative fuel industry needs government support. When you have another fuel, which is a niche market fuel, consumers need to have confidence in the fuel and they need to have an incentive to buy the fuel. Unless they have both those things, you will find that consumers do not take action and buy it. The whole mechanism out there is to encourage people to take up an alternative fuel that delivers environmental benefits and other benefits to this country. They need to have some incentive to do that. Without that incentive, they will not do it. They will simply drift back to the traditional fuels of petrol and diesel.

Therefore, we are keen to develop the argument. It concerns us that on the one hand we talk about cleaner fuels and yet on the other hand we tax probably one of the cleanest fuels around, which is LPG. The mechanism and the way that has been approached are basically spelling the death of our industry. While we wait for an excise level to be announced, our industry is dying quite rapidly. It is no good having an announcement of an excise that does not work because either way we will die.

**Senator STEPHENS**—Thank you for your submissions. They are a fairly profound warning to us of the situation in your industry. Mr North, you said in your submission that there was no consultation with the industry prior to the announcement in the budget.

**Mr North**—That is correct. The industry had had an engagement with government officials following the release of the results of the fuel tax inquiry—the so-called Trebeck report—but we had had no contact at all prior to the budget with government concerning the excise announcement. It came as a surprise because the industry had commenced a lot of the developmental work that I mentioned following the Trebeck report and, indeed, had set up an industry development fund to promote, with the automotive manufacturers, the new dedicated LPG engine vehicles which were becoming available. The major industry players had made significant contributions to that fund. It was going to be a separate company with separate

staffing, and all that was thrown into disarray and has been on the backburner since, figuratively speaking.

We did have the opportunity to engage the energy review task force secretariat when that was announced, and we were aware, because the Prime Minister had made the announcement, that the energy policy area was going to be looked at. On 5 March we went to see the energy review task force secretariat, and I have to say we have had very good discussions with them and we were able to bring a lot of information to the table concerning the benefits to the community of using LPG as an automotive fuel. We did recognise and learn at the time that there many other items that the task force were considering as well. Whilst LPG and autogas are very dear to our hearts, they were one of a constellation of factors that were being considered by the task force and indeed by government.

**Senator STEPHENS**—In your submission you say that there are about half a million vehicles fuelled by LPG at the moment. Are you able to quantify some of the comments that you have made about the immediately adverse impact on the industry? For example, you mentioned the cancellation of vehicle orders and a reduction in the resale value of vehicles. Can you tell us what the impact is on the industry in some kind of quantitative terms?

**Mr North**—I can quote you some instances, but I cannot recall specific companies. As Mr Neilsen said, in the fleet management business the business case for using LPG as an automotive fuel depends on two factors, including the economies that are achieved by the fuel compared with other fuels times the mileage that the vehicle does. The payback of the extra margin could be \$1,200 or \$1,400 to have that vehicle either factory fitted or retrofitted. Most fleet vehicles are leased, and that has an impact on the residual. The residuals for the vehicles at the end of a lease period were forecast to fall by as much as 20 per cent, which could be \$3,000 or \$4,000, so fleet owners and fleet leasers put their decisions on hold. I heard of one fleet of 3½ thousand vehicles, and even state government fleets, where moves had been in play for some time to have a clean automotive policy. Those decisions were deferred, and they await the announcement by government of the level of excise. That determines the economies of running the vehicle daily and the payback of the original cost of the equipment.

That then flowed through to the major automotive manufacturers. They would be better able to tell you than I am about the impact on their business, but the recent move of a company called APA—one of our members—into voluntary administration, which you would have read about, was caused by a decline in forward orders from the major car manufacturers for automotive cylinders or tanks, which was caused by a direct flow of uncertainty in the fleet business back through to the automotive manufacturers and then back to APA. There are companies in the industry who are fielding some effects of component manufacturers at this stage. I am sorry that I cannot quantify it in dollar terms for you, but it has been quite marked.

**Senator STEPHENS**—So the thrust of your argument from both of your submissions is that you both believe that your industry has been indiscriminately lumped in with the other fuels for taxation purposes. Is that the gist of it?

**Mr North**—I think so.

**Senator STEPHENS**—The suggestion is that, because your fuel has economic, environmental and social benefits, these need to be factored in. You mentioned several

different reports in your submissions. Is there somewhere that you can point us to that demonstrates some of those social, economic and environmental benefits of LPG over other fuels?

**Mr North**—Yes. I think the best one there would be the so-called Anyon paper, which is a spiral-bound book with our submission. That does have some quite interesting information on some of the environmental benefits compared with other alternative automotive fuels—not alternative fuels as such but alternatives to LPG, such as ultra low sulfur petrol and ultra low sulfur diesel. Those two products are quite efficient in greenhouse gas reduction but, compared with LPG, there are significant benefits. There are fewer oxides of nitrogen, fewer hydrocarbons and fewer particulates in particular compared with diesel—even ultra low sulfur diesel—and less carbon monoxide. On page 5, there is a rather extensive matrix showing a little more detail on some of the benefits that each of the fuels has on a comparative basis, looking at urban air pollution, global warming, greenhouse gases, engine noise, applications and availability. That would be the most up-to-date data we have. We provided this data to the task force secretariat, and it updated the latest information from Europe and some further information we had here from the CSIRO.

**Senator STEPHENS**—Having provided it to the task force, what has the government's response been to your submission?

**Mr North**—Our understanding from the task force is that the information that we provided has gone into their deliberations and been passed on to government—and indeed from the task force secretariat to the task force itself who, we understand, report periodically to the cabinet and to the cabinet energy committee. We have heard, from some of the questions that we have been asked in follow-up to that material we have submitted, that it has been taken into consideration.

**Senator STEPHENS**—You suggest in your submissions that the alternative transport fuels industry does need government assistance to survive. You suggest that 8c a litre and a \$1,200 rebate is the level of assistance that is required to sustain the industry. Is that right?

**Mr North**—Yes.

**Senator STEPHENS**—Do you see a date or a time when the industry might not need that level of assistance?

**Mr North**—We did not put a time on our submission. We had been thinking in the time frame that the government had been working to with full introduction of the excise. But we see a case for autogas—LPG—as an automotive fuel being treated like that for the foreseeable future. We did not put a time line on it. One of the reasons for that is that other countries around the world that provide varying types of support for LPG as an automotive fuel do not do that either, because the ongoing problems of pollution in the major cities and greenhouse gas reduction are things which, whilst they have time bound milestones and targets, are there as part of the environmental management policies of those governments and those countries. We would like to see the same treatment of autogas in Australia.

**Senator STEPHENS**—So you are saying that there are no horizons for industry support in other countries?

**Mr North**—Warring may be able to comment on that.

**Mr Neilsen**—For the vehicle manufacturer, the cost of making an alternative fuel vehicle for LPG and the technology cost for meeting the 2003 and 2004 and those sorts of emission standards have to equate to the general public—that is, whether or not they are interested in buying the vehicle. As you have heard here today, the whole mechanism that makes things work is the public—whether or not they want to buy the product. If there is no interest in buying the product, the product will not sell. The vehicle manufacturer has to be sure that people want to buy what he makes. Therefore, there has to be a reason for them to buy it. So, in terms of a time frame, I guess it depends on how broad the vehicle becomes in the fuel selection. At the moment, LPG is roughly around 8 per cent of transport fuels. We see that as only taking up to 10 per cent. We see that as being a critical niche segment of the transport fuels which gives some sort of security and risk management, because you have a suite of fuels to handle environment issues and supply issues. I think that is probably the critical focus.

**Senator STEPHENS**—Mr North, you make the point on page 5 of your submission that autogas is at catastrophic risk as an industry and as a fuel alternative if the government's proposed excise tax changes proceed. Is that not overstating the issue?

**Mr North**—No. I think the word 'catastrophic' was advisedly used. The industry is really poised now, waiting for the announcement. We hope the announcement will be one which will enable the industry to continue to play the part it has played to date. If the announcement is not one which enables the industry to continue to grow—and we are looking to grow at about 65,000 LP-gas powered vehicles a year; that was the target of the industry development fund we set up—then the industry, in autogas terms, would fade away.

**Senator STEPHENS**—I would like to get your perspective, Mr Neilsen. Mr North's submission suggests that autogas is an integral part of the entire LPG industry and essential to its viability in making clean gaseous energy available to one million householders. This is the 80-20 proportion of autogas as part of the alternative fuel industry.

**Mr Neilsen**—One of the issues we have is that 70 per cent of our users are in regional and country Australia. The autogas market provides the level of loading of the infrastructure, so we get economies of scale. The demise of the autogas industry will simply impose costs on traditional business. We would see that increasing the costs to the consumers who reside in regional Australia.

**Senator STEPHENS**—Mr Neilsen, you make the comment in your submission that if the autogas market is allowed to collapse we will be putting all our policy eggs into the diesel basket. That is a fairly clear statement about what we are really looking at happening, isn't it? And if consumers reject it where do we go to from there?

**Mr Neilsen**—I made that statement because of consumer confidence. We have spent 25 years or so getting people to have the confidence to take on LPG. You have seen what confidence there has been with ethanol. We are looking to go to hydrogen fuels in the future. To my way of thinking, if you destroy that sort of confidence and the ability of people to feel that they can switch to a fuel if someone is supporting it—like a government policy—and it suddenly disappears, I think it will be extraordinarily difficult to get other alternative fuels up.

I think there is a clear message here for government: you must remain fairly constant and make sure you keep the confidence of consumers. Once they change, they do not come back. That is our experience.

**Senator ALLISON**—Mr North, in your submission you make the point that LPG autogas produces up to 15 per cent less carbon dioxide than petrol fuelled counterparts. Have you done any figures on what would happen vis-a-vis the so-called assistance to alternative fuels, and to your fuel in particular, if there were a carbon tax or carbon levy—as has been proposed at various times—of, say, \$10 per tonne, which would be a fairly low rate? Would you see parity being achieved in terms of benefits of the fuel compared with petrol and the dollar attached to that?

**Mr Neilsen**—Perhaps I might answer that.

**Mr North**—It is a difficult one to answer.

**Mr Neilsen**—I think the answer to that, Senator, is that we have just started to look quite seriously at the carbon area because we can see that debate becoming more profiled, I guess. At this stage we do not have a position on that carbon tax or where that should be. It is something we have just started to engage in—

**Senator ALLISON**—I am not asking whether you are in favour of a carbon tax or levy. I am simply saying that, if we talk about assistance to your industry, this government is, through its greenhouse gas abatement program, paying roughly \$10 a tonne for abatement. If that were applied to your industry as it is to many other industries at the present time, I am wondering about the mathematics: would it make up for what has been described just now as assistance to your industry? Would that in fact be justifiable on the basis of greenhouse?

**Mr Neilsen**—I do not think \$10 would be sufficient.

**Senator ALLISON**—Have you put a dollar value on the environment benefits? You mention reductions: 80 per cent less air toxics—for instance, benzene, butadiene; 60 per cent less carbon monoxide; 50 per cent less particulates; 33 per cent less oxides of nitrogen et cetera. If you were to put a dollar value on that, would that combined with greenhouse make a difference?

**Mr Neilsen**—We did have Access Economics do a study for us based on greenhouse abatement. That was looking at tax efficiency. That study clearly showed the forgone excise on LPG neutralised, based on the greenhouse gas abatement, but that is on a tax efficiency basis.

**Senator ALLISON**—I understand. I have heard it occasionally said that if the market goes from Australia for LPG it will not make any difference because a third of your product is sold overseas and you would just simply sell 100 per cent instead of that third. Apart from what we have just been discussing with regard to greenhouse and air quality benefits, what difference would it make if LPG was to go entirely offshore?

**Mr Neilsen**—I guess basically what you are saying is: why don't we export all of our LPG? Certainly it is an economic benefit to the country, but there are some negatives to that. The negatives are that we actually lose an alternative fuel industry in this country and we have the immediate problem of impacting on the environment, because we are already getting

greenhouse benefits straight away at the moment and we would see that just disappear. I think there is a concern in Europe and Asia that the proliferation of diesel is causing an issue in city areas in terms of air quality. Quite honestly, I think that ignoring the benefits of LPG as a transport fuel addressing both greenhouse and air quality will just mean that this country will delay addressing those issues, as new technologies will take a lot longer to address those areas. I guess what you are looking at is a bit like a succession of technology, because if you simply want to destroy an advantage that you have currently and just export it then you will be importing other fuels to replace it. So on the one hand you are exporting LPG and on the other you are importing diesel or petrol to make up the difference. That would be my comment on it.

**Senator ALLISON**—You spoke earlier about the need for infrastructure supporting autogas to not subsidise but at least make affordable gas which is used in heating and cooking and also in rural industries. Can you indicate to the committee, firstly, what kinds of rural industries use LPG and, secondly, where you think the availability of LPG would disappear in country areas? Is it remote areas that it would not be possible to service? What would we be looking at in the loss of an energy source for country people?

**Mr North**—LPG is quite extensively used in intensive livestock production; in agriculture, in grain drying; and in meat production, as a power source for the meat-processing works. One of the reasons for that is related to the cleanliness of the product. Ultimately those products end up in the food chain, and you need to avoid any possible contamination in the production process. As most of those processes are base agriculture production processes, there is the possibility for contamination if the fuel used is not appropriate. Also, LPG is certainly used for remote power generation.

**Senator ALLISON**—The alternative would be diesel?

**Mr North**—That is right. There would not be a natural gas pipeline passing by some of these areas. In areas where there is not a natural gas pipeline—like in coastal areas or in areas where it is not economic to reticulate natural gas—LP gas would be used. For instance, there are older suburbs in Sydney where natural gas is reticulated, yet in another area only a kilometre away, where it is just not economically feasible to put a pipe through sandstone, underwater or through some other obstacle to reticulate natural gas into new homes, they rely on LPG. It is quite widespread.

**Mr Neilsen**—Perhaps I could add to that. With regard to what would happen to some of the remote areas, the other issue is that LPG provides gas to those who cannot get natural gas. It is another source of energy for their use. LPG would become uneconomical for those households. We could certainly get it to them but it would be at a cost and then we would see a growing reliance on electricity. That would lead to a couple of issues: the first is the pressure on the grid system and the second is the increase in greenhouse gas. Those are the fundamental trends that would occur.

**Senator ALLISON**—Generally speaking, the excise being applied to alternative fuels has been said by some to be about getting rid of inefficient fuels. Do you regard the industry as inefficient? Are there efficiencies to be gained some time down the track? Could you comment on that statement?

**Mr North**—I have not heard that comment. We have heard that the industry has been operating for 25 years and has not assumed a high enough profile in representing the industry on some of the issues that the senators have questioned us about here this afternoon. I am not aware of any particular efficiency gains that could occur. The LP gas industry utilises all the efficiencies which are available in terms of distribution, storage and production, and those are ultimately passed on to the consumers. There are matters on which we get questioned in terms of pricing, which are largely due to throughput in tonnage in a particular site. For instance, a city site might turn over 400 tonnes of autogas and a site in the bush might turn over 80 tonnes with the same capital investment needed. That is why you would pay more for autogas in Karratha, for instance, than you would pay in a suburb of Sydney or Melbourne. But I think the industry is efficient. The comment I had heard was that we were hiding our light under a bushel and needed to get out, be real and promote the industry, which we were doing prior to the announcement.

**Senator ALLISON**—I have one other quick question. I was surprised—I think it was in your submission, Mr North—to see that a large market is with retirees. Can you explain why it is that retirees have chosen LPG to fuel their vehicles?

**Mr North**—They have become retirees since they first had their car converted to autogas.

**Senator ALLISON**—I see.

**Mr North**—I could give you examples. I lived in Albury around the time that autogas was very much in its ascendancy. Those people—particularly those in Victoria, where I think there was very high adoption—have kept buying vehicles and had them converted to autogas. They have done that as they got older. That was one of the challenges facing the industry: because the cars were not there the younger people would rather consider a dedicated car bought new from the factory—just as you buy factory fitted airconditioning now whereas you used to have it retrofitted—so some of our consumers were growing old with our product.

**Senator ALLISON**—On that subject, who currently makes dedicated vehicles? Is there any indication that other auto manufacturers are heading down that path or have reversed a decision to do so?

**Mr Neilsen**—We have two manufacturers of dedicated at the moment, which are Ford and Mitsubishi, who have just released their dedicated vehicle. Toyota announced just prior to the budget announcement that they would be moving to a dedicated LPG vehicle, and Holden have also indicated that they will have a dedicated LPG vehicle out in 2004, when the new engine plant comes on stream. So we are basically set up with the four vehicle manufacturers here in Australia all producing dedicated LPG vehicles. The sadness to it all is that all those four manufacturers are obviously going through a fairly expensive technology program as they go into Euro 3 and Euro 4. To make that investment they needed to have some confidence and security in the long-term commitment by government. This decision has certainly thrown that whole program into chaos. I know of one particular manufacturer—I should not name them here—that have simply cancelled one level of technology move, saying that the risk of the investment at this stage is too high. They are just trying to keep their business ticking over without committing to too expensive a process. I think that will be the same for all of those. Those that have already signed up will have to go down that track for a

while, but they are not going to spend the money until they know whether there is a future in LPG.

**CHAIR**—Thank you, Mr North and Mr Neilsen.

[7.17 p.m.]

**BLACK, Mr Kevin Raymond, Managing Director, Natural Gas Vehicles Group Pty Ltd**

**CHAIR**—Do you have any comments to make about the capacity in which you appear?

**Mr Black**—I am also a director of the Australasian Natural Gas Vehicles Council. Although I do not appear on their behalf specifically today, the information that I provided to the committee is generally in line with the council's views on the legislation.

**CHAIR**—The committee has before it submission 13 on behalf of your company. Would you like to make some remarks before we proceed to questions?

**Mr Black**—Yes. I appreciate the opportunity to speak to you today. Our view is that the legislation as it stands actually represents a lack of any clear policy direction in terms of alternative fuels. The legislation as it stands identifies ethanol, biodiesel and low sulfur petrol as cleaner fuels and makes no reference to the others, although there is a provision for other alternative fuels to be included in the legislation at some later date. We are concerned that this is, if you like, a piecemeal introduction of policy in that the excise decision has been made and applies to all of the alternative fuels, but there has been no articulation of any wider consideration of an alternative fuels policy or where the government's thinking is going in that regard.

Along with the LPG industry, the natural gas industry has been dealt a body blow by the way this legislation has come about. As with most of the other witnesses who have appeared today, we had no indication that the excise decision was to be announced as part of the budget. It presents a difficulty in that decisions were on the cusp of being made in terms of our industry—which is probably in the same state as the biodiesel industry in terms of its infancy—and essentially all consideration of and investment in natural gas vehicles in Australia has virtually come to a standstill since the decision in May. Our company is just one example of that, although we are probably unlike most companies who are involved in the natural gas vehicles industry, who have an involvement in LPG or in the distribution of natural gas, in that we are dedicated to the natural gas vehicle concept.

Our business has virtually ceased to exist as a result of the excise decision. Without any clear indication of what policy direction is going to ensue, we have put a substantial amount of investment into, and have just completed development of, sequential multipoint injection systems for natural gas and LPG for modern engines, which make the engine technology equivalent to the existing petrol engine technology. We have just completed a project brief for what we believe to be the next generation of clean fuel vehicles and a demonstration of the transitional nature of natural gas—vehicles that run on 50 per cent natural gas and 50 per cent hydrogen—which is only a minor step in the process of developing the vehicles. Our colleagues in the United States have been running these vehicles for about three months now with some extraordinary success. Essentially, our view is that at the moment we have half or a third of a policy which relates to the imposition of fuel excise and that it needs to be part of a more integrated and rational approach to considering the future of alternative fuels in Australia.

**Senator STEPHENS**—Thank you, Mr Black, for your submission and the accompanying document. You make some fairly significant recommendations in your submission. On the

second last page you suggest that the additional cost to the budget of your recommendations would be no more than 50c per resident per year. Have you done any kind of back-of-the-envelope calculations about the financial impact of the recommendations and the changes that you are proposing?

**Mr Black**—Yes, we have, and I would be happy to supply that information to you.

**Senator STEPHENS**—Thank you very much, that would be very useful. You express your concern about the ad hoc approach to the policy making process around this. I understand that the whole issue got a bit hijacked by the ethanol drama earlier this year. I want this to be very clear. Your submission outlines the specific impacts on your own industry and, in particular, your own company. If the current legislation were to go through as proposed, what would the impact be for you?

**Mr Black**—If it were to go through as currently proposed, with effectively the imposition of an excise progressively from 2008, combined with the termination of the existing alternative fuels grants program in 2008, that would effectively be a double whammy. As it stands at the moment, there is, frankly, with the uncertainty that relates to all of that, nobody in this country who is prepared to invest in either vehicles or infrastructure to take it further. Effectively, we would have to either close down or go offshore. The industry generally in effect would do that. Let me give you an example of how things stand. We import and sell storage cylinders for compressed natural gas. In the six months prior to the announcement of the fuel excise, we were selling between 20 and 30 of those cylinders a month. In the five months since then, we have sold three cylinders.

**Senator STEPHENS**—That is pretty significant, isn't it? If you were to go offshore, what would that represent for New South Wales in terms of jobs and so on?

**Mr Black**—Right at the moment, probably only half-a-dozen jobs in the state. However, if the industry were to grow the way it has always been predicted it would grow, we would be looking at several hundred jobs—in New South Wales, Victoria and Tasmania primarily.

**Senator STEPHENS**—I do not know whether you can answer this question, but you have heard the other witnesses this evening talk about the two issues being lumped together in terms of ethanol, biofuels and gas. I suppose the real question is this: do you think this was an accident? Do you think it was deliberate or do you think that it was just done in some kind of ad hoc policy making, as you describe it?

**Mr Black**—I would prefer to think that it was just somebody dropping the ball.

**Senator STEPHENS**—Thank you.

**Senator ALLISON**—Mr Black, you criticise the Australian Greenhouse Office fairly strongly in your submission. You also suggest that the programs that currently provide for alternative fuels and conversions of vehicles should be primarily the responsibility of Treasury and the Australian Taxation Office. Can I invite you to expand on where you see the failures in terms of the current approach to conversions, in particular, and to infrastructure? Where have we gone wrong?

**Mr Black**—Perhaps I could go back a little bit into history. I was one of the people who had a role in the establishment of the original government policies relating to natural gas that

started with the announcement of the CNG infrastructure program at the Kyoto conference by the Prime Minister. That came as a result of a project that we undertook at the Liverpool City Council back in 1996-97. That project was based particularly on issues such as fuel security and air quality rather than greenhouse. However, when that policy was announced and when further support programs such as the alternative fuels conversion program were announced, they became part of the brief of the Australian Greenhouse Office. I have no problem with the professionalism or the dedication of the people who have been managing the program at the Australian Greenhouse Office, but the remit that they have is specifically a greenhouse one and does not take into consideration those other issues of fuel security, balance-of-payments benefits by using an indigenous fuel, air quality, health and social effects and what have you.

At the international natural gas vehicles conference in Washington last October, the spokesman for the Greenhouse Office presented the fact that their primary concern was greenhouse and that was the be-all and end-all of their consideration. I believe that, as a consequence, the bar for things such as the conversion grants program was such that vehicles which would have qualified for any program anywhere in the world, including in California, failed to qualify here in Australia because they did not show the significant greenhouse benefit over low sulfur diesel that the Greenhouse Office was looking for. While they did show huge benefits in particulates, air quality and air toxics, it was the greenhouse benefits that were driving the program. As a consequence and because the program was targeted at vehicles over 3½ tonnes and there were no vehicles being approved and qualified under that program apart from some urban buses, the CNG infrastructure program failed—there were no customers to buy the gas at the refuelling stations. Essentially, the way the program had been managed—and it was not only for natural gas; it was all alternative fuels—there have been virtually no vehicles approved except urban buses in the four or so years of the program.

**Senator ALLISON**—You suggest a specific excise rate for natural gas and you say that it should take into account the basic energy content of the natural gas on which the excise rate is to be based, the environment, resource security and energy futures credits. If that were to be the basis of the rate, would we end up with an overall credit or would there be an excise once you had done all that figuring?

**Mr Black**—That is something we would need to look at. I do not think anybody has done any numbers on the starting point, so it is very hard to work out what the credits might achieve. I would like to think that you would probably end up with an overall credit, but that is more wishful thinking than realistic.

**Senator ALLISON**—Do you think a desirable approach would be for the government to set targets for natural gas and the other alternative fuels and then work back on how to achieve those targets and set excise on the basis of whether or not they are achieved? Would you agree with that approach or not?

**Mr Black**—There would be an argument to support that; that certainly is the way the European Union is going. They have set a target of 20 per cent alternative fuels by 2020, half of which would be natural gas. They are predicating their policies on that basis.

**Senator ALLISON**—I would like to come back to energy security or resource security for fuels. We have not discussed that much as an issue this evening. Do you see any interest on

the part of the government in this question? If not, why do you think that is so, and why should Australia care about resource security?

**Mr Black**—No, we have not seen any evidence that it has a place in the government's thinking at this stage. Certainly, in terms of why it should be on the radar, we believe that Australia is more than self-sufficient in natural gas reserves. That is not only the gas reserves that we have identified so far and the traditional gas wells and the like; there is also a growing use overseas of such things as landfill methane, coal seam methane and biogas as sustainable fuels to add to that natural gas mix.

The reason that natural gas is so important to our fuel mix is that Australia is hugely dependent on transport for its industry—and primarily road transport. In the event of any sort of disruption to our fuel supply or indeed a massive price hike in our fuel supply pricing, the potential exists for our transport industry to be severely affected. Sixty-five per cent of the world's available oil reserves are in the Middle East and the majority of the rest is in Russia and Siberia. They are not exactly what you might call the most stable supply regimes. I believe it is absolutely vital that we have the capacity to adapt our energy market in the event that there is some form of crisis in the future.

**Senator ALLISON**—We have not discussed LNG much this evening, but presumably you can speak to the application of LNG.

**Mr Black**—Yes.

**Senator ALLISON**—What are the preferred applications for LNG?

**Mr Black**—Certainly, from our point of view, natural gas is natural gas and it is just a matter of how it is stored, whether it is CNG or LNG. LNG is effectively a much more dense way of storing the fuel and therefore you can get considerable range. We see the benefits in LNG to be in long-haul transport—interstate transport particularly—in interstate rail applications and in marine applications. We have been talking, for instance, with a fishing fleet operator who is extremely keen to use LNG in a mother ship application, where the heat exchange of converting the LNG from liquid to a gaseous state to operate the ship would also chill the catch. So it would result in a double saving for the operator.

**Senator ALLISON**—Are OEMs coming on line for LNG?

**Mr Black**—Not at the moment. Essentially, the OEMs are sitting back and waiting. As our friends from the ALPGA said, the OEMs will be driven by the market. We know that the state and local government market is showing considerable interest and will show considerable interest in the natural gas vehicle market when they can get an OEM product. Part of what our company has been working on for the last two years is an OEM gaseous fuel product that exactly emulates the current state-of-the-art petrol emission systems. It has been one of the drawbacks of gaseous fuels that, effectively, to build a dedicated LPG vehicle, for instance, it is necessary to take off all the you-beaut 2003 technology and put on you-beaut 1985 technology. We have worked to a point where we now have three separate fuel injection systems which are applicable to spark ignited engines for natural gas and we are about to start testing one of those with LP gas.

**Senator ALLISON**—It has often been said that, once you have Euro 3 or 4, particularly in trucks, and you have ultra low sulfur diesel, that is about as clean as it gets. Do you disagree with that?

**Mr Black**—There is a lot of dispute about the results when you get to ultra low sulfur diesel, particularly in particulates. You are actually talking about much finer particulates with potentially greater health hazards in terms of carcinogens. At this stage, I do not think that is something that has been addressed. Certainly, the ultra low sulfur diesels and the ultra low sulfur petrols will be cleaner than they are now and will probably produce similar exhaust emissions, but you have to remember that we are not talking about just exhaust emissions; we are talking about life cycle emissions. When you talk about life cycle emissions in the ultra low sulfur fuels, you are looking at much higher emissions in the refining process. That is pretty much borne out with the work that the CSIRO did on behalf of Environment Australia and the Greenhouse Office in their life cycle analysis, the results of which are included in our supplementary paper. Certainly, the low sulfur fuels are getting cleaner and there is no doubt that they will meet the standards that are required but, on any given parameter, if the fuel starts off cleaner then the results will always be cleaner.

**Senator ALLISON**—As I said earlier, word has it that this imposition of excise is all about getting rid of the inefficient alternative fuels. Is CNG inefficient?

**Mr Black**—Certainly not. CNG is probably the most efficient fuel for motor vehicle use that we now have. It can be and is in most cases delivered to the dispensing site by pipeline. It does not require refining; it simply requires compressing and liquefying to be used in a vehicle. It does not require any further processing to make it a clean fuel, particularly if the technologies are equivalent. It is certainly the way the rest of the world is going.

It is probably interesting to note that Argentina started its natural gas program at about the same time as the Prime Minister announced the CNG infrastructure program in November or December 1997. Since then we have put something like 600 vehicles on the road, most of them buses, although my company has four natural gas cars operating. In Argentina, they have put a million vehicles on the road simply because they had a well-thought-out program of support for natural gas vehicles. In Argentina and Brazil, they are currently putting 20,000 vehicles a month onto natural gas. It offers a lot of benefits that the other fuels do not, but at the same time there is always going to be a place for a wide range of fuels.

No one fuel is going to be dominant in the future, but we see the benefits of natural gas in its transition to the hydrogen economy particularly as being certainly the easiest to achieve, and we have made some references to that in the papers. As I have said, we are about to embark on a project that will actually combine natural gas and hydrogen in a standard Ford Falcon.

**CHAIR**—Thank you very much, Mr Black.

[7.44 p.m.]

**ROSE, Mr Griffith Frank, CVC Reef Ltd and Australian Biodiesel Consultancy**

**CHAIR**—I welcome you and invite you to make a brief opening statement.

**Mr Rose**—Firstly, I follow on from most of the comments of the previous speaker regarding the lack of warning of the decision to impose excise on alternative fuels—in particular, biodiesel. If the natural gas industry is in its infancy, then I suspect that the biodiesel industry has not yet been born, although it was conceived perhaps some time ago. It is typically made up of very committed players, and I would just like to point out one of the advantages that biodiesel has over the other alternative fuels that I have heard most of the discussion on—that is, there is really no substantial change to infrastructure required to implement biodiesel. It is a direct replacement for diesel and can be used virtually without any change to the infrastructure. You can put biodiesel in the tank one day and diesel in the tank the next day and continue alternating without causing any difficulty either in the operation or in the long-term maintenance of the facility, be it the vehicle or the actual distribution network.

The major impact of the introduction of the excise has been to raise uncertainty in the industry to a level where investment decisions are virtually impossible to make. What is necessary, more than anything, is a level of certainty as to the environment in which the industry is to operate. That comes down to the level of excise discussions—which, of course, are due to happen some time over the next four or five years—and the final level and, of course, to the possible impact of having an excise level that goes up and then comes down again, if the discussions do actually take into account the full benefits of biodiesel. If the final level of excise on biodiesel is substantially lower than that which is on petrodiesel, then you would have a rather unfortunate situation where, in the early stages of attempting to develop the industry when the benefits and the incentives should be maximised, they would in fact turn out to be more than they were going to be in the longer term.

The points the previous speaker made regarding resource security and balance-of-payments benefits hold true even more for biodiesel, potentially, because the rural industries would supply most of the feedstock and could be developed on the basis of supplying that feedstock. But that will not happen in the absence of substantial investment—and that will not happen in the absence of a secure understanding of the regime that is in place.

The main points that would really help this industry are these. The off-road grants should apply to all biodiesel, because the maximum benefits of biodiesel occur in places such as wetlands, wilderness and areas of environmental sensitivity. The benefits in these areas of biodiesel, compared with alternatives, especially petrodiesel, are enormous. The Sydney Harbour, for example, could benefit enormously if all the users of diesel on that waterway were able to make the choice, without financial penalty, to use 100 per cent biodiesel, which they are now not able to do because of the way the grants scheme works.

The other major points relate to time frames. The number of years between now and when the excise starts to take effect is so short that, with the significant investments required in infrastructure and plant capacity, you would not have time to recoup those investments and therefore have them effectively written off to then survive under the regime of excise. We are

not suggesting that it is impossible to live with excise in the longer term; it is just the time scale and the final level of it. Finally, a target of two per cent of alternative fuels by 2020 that some people have talked about—and various suggestions have been made—really is far too small. Again, as the previous speaker suggested, it needs to be a very much bigger number, because, in theory, there is sufficient feedstock for biodiesel plants to produce that much without significant impact on production. You are not growing an industry anywhere if all you are asking of it is to produce at that level. The really big impacts do come when you go beyond using up what is currently available and you can then start to build agricultural production capacity on the basis of a demand and a secure supply for your transport fuel needs.

**Senator STEPHENS**—I found your submission very interesting, thank you very much. You are agreeing that a two per cent goal by 2020 is grossly insufficient?

**Mr Rose**—Yes, indeed.

**Senator STEPHENS**—And your argument is that biodiesel certainly should not have the same rate of excise as diesel fuel?

**Mr Rose**—In 2012?

**Senator STEPHENS**—Yes.

**Mr Rose**—Yes, absolutely. It provides so many additional benefits—that are difficult, if not impossible in some cases, to quantify but are nonetheless real—that it would be absolutely inequitable to apply the same rate purely on the basis that it provides the same transport capability.

**Senator STEPHENS**—Thank you.

**Senator ALLISON**—The current proposal, as you would be aware, is to apply an excise on the basis of calorific content. Would you, like the gas and ethanol industry, like to see some other measures that determine what an excise rate should be and, if so, would you care to suggest what they might be?

**Mr Rose**—I do suggest that it should be far broader than simply the calorific value, because, as I said, you get so many additional benefits in terms of the greenhouse impact, the potential employment benefits, the actual air quality benefits and the resource security benefits that you cannot simply compare an existing diesel product with a biodiesel and say, ‘Biodiesel is 90 per cent of the calorific content of diesel; therefore, it should be 90 per cent of the excise.’ I am sorry, I cannot suggest any specific formula, but I would be happy to work with anyone to develop such a formula.

**Senator ALLISON**—As you say, your industry is not yet in its infancy even, but are you getting any feedback from the kinds of rural communities that might benefit from a biodiesel industry in their area? You talk about canola and the fact that we export 70 to 80 per cent of our production. Can you give the committee any feedback on the reaction to this excise and its impact on your potential industry?

**Mr Rose**—I cannot give you any particular or direct feedback from specific communities. However, there is universal willingness to embrace biodiesel, for all of the reasons that I talked about earlier—not only the potential for it to develop another commodity or another

market for a community's products but also, in particular, in areas of environmental sensitivity, the desire to use it instead of alternatives because it would offer far less potential for damage to that environment. Generally speaking, people want to be sustainable; they really do. It is a matter of economic reality, though, that these people will not be sustainable if it costs them an extra 30c a litre or whatever to do it; they just will not.

**Senator ALLISON**—Is it the case with biodiesel, as it is with ethanol, that technology that will come along over the next decade or so will not only reduce costs but also open up opportunities for other feedstock to produce biodiesel?

**Mr Rose**—I believe so. The plant that the Australian Biodiesel Consultancy has built in Wyong is an example of that. It is yet to be fully commissioned for other reasons—delays with permitting and development approvals and things like that. But it is an example of a plant that has been designed to take a very broad spectrum of input and produce a consistent quality product from it. There are many people overseas claiming to deliver that now, although, when you go and talk to them and look at what they have done, very few have any capability to deliver that in meaningful terms. But I believe it is the way of the future, yes.

**Senator STEPHENS**—Where did you say that plant was?

**Mr Rose**—It is in Wyong.

**Senator STEPHENS**—In what capacity is it producing?

**Mr Rose**—It is not producing at this moment. It has been built and has yet to be commissioned.

**Senator STEPHENS**—To produce how much?

**Mr Rose**—Its capacity roughly is 40,000 tonnes or 40 megalitres per annum.

**Senator STEPHENS**—When is it due to be completed?

**Mr Rose**—It is completed; it is just awaiting final approvals.

**Senator ALLISON**—What do new developers of biodiesel meet when they go to the bank manager and say they have this bright idea to set up a new plant?

**Mr Rose**—By and large, it is a very difficult sell. The bank manager wants to understand, firstly, that you have a market for your product and, secondly, that you have a feedstock for your product that will be reliable and that you will be able to use through the good years and the bad years and have access to in those times. It is a very difficult sell to get a bank manager to back you. I think everyone who has tried will testify to that.

**Senator ALLISON**—You talk about the development of new crop varieties that are nonedible. Is there some advantage in these crops? Do they use less water or fewer pesticides or something that we can be attracted to?

**Mr Rose**—It is not an area that is within my expertise; I am sorry. I believe that it is a higher yield crop and that it possibly can go on to a broader range, but I am not an expert on crops in that sense.

**CHAIR**—Thank you, Mr Rose.

[7.59 p.m.]

**FREE, Mr Anthony John, Manager, Excise Unit, Indirect Tax Division, Department of the Treasury**

**HARMS, Mr Michael, Acting General Manager, Indirect Tax Division, Department of the Treasury**

**PRESTON, Ms Kate, Policy Analyst, Indirect Tax Division, Department of the Treasury**

**CHAIR**—May I remind senators that officers of the Public Service may not, under the procedural rules governing this committee, be invited to comment on questions of policy. I welcome the witnesses. Would any of you like to make an opening statement?

**Mr Harms**—I will just make a short opening statement. The bills before the committee establish the Energy Grants Cleaner Fuels Scheme. That provides a generic framework for payment of cleaner fuel grants to importers and manufacturers of certain cleaner fuels. The Energy Grants Cleaner Fuels Scheme relates to the fuel tax reform and cleaner fuel measures announced in the 2003-04 budget. In the budget the government announced its policy in relation to fuel tax reform. Under these reforms all currently untaxed fuels used in internal combustion engines will be brought into the excise and customs duty system by 1 July 2008.

The introduction of excise on previously untaxed fuels will be accompanied by the use of cleaner fuel grants that will reduce the effective excise—that is, the excise less the grant—for these fuels for a transition period extending to 2012. The grant rates will be reduced in five even instalments from 1 July 2008 to 1 July 2012, raising the effective excise rate from zero before 1 July 2008 to the final excise rates applying to the fuels. The government is yet to announce these final excise rates that will apply to various fuels.

The first fuel to be subject to the Energy Grants Cleaner Fuels Scheme is biodiesel, and biodiesel became excisable at 38.143c per litre from 18 September 2003 in accordance with the government's budget announcement. The cleaner fuel grant will be payable to offset the customs and excise duty on biodiesel so that the current effective excise rate of zero for pure biodiesel is continued until 30 June 2008.

The Energy Grants Cleaner Fuels Scheme also fulfils the government's commitment in the Measures for a Better Environment package to encourage conversion from the dirtiest fuels to the most appropriate and cleaner fuels. From 1 July 2006 the government will provide grant payments for the production or importation of premium unleaded petrol with less than 50 parts per million sulfur for a period of two years, and similar arrangements will be implemented for diesel with less than 10 parts per million sulfur from 1 July 2007.

**CHAIR**—We have heard from a number of witnesses this evening that this new regime was announced in the budget without any prior consultation with participants in the industry. Is that true?

**Mr Harms**—I cannot comment on that. The budget announcement was as the result of cabinet considerations. Cabinet was advised by the—

**CHAIR**—No, that is not what I am asking you. I am asking you whether an event in fact happened—that is, consultation with the industry. Did it happen or didn't it?

**Mr Harms**—I am not aware. I cannot answer that.

**CHAIR**—You just do not know. Do you know, Mr Free?

**Mr Free**—There was no direct consultation with the industry in the period leading up to the budget announcement that I am aware of. The advice to the government in the budget process, which is often conducted without consultation on tax measures in a budget environment, was provided to the government by the Energy Task Force, which is a committee of senior public servants from a number of departments. The setting up of that task force was foreshadowed in the Prime Minister's speech to CEDA in November last year. But as to actually approaching industry in the budget context, I am not aware of any specific consultation.

**CHAIR**—Why wasn't there any?

**Mr Free**—I cannot speak for the motivation or the reasons—

**CHAIR**—I am not asking you to comment on whether or not there should have been. That is a view that senators might arrive at themselves. But I think I can ask you why in fact it did not happen.

**Mr Free**—Probably it was because it was conducted in the way taxation measures in budgets have been formulated over many budgets, which is normally a process which is conducted internally within government.

**CHAIR**—So you say that, because this was a revenue measure, it was in conformity with the established practice not to advertise potential changes to taxpayers. Is that the substance of what you are saying?

**Mr Free**—Yes, that would be a fairly good summary.

**Senator STEPHENS**—I want to continue on from Senator Brandis. You have had the opportunity to read the submissions to the inquiry and to listen to the evidence this evening. Firstly, I want to ask the Treasury's view of the alternative fuel production grant systems. Do you think they are effective and efficient?

**Mr Harms**—I do not know that Treasury has a view on whether they are effective or efficient. This bill is about implementing the government's policy as announced in the budget. The government's policy announcement referred to bringing all fuels onto a neutral tax basis in order to remove taxation distortions that currently exist in the market. The policies underlying the government's announcement of tax reform and, by association, these bills do not seek to differentiate between fuels on the basis of their fuel security or their environmental properties. This is about bringing all fuels onto the same neutral tax arrangements so that those fuels can perform without distortion in the marketplace.

**Mr Free**—As a general principle of the imposition of taxation law, one of the principles is tax efficiency. It is particularly important in imposing taxes on products where you try to impose the taxes in such a way that you do not affect economic choices purely for tax reasons. The comments about inefficiency should be seen in that light of inefficiency in a tax allocative sense. There certainly should not be any implication that somehow the various alternative fuels industries have technical inefficiencies or are wasting energy or resources in that sense. It is an issue about tax efficiency. Certainly, where products that are competing

with taxed conventional products, petrol and diesel, have not been taxed, the government has set out a pathway over a number of years as a transition so that they will be taxed on a fairly equivalent basis.

**CHAIR**—So Mr Harms, given that the policy objective is as you have summarised it, is it your view that this legislation is—and I do not want you to comment on the merits of the policy; you cannot do that—efficacious to achieve those objectives?

**Mr Harms**—Certainly.

**Senator STEPHENS**—Can you advise the committee and the witnesses here who are looking for some industry certainty about when the excise rates might be announced?

**Mr Harms**—I cannot provide you with any definite information about that. I understand that the excise rates will be announced later in this year.

**Senator STEPHENS**—In this year?

**Mr Harms**—The 2003 calendar year.

**Mr Free**—In the Treasurer's press release on budget night he said:

The final excise rates to apply to fuels will be determined later this year—  
as in 2003—

and will take into account factors such as the energy content of fuels.

**Senator STEPHENS**—We heard earlier from the Australian Coalition for Ethanol from Queensland. Their concern is about a significant policy shift. They provided us with evidence, including the following correspondence from Minister Truss where he actually signed off:

On the matter of the excise exemption for fuel ethanol, I can confirm on behalf of the government that, as stated in the 'Biofuels for Cleaner Transport' policy, the current exemption of fuel ethanol from the \$0.38 per litre excise on petroleum products will be maintained.

That was the basis on which they made a lot of investment decisions. Did Treasury provide advice to Minister Truss's office?

**Mr Free**—I am not aware of that letter. I can say that the policy that has been implemented appears to be totally consistent with that.

**Senator STEPHENS**—Their interpretation is not that it is consistent, is it? They are arguing that there has been a significant policy shift.

**CHAIR**—Let us not have a debate about what your interpretation is of their interpretation. Let us just show you, Mr Free, the letter and let you read it. Senator Stephens might care to pursue that line of questioning after you have read the letter.

**Senator STEPHENS**—That is fine. My question really was whether or not Treasury actually provided that advice to Minister Truss's office.

**CHAIR**—We will just pause and let the officers read the letter.

**Mr Free**—As I said, I am not aware of that letter. I will have to take it on notice as to whether Treasury provided that advice. I should add that it was written prior to my employment by the Treasury. The effective excise on domestically produced fuel ethanol in Australia is zero until 1 July 2008.

**CHAIR**—Can you help, Mr Harms?

**Mr Harms**—No. I was not in Treasury at that time either. I can only say that I have not provided any advice along these lines to Minister Truss or to the department.

**CHAIR**—What about you, Ms Preston?

**Ms Preston**—We all commenced in Treasury on the same date.

**Senator STEPHENS**—Given that you talk about this legislation trying to provide some uniformity across the industry, does Treasury have a view about the differing administration arrangements for ethanol and biodiesel with respect to the production grants?

**Mr Harms**—Again, that is a matter of government policy. It was announced in the budget that the existing ethanol arrangements administered by the Department of Industry, Tourism and Resources under contract would continue, and the government announced that different arrangements would apply for biodiesel.

**Senator STEPHENS**—I am struggling to understand why fuels that are so different are treated so uniformly, and I am interested in knowing whether or not Treasury can advise whether there are some overseas examples of how different fuels are being treated by governments that suggest that this is the best way to go?

**Mr Free**—With reference to fuels that you have described as being so different being treated similarly, the Treasurer's press release of 13 May that I referred to before states:

The reforms will establish a fairer and more transparent fuel excise system with improved competitive neutrality between fuels.

This brings me back to the comment I made about diesel and petrol, which form over 92 per cent of the transport fuels market and are both taxed. These other products, which have exactly the same function, to date have not been taxed. The government has made the decision to bring them into the taxation system through a phased process which it considers addresses all the commitments it has made to those fuel industries. While the nature of the fuels in some cases may be quite different, they have the fundamental purpose of being used in an internal combustion engine, in particular, to provide transport for vehicles, so there is a similarity in that purpose, which is being taxed.

**CHAIR**—Can I put it this way: the commonality is to be found not in the composition of the fuel but in the function?

**Mr Free**—That is certainly correct, Senator.

**Senator STEPHENS**—In the minister's second reading speech, he does not mention gas. He only mentions biodiesel and ethanol. Given the evidence of the witnesses from the gas industry here this evening, do you have any comments to make about their concerns regarding the impacts of this legislation on the Australian gas industry?

**Mr Harms**—I do not have any comments to make about their concerns relating to the gas industry. I can comment on what was in the second reading speech. The explanation for that lies with the fact that the judgment is that ethanol and biodiesel, which are used and distributed in fairly much the same way as petrol and diesel, can be accommodated within the existing excise system without any great need for change. It has been decided—and I think it

is in the press releases—that the administration of the new tax arrangements for the gaseous fuels will be implemented in consultation with industry to ensure that the most effective and efficient means are put in place for taxing those fuels. It may be that, because they have a different distribution chain and they have different dual uses from the conventional fuels, those arrangements may differ. So the bill that you have before you provides the capacity to deal with those fuels. If it is determined that the excise system, as it is currently administered through the Excise Act, is not the most appropriate means of addressing those fuels then different legislation may need to be introduced for them at a later date.

**Senator STEPHENS**—Can you advise the committee whether the implications for the gas industry were specifically considered in the development of the legislation?

**Mr Harms**—No. The legislation, as I previously stated, implements government policy.

**Senator ALLISON**—I would like to explore what you say is not yet decided—and that is the rate of the excise. You started by saying that you are not seeking to differentiate on the basis of environment, fuel security or, presumably, a whole range of other measures that have been raised tonight. And you say that you want to remove tax distortions that exist. What then are the variables in terms of the excise and how it might be applied? What criteria will be used to establish that final excise rate?

**Mr Free**—You have mentioned a number of factors, such as energy security, environmental considerations and the like. The government will assess the quantum of those—where they can be quantified—and will assess whether they should be taken into account by some method through the excise rates or should be separated from the excise rates and—if they want to address those issues—what are the measures by which that can be done. The government has not made its announcement on the rates yet so I cannot speculate on whether those factors will be explicitly taken into account in the rates or whether there will be other measures to assess those particular factors.

**Senator ALLISON**—What process will you use to arrive at which of those factors will be taken into account?

**Mr Free**—The general process is the normal government process of decision making where decisions are taken by cabinet and, in this case, on the advice of the energy task force, which was set up following the Prime Minister's announcement in November last year that energy was one of the strategic priorities for the government.

**Senator ALLISON**—To what were you referring when you said that you were not seeking a differential on the basis of environmental or fuel security? I wrote it down because it is quite important.

**Mr Free**—I was explaining what was meant by the Treasurer's statements in his press release about improved competitive neutrality; whereas, if you are going to tax on pure tax principles, you would not take those factors into account in the tax rate, you would try to tax fuels in as neutral way as possible, noting that there are some difficulties in that which various parties have alluded to in that the pure energy content of fuels is not an exact fit on how far you might drive your vehicle using a particular fuel. There is an issue that would be a perspective on pure tax policy, that you would try to set the tax rate so that in the outcome that you are trying to tax they are as neutral as possible. As has been raised by various submissions

and as you have raised, there are other factors which to date have been given as various reasons for different fuels having different tax rates. The government will make an assessment of the weighting of those factors and how best to deliver any particular assistance to industries or fuels in accordance with that weighting.

**Senator ALLISON**—Mr Free, I am sure you have given the witnesses who are here tonight some hope for the future but you have also heard them say that their industries, in the case of LPG or natural gas, are effectively going to go broke before too long. What do you understand to be the time frame by which these other factors might be articulated and in which you might talk with industry about what factors should be taken on board?

**Mr Free**—My understanding is that many of the industries here tonight, ALPGA in particular, have had quite detailed discussions with members of the energy task force, and I have sat in on some of those discussions. The energy task force is taking them into account in advising government. As to the timing, I can only repeat the operative part of the Treasurer's press release that says:

The final excise rates to apply to fuels will be determined later this year ...

**Senator ALLISON**—Later this year?

**Mr Free**—Yes, that is in the Treasurer's press release of 13 May, issued on budget night.

**Senator ALLISON**—What sort of modelling will Treasury do with regard to the viability of the various fuels within the alternative sector?

**Mr Harms**—I do not understand the question. What modelling are you thinking the Treasury would make in relation to the viability of those fuels?

**Senator ALLISON**—The Treasury does not have an interest in whether natural gas or LPG is a viable industry? You are just relying on the energy task force to make those judgments?

**Mr Harms**—Treasury is a member of the energy task force and I will be involved with the energy task force in preparing those papers.

**Senator ALLISON**—So you have got the alternative fuels industry coming to the energy task force saying, 'We're going to go broke. Our APA has now gone into liquidation or administration; orders are down 50 per cent for LPG vehicles; Dalby can't get further funds for their development.' How do you check whether what we are being told and what you must be being told in the energy task force is right or not? We are hearing that the alternative fuels industry has been struck a body blow. How do you assess whether that is fanciful or based in economic reality?

**Mr Free**—As I mentioned earlier, decisions are made by the government through the cabinet process. Normally what happens in the cabinet process is that the government has a full submission which analyses those factors. As has been said by some of the earlier witnesses—I recall Ray North from ALPGA saying—

**Senator ALLISON**—Sorry, Mr Free, that was not my question. We understand cabinet makes this decision, but cabinet, you said, will act on the recommendations of the energy task force.

**Mr Free**—Yes.

**Senator ALLISON**—You are on the energy task force. My question is: who is doing the modelling to check whether the industry is telling us the truth? They have come along tonight and said, ‘It is the end of the industry.’

**Mr Free**—I am not on the energy task force; I am a Treasury officer.

**Senator ALLISON**—Mr Harms, can you answer that question?

**Mr Harms**—I am not on the energy task force either. Any modelling of that nature would be done by the energy task force. The advice that we provide to the task force through our membership is in relation to the economic and the fiscal policies that might ensue.

**CHAIR**—But what about the microeconomic impact on the industry? Do you have regard to that?

**Mr Harms**—We have not been advising at that level, no.

**CHAIR**—You can see Senator Allison’s point, can’t you? You have told us—and I understand the reasons you have offered, Mr Free—why there was no prior consultation with the industry, the policy is announced and the industry now says, ‘The economics don’t work for us.’ Presumably, that was not known or anticipated before the policy was announced because, among other things, the industry was not consulted. The industry now says this. Will there be a process by which the propositions you have heard uttered this evening will be tested, whether by way of economic modelling or in some other empirical way? Is that going to happen?

**Mr Harms**—Not in any other empirical way. The LPG Association has provided its own modelling to the energy task force. We have seen aspects of that and have provided our advice in relation to that. We are not modelling those aspects ourselves independently.

**Senator ALLISON**—Who from Treasury is on the energy task force?

**Mr Harms**—I guess the secretary is the person who would be represented, but he delegates that to an executive director and the meeting is also attended from time to time by a general manager and more recently by our general manager in the revenue group.

**Senator ALLISON**—Who is that?

**Mr Harms**—David Parker.

**Senator ALLISON**—Why was Mr Parker not invited to come this evening?

**Mr Harms**—He has nothing to do with this legislation.

**Senator ALLISON**—I thought you said he was on the energy task force.

**Mr Harms**—I did. That energy task force has a different role to the one that we have.

**Senator ALLISON**—What is your role, Mr Harms?

**Mr Harms**—My role is to implement government policy into legislation and to advise government in relation to policy specifically to do with indirect tax.

**Senator ALLISON**—Okay.

**Mr Harms**—To answer your question more fully, if you are wondering about that, I understood that this committee was examining the bills which set up a cleaner fuels scheme to pay grants to reduce the incidence of taxation. I have been involved in providing advice to government and drafting this legislation, so I am best suited to answer questions about it.

**Senator ALLISON**—All right, thank you.

**CHAIR**—So you are saying that the questions that Senator Allison is directing to you seek responses that you are just not in a position to provide?

**Mr Harms**—That is right.

**Senator ALLISON**—If I could go to your submission, you have been asked to implement the budget measure which—and I will quote from your submission:

... is to encourage conversion from the dirtiest fuels to the most appropriate and cleanest fuels.

You have been here this afternoon and this evening. Is it your view that this first step, if you like, and the subsequent steps will do that? Will they encourage the cleanest fuels and the most appropriate fuels?

**Mr Harms**—In relation to that phrase? That is part of the aim of this legislation and specifically in relation to encouraging the early production of ultra low sulfur fuels. So the ‘cleaner and more appropriate fuels’ that that paragraph refers to are the government’s announcements in relation to ultra low sulfur fuels.

**Senator ALLISON**—I notice that you said ‘cleaner’, but in fact it is ‘cleanest’. Where do you rate ultra low sulfur fuels in the range of dirty, cleanish, cleaner and cleanest?

**Mr Harms**—I have not made those comparisons.

**Senator ALLISON**—But you are implementing what you put in your submission was the commitment.

**Mr Harms**—That refers to the government’s commitment as per its announcement in the budget papers.

**CHAIR**—I think, in fairness, Mr Harms did tell us in response to a question from me some little while ago that the view is that this legislation is efficacious in giving effect to that policy.

**Mr Harms**—That is correct.

**Senator ALLISON**—I probably know the answer to this question but you have not done a study, and to your knowledge no independent study has been done, of the viability of any aspect of the alternative fuels industry—and I will take that as a given. What about the cost effects of public health issues related to cleaner/cleanest fuels? Has any work been done on that? Was Environment Australia invited to do some work on this question to feed into this process; and, if not, why not?

**Mr Harms**—Environment Australia is represented on the energy task force.

**Senator ALLISON**—That was not what I asked.

**Mr Harms**—What work was commissioned by Environment Australia is beyond my knowledge; I do not know. Environment Australia has had only technical input into the drafting of these bills. Basically it has provided advice to us about the way in which our fuel

standards are determined. So in terms of drafting these bills, whilst we have had some engagement with Environment Australia, it is not along the lines that you are alluding to.

**Senator ALLISON**—It would have been useful if we had had someone on the energy task force here tonight to answer those questions. I wonder whether you could take on notice whether Environment Australia or the Australian Greenhouse Office made submissions in the development of this legislation.

**Mr Harms**—I can answer that question—and I am sorry, I thought I had. Environment Australia has not made submissions in the development of this legislation.

**Senator ALLISON**—And the Australian Greenhouse Office?

**Mr Harms**—Nor has the Australian Greenhouse Office.

**Senator ALLISON**—Or the Department of Health and Ageing?

**Mr Harms**—Nor the Department of Health and Ageing.

**Senator ALLISON**—What about consideration of balance of payments—the general economic issues that fall under energy security and the kind of economic end of this debate? Has Treasury done any work on establishing longer term what the likelihood is in terms of Australia's economic interests overall?

**Mr Harms**—Not in relation to the development of this legislation. I think the primary responsibility for policy of that nature rests with the department of industry.

**Senator ALLISON**—Mr Free, you have talked about efficiency in a tax allocative sense. How efficient would this be if we ended up with no alternative fuel sector? I suppose I am answering my own question: it probably would be very efficient if you only had to bother about excise on petroleum products. Is that what you mean by efficiency?

**Mr Free**—In economics terms, efficiency means that the resources go to the highest valued uses, which are normally determined by market. The Treasurer's press release, from which I think you were extracting the words about inefficient investments, was made in that sense of tax efficiency. Some of the growth—or perhaps much of the growth; it is hard to say—in the LPG industry, for example, has been purely driven by the fact that it was not taxed at all historically compared to a product which provides exactly the same purpose—namely, driving a motor vehicle. The government has made that decision, as announced by the Treasurer, that in the longer term that is not appropriate, and he has given the reasons in his press release. But the government has also recognised that investments have been made in those types of areas, in LPG and in other alternative fuels, so it has put in place a fairly lengthy adjustment process, which is not completed until 2012, with in the first five years of that adjustment process there being no effective excise at all.

**Senator ALLISON**—I am sorry, which five years—2008 to 2012?

**Mr Free**—No, from now until 2008. There is no tax on LPG until 2008. No effective tax on ethanol until 2008. No effective tax on biodiesel until 2008. No tax on CNG until 2008. No tax on LNG until 2008.

**Senator ALLISON**—In identifying 2008 as the beginning of the transition period—that is five years from now—what factors were taken into account? Were they things like pay-back

periods, economies of scale, state of the industry at a particular point in time, investment already committed? What sorts of factors were considered in that 2008 date and, for that matter, the 2012 date?

**Mr Free**—I think we are getting into some policy areas that I probably cannot comment on, other than to say that the government would have weighed up those considerations when it made the decision and balanced them out. In the Treasurer's press release, one thing he did comment on is that they fulfilled the government's existing commitments concerning the tax treatment of fuels which were that—

**Senator ALLISON**—So Treasury per se did not have a role in developing a formula or saying, 'This is the time when this industry will be viable or not viable'?

**Mr Free**—Certainly Treasury can advise what the government's commitments were, which, for the LPG industry, was for a rolling five-year commitment. That essentially meant that five years notice was given when excise was going to be applied. Certainly the government considers it has met that commitment. There was reference to the statement prior to the last election about biofuels. My understanding is that governments normally give commitments on tax matters for the life of the next government. Certainly from now until whenever the next election is, whenever that may be, there is no effective tax on biodiesel or ethanol, hence the Treasurer's statement that the government has fulfilled its existing commitment.

**Senator ALLISON**—What work was done on this measure in relation to the 350 megalitres target by 2010, I think it was, or 2020? That is the Prime Minister's target. What do you see as being the relationship between that prime ministerial target and what has been proposed?

**Mr Free**—Again I would quote from the Treasurer's press release, that the arrangements 'will provide the opportunity for currently untaxed fuels to establish their commercial credentials in the marketplace'. Similarly, on budget night, in relation to biofuels, the minister for environment made a press statement which talked about the government's ongoing commitment to a commercially viable renewable fuels industry—'commercially viable' meaning that, over a lengthy transition period, those fuels should be on a much more tax neutral basis with the principal conventional fuels that they compete with.

**Senator ALLISON**—By that time, which fuels would you expect to have 'survived'?

**Mr Free**—The fuels that find acceptance in the market.

**Senator ALLISON**—Let us take CNG for starters. That does not find acceptance at this point in time; is it going to in 2008 or 2012?

**Mr Free**—I do not think I can comment on that. I do not know what the market will be in 2008 or 2012. That is the whole objective of the policy—to provide a more neutral market so that the market will determine which of those fuels finds its place in the fuel mix. Should the government wish to put in place some other measures to encourage particular fuels, they will do so but not necessarily through differential tax treatment. As an example of that, I refer you to the press release of 25 July by the Hon. Joe Hockey, who was acting industry minister at the time, which indicated that the government was going to allocate \$37 million to fund

capital subsidies for new or expanded biofuels capacity. I understand that followed on from the biofuels policy, which has been referenced by a number of witnesses before the committee.

**Senator ALLISON**—I think we can understand why the industry might be a bit confused about where Treasury is going. On the one hand, you talk about the rate of excise being as yet not established and it may take into account environment or health or a range of other resource security issues—the list of possible criteria that might be applied in establishing the excise. Now you say—as I understand it and correct me if I am wrong—that you would be looking for a standard rate but other ways of providing assistance. Is that what you are suggesting?

**Mr Free**—I would say that the government has not yet announced the final rates. It will take various factors into account, including the energy content. Whether those factors feed into some type of differentiation in the rates or whether the government considers that measures need to be put in place to respond to those and will do so through other means is something on which a decision has not been made available publicly. I state again that the Treasurer's press release referring to later this year relates to the timing.

**Senator ALLISON**—We are probably getting a bit circular now.

**Mr Free**—Yes.

**Senator ALLISON**—I come back to the question process. I know you have not been able to help us much in this sense, but what should the industry do to make its case? Should it now be writing to the energy task force? What is the next stage in the energy task force's process in coming up with a recommendation for an announcement—and I think you said later this year?

**Mr Free**—Later this year.

**Senator ALLISON**—There is not much left of this year; there is really only November and a bit of December. At what point is the information going to feed into that decision-making process, and how?

**Mr Harms**—Just to answer that, I think a lot of industries appearing here tonight indicated they have had no difficulty at all in making contact with the energy task force and putting their point of view. Many of them indicated that they thought they had already had ample opportunity to put their views before the energy task force. I am sure that the energy task force would welcome any of those who thought they had not done so to approach it—unless it is about the timing. Obviously, as the government has indicated, the announcement on excise rates will be made before the end of the year.

**Senator ALLISON**—There is no formal process? That is what I am trying to get at. You say they have already had access to the energy task force and they might still be able to have access, but there is no date by which a response—

**Mr Harms**—The energy task force has not called for public submissions with a response—or anything like that.

**CHAIR**—Is the answer to Senator Allison's question—that is, that there is no formal process—yes or no?

**Mr Harms**—There is no formal process for consultation.

**Senator ALLISON**—I think I have reached the end of all that. So there is no formal process. There will be a report from the energy task force to cabinet. Presumably that will not be a public document.

**Mr Harms**—I don't know that a report would be the product, but certainly there would be cabinet memorandums, which would be prepared by the energy task force, for consideration by the energy committee of cabinet.

**Senator ALLISON**—Does the energy task force have more work to do by way of meetings and so forth?

**Mr Harms**—I believe it has quite a wide agenda, in relation to energy, as foreshadowed in the Prime Minister's statement last year.

**Senator ALLISON**—How often does it meet?

**Mr Harms**—It probably meets on a monthly or bimonthly basis—as the need arises. I can certainly recall it meeting every month or so over the past six months, or more.

**Senator ALLISON**—For the benefit of the witnesses who are still here, who might want to make another submission, by what date do you expect the energy task force to be making its recommendations—whether they are in report form or memo form? What would you advise those here who might still want to say something?

**Mr Harms**—I would advise them to contact the secretariat of the energy task force in the Department of the Prime Minister and Cabinet, to make inquiries as to what time—or what capacity—they might have to make those submissions. I am not familiar with either the timetable or work plan of the task force.

**Senator ALLISON**—But you would expect it to be fairly soon, if cabinet is going to make a decision by—

**Mr Harms**—It would be sooner rather than later, I would think. It is October now.

**Senator STEPHENS**—I just went back to the explanatory memorandum, given that you said your role in this has been to develop the process by which government policy can be implemented. I notice, on the last page of your submission, the argument that the passage of the bills in the spring sittings is critical because the proposal to impose duty on biodiesel became effective from 18 September. Can Treasury advise of the industry impact? Can you quantify at all the industry impact of not actually passing these bills?

**Mr Harms**—In consultation with the Australian Taxation Office, arrangements are currently in place so that, in the short period leading up to 11 December, there should not be any financial implications for industry over the passage of this bill. Although biodiesels have become excisable since 18 September, the ATO has put in place arrangements to defer the collection of that duty—until, I think, 11 December.

**Mr Free**—Or until the grants are available—whichever is earlier.

**CHAIR**—We note from the concluding words of your submission the intrinsic urgency of this.

**Mr Harms**—The other element of it is actually providing certainty to industry. As I understand it, there is only one current producer of biodiesel. We heard from the witness tonight that their particular plant, although it is built, is not yet in production. However, we have had intelligence that they would be producing biodiesel sooner rather than later. So, in order to provide those players and others with certainty in which to operate, it is preferable that this bill is passed.

**Mr Free**—If I can add to that, that is insofar as it affects biodiesel, which is the first product to be subject to the grants process. While the grants for the production and importation of cleaner, low sulfur fuels will not commence until, it is anticipated, 1 January 2006, I recall the AIP witnesses stating that it would give the industry certainty because that will make very significant investments in refineries and the like some time ahead of that. While it does not directly affect them at the moment, there is an issue about providing certainty for those investments for cleaner fuels in the future.

**Senator STEPHENS**—I will just ask you a logistical question. Are you able to advise where the regulations are at in terms of being drafted?

**Mr Harms**—The regulations have been drafted.

**Senator STEPHENS**—They have been?

**Mr Harms**—They have been drafted, yes.

**CHAIR**—They have not been published, have they?

**Mr Harms**—No, and they have not yet been presented to the minister for approval. The timing of when this legislation is passed will govern the timing of those regulations going to executive council. As senators are probably aware, regulations cannot be made until primary legislation has received royal assent.

**CHAIR**—No, but draft regulations can be published and that practice has been observed in the past elsewhere. I understand there are limitations to that but, when you have the industry crying out for guidance, it is not an unusual thing for draft regulations to be published—and those who rely upon them are made very aware that they are only draft regulations. Nevertheless, that could be done here, couldn't it?

**Mr Harms**—I am not aware of regulations being published. Certainly none of the regulations I have been involved with in the past have been published. In one instance, we did make regulations available on a confidential basis to industry. But, at the moment, where we are at with the regulations is that they are in draft form.

**CHAIR**—So it is just a question of getting the minister to sign off on them.

**Mr Harms**—Yes. And at this stage they only affect biodiesel in any event.

**Senator STEPHENS**—Do the regulations as they are currently drafted incorporate performance measures to be placed on the production grants or anything like that?

**CHAIR**—I do not think that is a proper question, Senator. The regulations are not a public document. We have been told that. I do not think it is fair to inquire of these officers—or indeed of anyone—what is contained in what is, at the moment at least, a confidential draft.

**Mr Harms**—But, Senator, I think I can tell you in broad terms what the regulations contain. They can only prescribe what is given a head of power in the legislation in any case. The sort of thing that you just alluded to has no head of power in the legislation. What is prescribed in the regulations is firstly under the meaning of cleaner fuel, so, although the legislation itself specifies biodiesel, the regulations will go on to specify biodiesel when it is blended with diesel. The regulations will provide the rate, which is simply the equivalent of the excise rate since, until 2008, this scheme is intended to reduce the effective excise rate to zero. It will provide a formula for calculating the amount of grant which has specific application when biodiesel is blended with other products, since the grant would only apply to a portion of the final fuel. Other than that, I think that is all that is contained in the regulations.

**Senator STEPHENS**—There is one other comment at paragraph 1, page 19 on disqualifying circumstances, which mentions that the regulations may prescribe circumstances additional to those provided for in clause 7 that would disqualify a claimant from entitlement to a grant. I presume that refers to disqualifying circumstances other than the circumstances that qualify?

**Mr Harms**—And to circumstances other than the three above that in the legislation. There are no such circumstances prescribed, nor is there any intention to prescribe such circumstances. That head of power simply allows the ability to prescribe some future unknown event. If people organise themselves in such a way as to take advantage of the legislation beyond the original intent of the government, that head of power would allow the government to prescribe such an arrangement as being a disqualifying circumstance.

**Senator STEPHENS**—Thank you.

**CHAIR**—Mr Harms, Mr Free and Ms Preston, thank you very much. There were a couple of questions taken on notice. The reporting date for this committee is 16 October. Can I arbitrarily set Friday of this week as the date by which the answers to questions on notice are to be provided to the secretary. That concludes this public hearing. I thank the witnesses for their attendance.

**Committee adjourned at 8.56 p.m.**