

The Senate

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Economics Legislation Committee

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Provisions of the Energy Grants (Cleaner Fuels)  
Scheme Bill 2003 and the Energy Grants (Cleaner  
Fuels) Scheme (Consequential Amendments)  
Bill 2003

October 2003

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# LIST OF ABBREVIATIONS

ACE	Australian Coalition for Ethanol
AfMA	Australasian fleet Managers Association
AIP	Australian Institute of Petroleum
ALPGA	Australian Liquefied Petroleum Gas Association Ltd
ARFUELS	Australian Renewable Fuels Pty Ltd
ATO	Australian Taxation Office
cpl	cents per litre
LPG	Liquid petroleum gas
ppm	parts per million
PGBAA	<i>Product Grants and Benefits Administration Act 2000</i>
ULP	Unleaded petrol





# CHAPTER 1

## INTRODUCTION

### Reference of the Bills

1.1 On 17 September 2003, the Senate adopted the Selection of Bills Committee Report No. 11 of 2003 and referred the Energy Grants (Cleaner Fuels) Scheme Bill 2003 and the Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003 to the Senate Economics Legislation Committee for inquiry and report by 16 October 2003.

1.2 The reasons stated by the Selection of Bills Committee for referral of the bills were:

- The hasty submission of the bills;
- Questions as to the administrative and funding arrangements applying to biofuels and ethanol;
- The definition of a 'cleaner fuel' under the bills; and
- The continued subsidisation of the alternative fuel industry despite its perceived poor performance.<sup>1</sup>

### Purpose of the Bills

1.3 The purpose of these bills is to bring forward production of higher quality fuels before it is mandated under the provisions included in the *Fuel Quality Standards Act 2000*.<sup>2</sup>

#### The Energy Grants (Cleaner Fuels) Scheme Bill 2003

1.4 The Energy Grants (Cleaner Fuels) Scheme Bill 2003 provides a generic framework for the payment of grants for the importation and manufacture of cleaner fuels:

- The bill will initially allow for the payment of a grant for the importation and domestic production of final fuels containing biodiesel. The grant will offset the excise and customs duty payable on biodiesel from 18 September 2003 and continue the current excise rate of zero for 100 per cent biodiesel until 30 June 2008. The grant will also be payable of fuel blends containing biodiesel,

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1 Senate Selection of Bills Committee, Report No, 11 of 2003, 17 September 2003.

2 Explanatory Memorandum, Energy Grants (Cleaner Fuels) Scheme Bill 2003 and Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003, pp. 3-4.

extending an effective excise rate of zero to the biodiesel component of fuel blends for the same period.

- The bill will also provide for a grant to offset the excise and customs duty on the manufacture and importation of ethanol when the existing subsidy arrangements administered under contract by the Department of Industry, Tourism and Resources finishes on 30 June 2008.

1.5 The grant payable for biodiesel and ethanol will be progressively reduced in five even annual instalments beginning 1 July 2008 and ending 1 July 2012 to arrive at a final effective excise rate for these fuels.

1.6 The Energy Grants (Cleaner Fuels) Scheme Bill 2003 also allows for the payment of grants to encourage the introduction of low sulphur fuels. A grant will be paid for the importation and manufacture of premium unleaded petrol with less than 50 parts per million sulphur for a period of two years from 1 January 2006. A similar grant will be implemented for diesel with less than 10 parts per million sulphur from 1 January 2007.<sup>3</sup>

#### The Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003

1.7 The Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003 makes a number of consequential amendments as a result of the Energy Grants (Cleaner Fuels) Scheme Bill 2003. The bill brings the scheme under the administration and compliance framework of the *Product Grants and Benefits Administration Act 2000* (PGBAA). It also updates the registration provisions in the PGBAA to accommodate the requirement that claimants for a cleaner fuel grant register and claim under the existing provisions of that act.

1.8 Some of the amendments to the PGBAA have the effect of extending the offence in subsection 8C(1) of the *Taxation Administration Act 1953* to recipients of a cleaner fuel grant. These amendments are designed to ensure the integrity of the scheme by providing effective compliance measures.

1.9 The bill also makes some changes to certain provisions in the *Excise Act* concerning the administration, condition and duration of licences and amends both the *Excise Act 1901* and the *Fuels Quality Standards Act 2000* to make provision for information gathering and information sharing.

### **Background to the Bills**

1.10 In May 1999, the Government released *Measures for a Better Environment*. In this statement, the Government undertook to introduce an energy credit scheme to

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3 Explanatory Memorandum, Energy Grants (Cleaner Fuels) Scheme Bill 2003 and Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003, pp 3-4. See also submission 6, Treasury, pp. 2-3.

provide incentives and funding for conversion from the dirtiest to the most efficient and cleanest fuels.

1.11 The Government implemented this proposal through the *Diesel and Alternative Fuels Grant Scheme Act 1999*.<sup>4</sup> Section 4(2) of the Act stated that:

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

1.12 In March 2001, the Prime Minister announced that the Government was establishing an inquiry into the total structure of fuel taxation in Australia.

1.13 Subsequently, in October 2001 in the lead up to the November 2001 federal election, the Government released its *Biofuels for Cleaner Transport* position paper. In this paper, the Government:

- Made a commitment to maintain the fuel excise exemption for ethanol and biodiesel;
- Set an objective that fuel ethanol and biodiesel produced in Australia from renewable resources would contribute at least 350 million litres to the total fuel supply by 2010:
  - To implement the 350 million litre objective, the Government would provide through a grants process from 2002/03, a capital subsidy at the rate of \$0.16 per litre of biofuel produced for new or expanded domestic production infrastructure. The grant continues until total new domestic production reaches 310 million litres or the end of 2006-07, whichever is sooner.
  - To be eligible for the subsidy, a new or additional production plant would need to be able to produce a minimum volume of 5 million litres of biofuel each year. A maximum grant of \$10 million would apply for each new or expanded plant.<sup>5</sup>

1.14 The Fuel Tax Inquiry Committee subsequently handed down its report in March 2002. In its report, the Committee recommended that customs and excise duty should apply to all liquid fuels, irrespective of their derivation.<sup>6</sup>

1.15 The Government initially rejected this recommendation, at least partly on the basis that it was 'contrary to the Government's election commitment to maintain

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4 The Diesel and Alternative Fuels Grant Scheme Act 1999 has since been replaced by the Energy Grants (Credit) Scheme Act 2003, which commenced on 1 July 2003.

5 Coalition Government, *Biofuels for Cleaner Transport*, <http://www.liberal.org.au/policy/bio.pdf>, p. 2.

6 Fuel Taxation Overview Report, Summary of Recommendations, p. 29.

excise exemption for fuel ethanol and biodiesel.<sup>7</sup> However, in the 2003-04 Budget, this position was reversed. The government indicated that:

- a) To achieve a more consistent fuel excise regime and a more certain investment climate, effective excise rates for currently untaxed fuels would be increased in a series of five even, annual steps starting on 1 July 2008. The Government would determine final rates in due course. Final excise rates would have regard to the energy content of fuels.
- b) Existing subsidy arrangements for ethanol would continue until the new arrangements commenced in 2008. Broadly similar treatment would apply to biodiesel from 18 September 2003. That is, excise would apply but this would be fully offset by a subsidy until 1 July 2008.
- c) The Government would encourage the early take-up of ultra-low sulphur diesel by increasing the excise for regular diesel (compared to ultra-low diesel) by 1 cent per litre on 1 July 2003 and again on 1 July 2004. From 2006, further measures would encourage the production of clean petrol and zero sulphur fuels.

1.16 In accordance with this position adopted in the 2003-04 Budget, from 18 September 2003, biodiesel became subject to excise and customs duty. However, under the Energy Grants (Cleaner Fuels) Scheme Bill 2003, a grant equivalent to the amount of duty will be available to importers and manufacturers of biodiesel, giving an effective zero excise/customs rate.

1.17 Although not dealt with in the Bill, according to the *Explanatory Memorandum*, grants will also be made available under the cleaner fuels grants scheme for ethanol manufacture and importation once existing ethanol subsidy arrangements expire in 2008.<sup>8</sup>

## **Financial Impact of the Bills**

1.18 The *Explanatory Memorandum* states that the estimated cost of the biodiesel grant will be \$15 million in 2003-04, \$44 million in 2004-05, \$76 million in 2005-06 and \$99 million in 2006-07. The costs involved in respect of the low sulphur fuels are \$1 million in 2005-06 and \$41 million in 2006-07. These figures do not take into account the revenue to be raised by the imposition of excise and customs duty.

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7 Hon. Peter Costello, Treasurer, 'Report of the Fuel taxation Inquiry', Press Release No. 27, 14 May 2002.

8 Department of the Parliamentary Library, *Bills Digest No 33 2003-04: Energy Grants (Cleaner Fuels) Scheme Bill 2003*, pp. 1-2.

## Main Provisions of the Bills

1.19 The provisions of the Energy Grants (Cleaner Fuels) Scheme Bill 2003 deal specifically with the importation and manufacture of biodiesel, ethanol and low sulphur fuels.

### Clause 3

1.20 Clause 3 provides that the Commissioner of Taxation has general administration of the Act.

### Clause 4

1.21 Clause 4 contains key definitions, including:

- a) *Biodiesel* means fuel used for an internal combustion engine; and manufactured by chemically altering vegetable oils or animal fats (including recycled oils from these sources) to form mono-alkyl esters. Biodiesel must comply with the relevant fuel standard made under the *Fuel Quality Standards Act 2000*.
- b) *Cleaner fuel* means biodiesel or a fuel or blend prescribed by regulations that also complies with the relevant fuel standard.
- c) *A licensed person* is a person who is licensed under the *Excise Act 1901* as a manufacturer or the holder of a storage licence in respect of goods of a kind including fuel, or a person specified for permission given under the *Excise Act 1901* or *Customs Act 1901* for goods of a kind including the fuel.

### Clause 5

1.22 Clause 5 sets out the circumstances in which someone is provisionally entitled to a cleaner fuel grant. Essentially, the clause requires that a claimant must be either an importer, manufacturer or a licensed person in respect of a cleaner fuel, and only then if the cleaner fuel is consumed or sold into the market in its final form.

### Clause 6

1.23 Clause 6 provides that claimants for grants must be registered under section 9 of the *Product Grants and Benefits Administration Act 2000* for the purposes of entitlement to a cleaner fuel grant. Section 9 of that Act is itself amended by clause 3 in Schedule 1 of the Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003.

### Clause 7

1.24 Clause 7 sets out the circumstances in which a person meeting the requirements of clause 6 may nevertheless be disqualified from having a provisional entitlement to the grant. Those circumstances are:

- a) Selling the fuel to a licensed person;
- b) Including the fuel in a fuel blend;
- c) Where the Tax Commissioner makes a determination under subsection 34(1) of the *Product Grants and Benefits Administration Act 2000* that a person has taken a course of action ‘for the sole or dominant purpose of enabling a particular act or transaction to be taken into account in determining a grant or benefit’; or
- d) Where the regulations prescribe further disqualifying circumstances.

### Clause 8

1.25 Clause 8 indicates that if a person is entitled to a cleaner fuel grant, the entitlement is to be worked out in accordance with the regulations. In turn, the *Explanatory Memorandum* indicates:

Claimants will be required to self-assess their entitlements to a cleaner fuel grant. The regulations will prescribe different amounts of grant for different cleaner fuels and blends of fuels, including that the amount of grant may be nil. The regulations will also prescribe a basic rule for working out the amount of the grant payable and how the grant will be calculated if the regulations set out different amounts in respect of blends.

### Clause 9

1.26 Clause 9 sets out a standard regulation-making power.<sup>9</sup>

## **Submissions**

1.27 The Committee advertised its inquiry into the provisions of the Energy Grants (Cleaner Fuels) Scheme Bill 2003 and the Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003 on the internet and in *The Australian*. In addition, the Committee contacted a number of individuals and organisations alerting them to the inquiry and inviting them to make a submission. A list of submissions is at **Appendix 1**.

## **Hearings and Evidence**

1.28 The Committee held one public hearing on this inquiry at Parliament House, Canberra, on Tuesday, 7 October 2003. A list of witnesses is at **Appendix 2**.

## **Acknowledgement**

The Committee wishes to thank all those who assisted with its inquiry.

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<sup>9</sup> Department of the Parliamentary Library, *Bills Digest No 33 2003-04: Energy Grants (Cleaner Fuels) Scheme Bill 2003*, pp. 2-3.

# **CHAPTER 2**

## **THE PROVISIONS OF THE ENERGY GRANTS (CLEANER FUELS) SCHEME BILL 2003**

### **Introduction**

2.1 This chapter examines the evidence to the Committee during the inquiry on the principal provisions of the Energy Grants (Cleaner Fuels) Scheme Bill 2003:

- a) The payment of a grant to offset the excise on biodiesel from 18 September 2003; and
- b) The payment of grants to encourage the introduction of low sulphur fuels.

### **The Payment of a Grant to Offset the Excise on Biodiesel**

2.2 As indicated in Chapter 1, from 18 September 2003, biodiesel became subject to excise and customs duty at the rate of 38.143 cents per litre. However, under the Energy Grants (Cleaner Fuels) Scheme Bill 2003, importers and manufacturers of biodiesel will, in certain circumstances, be eligible for a grant equivalent to the amount of excise until 1 July 2008.

2.3 In its written submission, Treasury highlighted the importance of immediate implementation of the Energy Grants (Cleaner Fuels) Scheme Bill 2003 and the Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003 to ensure the availability of the grant:

The passage of these bills in the Spring sitting of Parliament is critical as the excise and customs tariff proposals to impose duty on biodiesel became effective on 18 September 2003. The imposition of duty on biodiesel in the absence of the corresponding provision of a grant has the potential to cause short-term cash flow problems for importers and manufacturers of this fuel. The Australian Taxation Office is currently deferring the collection of duty on biodiesel via an administrative arrangement until the EGCFs Bills are given Royal Assent. However, this arrangement is only suitable as a short-term contingency and passage of the bills is necessary to provide certainty to industry over the tax treatment of biodiesel.<sup>1</sup>

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1 Submission 6, Treasury, p. 4.

2.4 In the hearing on 7 October 2003, Mr Harms from Treasury indicated that the arrangement for the Australian Taxation Office (ATO) to defer collecting the excise is due to expire on 11 December 2003.<sup>2</sup>

#### The Availability of the Grant to Importers of Biodiesel

2.5 In its written submission, the Australian Biofuels Association argued that the provision of the grant under the Energy Grants (Cleaner Fuels) Scheme Bill 2003 to importers of biodiesel is inconsistent with the approach adopted in regard to ethanol. The Association suggested that the importation of highly subsidised ethanol from Brazil represents a threat to the establishment and viability of the domestic biofuels industry in Australia. Accordingly, the Association recommended that this provision be removed from the bill.<sup>3</sup>

2.6 This position was also expressed by Mr Gordon from the Australian Biofuels Association in the hearing on 7 October 2003:

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.<sup>4</sup>

#### **The Payment of Grants to Promote Low Sulphur Fuels**

2.7 In the 2003-04 Budget, the Government announced the following measures to encourage the use of low sulphur fuel in Australia:

- a) Payment of a grant for producing or importing diesel with 10 parts per million (ppm) or less sulphur content for two years from 1 January 2007, funded by an increase in excise/customs duty on all diesel sufficient to fund the proposal; and
- b) Payment of a grant for producing or importing premium unleaded petrol with 50 ppm or less sulphur content for two years from 1 January 2006, funded by an increase in excise/customs duty on all petrol sufficient to fund the proposal.<sup>5</sup>

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2 *Transcript of Evidence*, Harms, p. E.40.

3 Submission 14, The Australian Biofuels Association, pp. 6-7.

4 *Transcript of Evidence*, Gordon, p. E4.

5 Budget Papers 2003-04, Part 1, p. 1-23.



2.8 The Energy Grants (Cleaner Fuels) Scheme Bill 2003 provides a framework to deliver these grants for low sulphur fuels. The level of and conditions for the receipt of the grants will be set by regulation made under the bill.

2.9 In its written submission, the Australian Institute of Petroleum (AIP) – representing BP Australia Ltd, Caltex Australia Limited, Mobil Oil Australia Pty Ltd, and the Shell Company of Australia Ltd – strongly supported the measures and accordingly recommended the prompt passage of the bill.<sup>6</sup>

2.10 This position was reiterated by Mr Macpherson from AIP in the hearing on 7 October 2003:

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.<sup>7</sup>

2.11 In its written submission, AIP also noted that the provision of the grant would increase the flexibility of the petroleum industry to respond to cleaner fuel requirements. Companies can decide when to introduce cleaner fuels, prior to the imposition of mandatory standards under the *Fuel Quality Standards Act 2000*, based on their individual circumstances.<sup>8</sup>

2.12 The Committee also received separate submissions from BP Australia and Caltex recommending passage of the bill without delay. In particular, Caltex also strongly commended the Government for making the grant available, and also suggested that such an approach would promote the introduction of cleaner fuels sooner than mandated under the provisions included in the *Fuel Quality Standards Act 2000*.<sup>9</sup>

### The Benefits of Low Sulphur Fuels to the Environment

2.13 Parties to the inquiry also highlighted the environmental benefits of low sulphur fuel. For example, Caltex argued in its written submission that the most important development to improve air quality further in Australia is the development of petrol and diesel with reduced levels of sulphur. Such fuels allow for the fitting of

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6 Submission 11, AIP, pp. 1-2.

7 *Transcript of Evidence*, Macpherson, p. E10.

8 Submission 11, AIP, pp. 2-3.

9 Submission 7, BP Australia, pp. 1-2. Submission 10, Caltex, p. 1.

anti-pollution devices to reduce emissions of fine particulate oxides of nitrogen, which in combination create photochemical smog.<sup>10</sup>

2.14 Similarly, in its written submission, BP Australia argued that low sulphur fuels are in the national interest because they will directly and indirectly benefit:

- a) Air quality;
- b) Fuel efficiency, thereby reducing greenhouse gas production; and
- c) The consumer.<sup>11</sup>

2.15 Finally, the Committee also notes the advice of AIP that the US Environmental Protection Agency has found that there are significant community and environmental benefits to be gained from moving to low sulphur fuels.<sup>12</sup>

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10 Submission 10, Caltex, p. 2.

11 Submission 7, BP Australia, pp. 1-2.

12 Submission 11, AIP, p. 2.

# CHAPTER 3

## THE FINAL EXCISE RATE OR RATES

### Introduction

3.1 This chapter examines the final fuel excise rate or rates, to be implemented incrementally between 1 July 2008 and 1 July 2012, with reference to:

- a) The move to tax neutral treatment of competing fuels;
- b) Consultation with the industry on the Government's energy reforms;
- c) Means of determining the final excise rate or rates; and
- d) The impact of current uncertainty regarding the excise rate or rates.

### The Move to Tax Neutral Treatment of Competing Fuels

3.2 In the 2003-04 Budget, The Government indicated that it was moving to adopt tax neutral treatment of competing fuels after 1 July 2012 in order to remove taxation distortions that currently exist in the fuel market. The Budget Papers for 2003-04 state in part:

The Government will reform the fuel excise system to promote long-term sustainability and move to a neutral tax treatment between competing fuels. Reforms will also support the production of cleaner fuels and provide a more certain framework for investment in the fuels sector. This is consistent with the Government's strategic policy goal of an efficient and competitive energy sector.<sup>1</sup>

3.3 As indicated in Chapter 1, under this proposal, the effective excise rates for currently untaxed fuels such as liquid petroleum gas (LPG) would be increase in a series of five, even, annual instalments starting on 1 July 2008 and ending 1 July 2012. At the same time, the grant payable for biodiesel and ethanol will be progressively reduced in five even annual instalments beginning 1 July 2008 and ending 1 July 2012.

3.4 During the hearing on 7 October 2003, Mr Free from Treasury indicated that the decision to adopt tax neutral treatment of competing fuels was made on the basis that all fuels have a single fundamental purpose – powering internal combustion engines. This is regardless of the fact that different fuels have very different physical properties.<sup>2</sup>

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1 Budget Papers 2003-04, Part 1, p. 1-22.

2 *Transcript of Evidence*, Free, p. E.34.

3.5 The Committee also notes the evidence of Mr Harms from Treasury in the hearing on 7 October 2003 that the final excise rate or rates for different fuels, which will be implemented incrementally between 1 July 2008 and 1 July 2012, will be announced later in the 2003 calendar year, in accordance with the Treasurer's Press Release on Budget night. That Press Release stated:

The final excise rates to apply to fuels will be determined later this year and will take into account factors such as the energy content of fuels.<sup>3</sup>

## **Consultation with the Industry on the Government's Energy Reforms**

3.6 The Committee notes concern amongst some parties to the inquiry that they were not consulted prior to the move to adopt tax neutral treatment of competing fuels. For example, Mr North from the Australian Liquefied Petroleum Gas Association Ltd (ALPGA) indicated in the hearing on 7 October 2003 that the industry was not consulted prior to the 2003-04 Budget, although there was an opportunity to engage the Government's Energy Task Force.<sup>4</sup>

3.7 The Committee subsequently raised this matter with Treasury officials during the 7 October 2003 hearing. In response, Mr Free from Treasury indicated:

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.<sup>5</sup>

3.8 During the inquiry, various parties also argued that the setting of an excise rate or rates on alternate fuels reverses previous government commitments.

3.9 For example, the Australian Coalition for Ethanol (ACE)<sup>6</sup> argued that the proposal to implement an excise on ethanol from 1 July 2008 is inconsistent with the Government's earlier commitment in *Measures for a Better Environment* (May 1999) and *Biofuels for Cleaner Transport* (October 2001) to maintain the fuel excise exemption for ethanol and biodiesel.

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3 *Transcript of Evidence*, Harms, p. E.33.

4 *Transcript of Evidence*, North, p. E20.

5 *Transcript of Evidence*, Free, p. E.32.

6 A grouping of ethanol proponents, business organisations, regional Shires, Town and City councils, Chambers of Commerce and Independent Fuel Suppliers (primarily from Queensland).

3.10 In addition, ACE also cited to the Committee a letter dated 11 March 2002 from the Hon Warren Truss, Minister for Agriculture, Fisheries and Forestry, in which the Minister stated:

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.

3.11 Similarly, the Natural Gas Vehicles Group Pty Ltd noted in its written submission that the announcement of the excise on LPG was made almost exactly one year after the Treasurer's Media Release of 14 May 2002 in response to the Fuel Tax Inquiry which stated:

The proposal to tax all fuels based on their relative energy content would impose tax on previously unexcised fuels such as ethanol and LPG. This would have implications for the LPG retail fuel industry and LPG conversion businesses, and is also contrary to the Government's election commitment to maintain excise exemptions for fuel ethanol and biodiesel. For these reasons, the Government will not be implementing this recommendation.<sup>7</sup>

3.12 In response to these concerns, Mr Free from Treasury noted in the hearing on 7 October 2003:

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.<sup>8</sup>

## **Means of Determining the Final Excise Rate or Rates**

3.13 In its written submission, the Australian Biofuels Association indicated its understanding that the Government is proposed to move to a fuel excise system based solely on the energy content of a fuel. This is to be achieved by adopting the calorific value of each fuel based on British thermal units or megajules per litre.

3.14 This understanding was reiterated by Mr Gordon from the Australian Biofuels Association in the hearing on 7 October 2003:

... 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—

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7 Submission 13, The Natural Gas Vehicles Group Pty Ltd, p. 3.

8 *Transcript of Evidence*, Free, p. E.38.

indeed, no other country in the world, as far as our knowledge goes, has adopted this approach.<sup>9</sup>

3.15 However, a number of parties to the inquiry argued that the Government should set fuel excise rates based on a broader range of considerations than simply the energy content of a fuel.

3.16 For example, in its written submission, the Natural Gas Vehicles Group Pty Ltd argued that a fuel excise rate should be set specifically for natural gas based on the following considerations:

- a) The basic energy content of natural gas;
- b) An ‘environmental credit’ to take into account the environmental benefits of natural gas;
- c) A ‘resource security credit’ to take into account the benefits associated with natural gas as an abundant and secure indigenous resource; and
- d) An ‘energy futures credit’ to reflect the role that natural gas will play in the transition to the hydrogen economy.

3.17 This position was reiterated by Mr Black from the Natural Gas Vehicles Group Pty Ltd in the hearing on 7 October 2003.<sup>10</sup>

3.18 Similarly, Australian Renewable Fuels Pty Ltd (ARFUELS) advocated that fuel excise rates be based on a range of factors, notably greenhouse gas and air toxic impacts (especially given that low sulphur fuels are receiving preferential treatment under the bill).<sup>11</sup> ARFUELS argued that it would be inconsistent if biodiesel – an unequivocally cleaner fuel than diesel – was ultimately to be excised at the same rate as diesel. As stated by ARFUELS:

This would send a clear message that the Government considers the two fuels to be equivalent in all material aspects. However, the impact of biodiesel and diesel are equivalent only on a functional level. The economic, social and environmental impacts of the two fuels are completely different.<sup>12</sup>

3.19 The Committee examines below the range of factors which parties argued should be considered when determining the excise to be applied to a particular fuel.

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9 *Transcript of Evidence*, Gordon, pp. E4 – E5.

10 *Transcript of Evidence*, Black, p. E26.

11 Submission 12, ARFUELS, p. 5.

12 Submission 12, ARFUELS, p. 2.

### Australia's energy self-sufficiency

3.20 A number of parties to the inquiry argued that self-sufficiency in energy should be a factor in determining the rate of excise to be applied to certain fuels.

3.21 For example, the ALPGA argued that Australia's self-sufficiency in LPG helps Australia to be more self-reliant at a time of international insecurity, and that LPG should be given recognition for increasing Australia's energy self-sufficiency. The ALPGA cited figures that Autogas prevents the importation of 13 million barrels of oil (the Committee assumes per annum).<sup>13</sup>

3.22 By contrast to Australia, the ALPGA noted in its paper entitled 'The Role of LPG (Autogas) in Transport Fuel Policy' that other countries such as the US and Japan incur significant costs to ensure energy security. For example, the US Strategic Petroleum Reserve has a capacity of 700 million barrels worth \$US17.5 billion.<sup>14</sup>

3.23 Similarly, in its written submission, the Natural Gas Vehicles Group Pty Ltd noted that Governments around the world are taking steps to diversify transport fuel supplies and increase energy independence. However, the Group suggested that Australia is complacent in its expectation of ongoing reliable supplies of crude oil.<sup>15</sup>

3.24 Finally, the Australian Biofuels Association argued in its written submission that biofuels can play a role in increasing national energy security. In particular, biofuels such as ethanol and biodiesel have the unique advantage of being renewable fuels.<sup>16</sup>

### Environment

3.25 A number of parties to the inquiry also argued that the environment should be a factor in determining the rate of excise to be applied to certain fuels.

3.26 In general terms, the Australian Biofuels Association argued in its written submission that all alternative fuels when mixed with petrol and diesel fuels have the advantage of reducing emissions of uncombusted hydrocarbons and toxic aromatic components.<sup>17</sup>

3.27 In relation to the specific environmental advantages of biodiesel:

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13 Submission 3, ALPGA, p. 2, 5.

14 Cited in Submission 4, Elgas, p. 4.

15 Submission 13, The Natural Gas Vehicles Group Pty Ltd, p. 4.

16 Submission 14, Australian Biofuels Association, p. 2.

17 Submission 14, Australian Biofuels Association, p. 1.

- a) Equitox Management Pty Ltd noted in its written submission that biodiesel is the lowest emitter of greenhouse gasses of all fuels, with a sulphur content of less than 10 ppm.<sup>18</sup>
- b) ARFUELS argued in its written submission that biodiesel is an unequivocally cleaner fuel than diesel both in terms of greenhouse gas emissions and air toxics. ARFUELS noted that biodiesel is the only alternative fuel in the US to successfully complete Environment Protection Authority Tier I Health Effects Testing under section 211(b) of the Clean Air Act, which is claimed to provide the most thorough inventory of environmental and human health effects attributes that current technology will allow.<sup>19</sup>

3.28 Similarly, in its written submission, the ALPGA highlighted the environmental benefits of LPG. The ALPGA argued that LPG is an environmentally cleaner fuel (estimated up to 15 per cent lower carbon dioxide than petrol), and cited figures that Autogas currently reduces carbon dioxide emissions by more than 840,000 tonnes per annum.<sup>20</sup>

3.29 In turn, other parties argued that an excise penalty should be applied to environmentally unclean fuels like diesel. For example, in its written submission, the Australasian fleet Managers Association (AfMA) argued that an increase in the use of diesel in Australia at the expense of LPG would have an adverse impact on the health of the community, due to the output of nitrous oxides and particulate matter from combustion of diesel fuel. Indeed, AfMA cited a major US Environmental Protection Agency study entitled the 'Health Assessment Document for Diesel Engine Exhaust' which concluded:

DE (diesel exhaust) is considered to pose a human lung carcinogenicity hazard, which is expressed in a weight-of-evidence conclusion that DE is judged to be a 'probable' human carcinogen, or is 'likely to be carcinogenic in humans by inhalation' at environmental or higher exposure conditions.

3.30 AfMA also cited other studies in support of this position including the Victorian Environmental Protection Agency studies entitled 'Melbourne Mortality Study' and the 'Hospital Admissions Report' which clearly linked the incidence of mortality and hospital admissions to the levels of nitrous oxides and particle matter in the environment.<sup>21</sup>

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18 Submission 2, Equitox Management Pty Ltd, p. 3.

19 Submission 12, ARFUELS, p. 3.

20 Submission 3, ALPGA, pp. 2, 5.

21 Submission 8, AfMA, p. 2.



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### Distribution Mechanisms

3.31 Another factor cited to the Committee as a valid consideration when determining fuel excise rates was the fuel distribution network.

3.32 In its written submission, the ALPGA highlighted that the route to market for gaseous fuels such as LPG is totally different from that for ethanol and biodiesel. Fuels like LPG, Autogas and Compressed Natural Gas require dedicated fuel distribution, supply and delivery infrastructure as well as special vehicle engine systems. By contrast, ‘fuel extenders’ such as biodiesel and ethanol can be added to traditional oil-based petrol and diesel.<sup>22</sup>

### Employment

3.33 In its written submission, ALPGA argued that employment should also be a factor in deciding the rate of excise to be applied to different fuels. The ALPGA indicated that the LPG industry currently employs 15,000 – jobs which could be lost if the LPG industry moved offshore.<sup>23</sup>

### Regions

3.34 In its written submission, the ALPGA also argued that the maintenance of the regions should be a factor in deciding the rate of excise to be applied to different fuels. The ALPGA noted that many parts of Australia rely on LPG, but that without LPG’s availability at a reasonable cost, they would be forced to rely on electricity or wood.<sup>24</sup>

### Hydrogen Fuel

3.35 A final factor cited to the Committee as a valid consideration when determining excise rates for different fuels was the future development of the hydrogen economy. The Natural Gas Vehicles Group Pty Ltd noted that LPG is the most suitable path to the development of a hydrogen economy because the established refueling infrastructure to support natural gas vehicles could in turn be used to support hydrogen vehicles as they become available.<sup>25</sup>

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22 Submission 3, ALPGA, p. 1.

23 Submission 3, ALPGA, p. 2.

24 Submission 3, ALPGA, p. 2.

25 Submission 13, The Natural Gas Vehicles Group Pty Ltd, p. 5.

### The Recommendations of the Energy Task Force

3.36 In deciding the final rate of excise to be applied to different fuels, Mr Free from Treasury indicated that the Cabinet would be advised by the Energy Task Force, which will give consideration to factors such as those identified above.<sup>26</sup> Mr Free commented:

... 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.<sup>27</sup>

### **The Impact of Current Uncertainty Regarding the Excise Rate or Rates**

3.37 During the inquiry, a number of parties argued that the current uncertainty over the final fuel excise rate or rates has placed investment in the alternative fuel industries at risk, and has caused the immediate cessation of various projects. The Committee examines separately below the impact on the biodiesel/ethanol and LPG industries.

#### The Biodiesel and Ethanol Industries

3.38 In its written submission, ACE indicated that current uncertainty in the ethanol industry over the excise has already caused a number of projects to be put on hold. Those projects include:

- a) CSR projects to spend \$100 million to upgrade its Sarina Distillery and to develop a new, larger facility in the Burdekin, south of Townsville; and
- b) Dalby Bio-Refinery's proposed construction of a new plant, which went to tender for the first stage of construction in November 2002, with construction expected to have begun in early 2003. This is a \$79 million project.<sup>28</sup>

3.39 This concern was reiterated by Mr Elliott from ACE in the hearing on 7 October 2003. Mr Elliott noted that the current uncertainty over final fuel excise rates for biodiesel and ethanol is causing considerable uncertainty in the industry.<sup>29</sup> In relation to the Dalby Project, Mr Elliott noted that it has been on hold since September

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26 *Transcript of Evidence*, Free, pp. E.35-E.36.

27 *Transcript of Evidence*, Free, p. E.39.

28 Submission 5, ACE, p. 1. *Transcript of Evidence*, Elliott, p. E13.

29 *Transcript of Evidence*, Harrison, p. E12.

2002, and will be shelved permanently if there is not shortly some certainty about the future viability of the project.<sup>30</sup>

3.40 The Committee also notes the evidence of Mr Rose from the Australian Biodiesel Consultancy:

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 ...<sup>31</sup>

3.41 In turn, Mr Rose argued that the final rate of excise for biodiesel in 2012 should be well below that for diesel fuel, reflecting the environmental and other benefits of biodiesel.<sup>32</sup>

3.42 Similarly, Mr Gordon from the Australian Biofuels Association argued that the future of the biodiesel and ethanol industry will depend on the final excise rates applied to biodiesel and ethanol. However, without such information, Mr Gordon suggested that it is very difficult to speculate as to the future of the industry.<sup>33</sup>

#### The LPG Industry

3.43 Similar to the biodiesel and ethanol industries, a number of parties in the LPG industry also highlighted the impact that the current uncertainty regarding the final excise rate or rates is having on their industry.

3.44 For example, in its written submission, The Natural Gas Vehicles Group Pty Ltd argued that the announcement of the imposition of an excise on Autogas, in the absence of any details concerning the rate or any offsetting support programs, has led to a policy vacuum. This has created doubt, uncertainty and confusion in the minds of vehicle owners, fleet operators and infrastructure providers in the Natural Gas Vehicle Industry.

3.45 In turn, the Natural Gas Vehicles Group Pty Ltd cited evidence that all plans to invest in LPG vehicles and infrastructure have ceased. In particular, companies in the industry have shelved or abandoned projects involving tens of millions of dollars in sales due to the lack of clear policy direction and negative signals that have been given by the Government.<sup>34</sup>

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30 *Transcript of Evidence*, Elliott, pp. E13-E14.

31 *Transcript of Evidence*, Rose, p. E.29.

32 *Transcript of Evidence*, Rose, p. E.30.

33 *Transcript of Evidence*, Gordon, p. E4.

34 Submission 13, The Natural Gas Vehicles Group Pty Ltd, p. 3.

3.46 Similarly, in its written submission, the ALPGA noted that even though the excise will not be introduced until 2008, the Government's decision is having a direct impact now. The ALPGA cited cancellation of vehicle orders, reduction in resale value of vehicles, investment research, development and promotion plans put on hold, market uncertainty and threats to industry employment.

3.47 This was reiterated in the hearing on 7 October 2003 by Mr North from the ALPGA:

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.<sup>35</sup>

3.48 Finally, in its written submission, AfMA noted that several AfMA members are already indicating that they will either stop using or not consider using LPG.<sup>36</sup>

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35 *Transcript of Evidence*, North, p. E19.

36 Submission 8, AfMA, p. 3.

# CHAPTER 4

## THE TIMING OF THE GOVERNMENT'S ENERGY REFORMS

### Introduction

4.1 This chapter examines the timing of the Government's energy reforms, with specific reference to:

- a) The five-year excise free window for biodiesel and ethanol; and
- b) The incremental implementation of the excise on LPG from 1 July 2008.

### The Five-year Excise Free Window for Biodiesel and Ethanol

4.2 As indicated in Chapters 1 and 2, the Energy Grants (Cleaner Fuels) Scheme Bill 2003 provides a generic framework for payment of a grant for the importation and domestic production of biodiesel from 18 September 2003 until 30 June 2008. The grant will provide a 100 per cent offset of the excise and customs duty payable on biodiesel from 18 September 2003, an effective five-year excise free window. Similar administrative arrangements apply to the production of ethanol.

4.3 However, a number of parties argued in their written submissions that this five-year window is insufficient time for biodiesel and ethanol producers to achieve a competitive market position:

- a) The Australian Biodiesel Association argued that the time needed to develop the infrastructure for a new biodiesel plant would mean that any such plant would have only 1-2 years to recoup capital expenses before the imposition of the excise, making the venture unviable.<sup>1</sup>
- b) Similarly, Equitox Management Pty Ltd, which is a current refiner of canola oil, suggested that it would take approximately 18 months to build a biodiesel plant, leaving only 3 years in which to recoup costs prior to the imposition of the excise. Equitox Management Pty Ltd suggested that a viable business would require a lead time of at least until 2010.<sup>2</sup>

4.4 In addition, ACE argued in its written submission that the current projects in the pipeline to increase Australia's production of ethanol to around 350 million litres

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1 Submission 9, Australian Biodiesel Association, p. 1.

2 Submission 2, Equitox Management Pty Ltd, p. 3.

per annum by 2010, to meet the objective set by the Government in the *Biofuels for Cleaner Transport* position paper, will not go ahead if the Government implements its proposal to increase excise on ethanol from 1 July 2008.

4.5 Accordingly, ACE recommended that the excise rate on ethanol be maintained at zero. Alternatively, it recommended that new projects be guaranteed an effective minimum ten-year excise free period.<sup>3</sup>

4.6 The Committee notes that these arguments were reiterated during the hearing on 7 October 2003. For example, Mr Gordon from the Australian Biofuels Association indicated that the ethanol and biodiesel industries are currently not sustainable in direct competition with petroleum fuel without Government assistance. However, Mr Gordon suggested that within 10 years, the biodiesel industry could compete successfully, and that accordingly, a ten-year window for the payment of the grant would be more appropriate than the current five-year window. Mr Gordon continued:

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.<sup>4</sup>

4.7 Similarly, Mr Harrison and Mr Elliott from ACE argued that the five-year window is totally inadequate for any investment, and would not allow further growth of the industry.<sup>5</sup> As stated by Mr Elliott:

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.<sup>6</sup>

## **The Incremental Implementation of the Excise on LPG from 1 July 2008**

4.8 The Committee notes that in its written submission, Victorian Autogas Supplies Pty Ltd suggested that in the event that the excise levels proposed by the Fuel Tax Inquiry in March 2002 are implemented without any suitable buffers, then the LPG industry would be ‘destroyed almost overnight.’<sup>7</sup>

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3 Submission 5, ACE, p. 3.

4 *Transcript of Evidence*, Gordon, pp. E5-E6.

5 *Transcript of Evidence*, Harrison, p. E12.

6 *Transcript of Evidence*, Elliott, p. E15.

7 Submission 1, Victorian Autogas Supplies Pty Ltd, p. 1.

4.9 In support of this argument, Victorian Autogas Supplies Pty Ltd suggested that implementation of the recommendation made by the Fuel Tax Inquiry would lead to a drop in the differential between LPG and unleaded petrol (ULP) to 24.4 cents per litre (cpl). In turn, Victorian Autogas Supplies Pty Ltd cited the impact of similar short-term falls in the price differential between LPG and ULP following the introduction of the goods and services tax:

- a) In November 2002, the differential between ULP and LPG was compressed to as low as 34 cpl. This resulted in a 26 per cent drop in sales of LPG from the previous month, and a 34.4 per cent drop against November 1999 sales.
- b) In December 2002, the differential between ULP and LPG fell to below 30 cpl, leading to a 49 per cent drop in turnover (presumably on the previous month).<sup>8</sup>

4.10 Victorian Autogas Supplies Pty Ltd suggested that the reason the LPG market is so sensitive to price movements vis-à-vis the ULP market is that many LPG systems are dual fuel systems – they may also run on ULP. Accordingly, consumers will only continue to use LPG if they perceive that they are getting a financial benefit. Otherwise, they will revert to ULP.<sup>9</sup>

4.11 Similarly, in its written submission, AfMA, which represents over 600 members with responsibility for over 800,000 vehicles, suggested that even presently without the excise, the business case for purchasing alternative fuel vehicles is at best marginal and at worst a loss making venture.

4.12 To illustrate this point, AfMA cited the example of a dedicated LPG Ford, which it indicated retails at a \$1,400 premium to the normal ULP Ford, but resells at conservatively \$1,000 less. AfMA suggested that this combined penalty of \$2,400 would require a payback period of 85,000 km using the cheaper LPG.

4.13 Accordingly, AfMA argued that the Government's energy reforms and the imposition of the excise would render alternative fuels such as LPG effectively uncompetitive, and would further encourage the use of diesel as the fuel of first choice.<sup>10</sup>

4.14 Similar concerns were expressed in the hearing on 7 October 2003. For example, Mr Black from the Natural Gas Vehicles Group Pty Ltd indicated:

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

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8 Submission 1, Victorian Autogas Supplies Pty Ltd, pp. 1-2.

9 Submission 1, Victorian Autogas Supplies Pty Ltd, pp. 2-3.

10 Submission 8, AfMA, pp. 1-2.

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.<sup>11</sup>

4.15 In turn, Mr Neilsen representing Elgas indicated:

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.<sup>12</sup>

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11 *Transcript of Evidence*, Black, p. E.25.

12 *Transcript of Evidence*, Neilsen, p. E19.



# CHAPTER 5

## OTHER ISSUES

### Introduction

5.1 This chapter examines two issues raised during the inquiry in relation to the ethanol industry:

- a) The market environment for ethanol blended petrol – E10; and
- b) Whether there should be additional assistance to the ethanol industry.

### The Market Environment for Ethanol Blended Petrol – E10

5.2 In its written submission, ACE argued that Australian consumers have lost confidence in ethanol blended petrol (E10) in the light of the debate in Australia in late 2002 about the impact of ethanol on engines. In addition, ACE suggested that the ethanol industry has been damaged by a lack of a clear policy position from Government and the opposition of oil companies to ethanol.

5.3 However, ACE noted that in 2002-03, BP Australia conducted a E10 trial in Brisbane which went extremely well from a technical perspective, and demonstrated that E10 could be manufactured and marketed with no adverse impact on customer vehicles.

5.4 To address this concern, ACE advocated that all companies be obliged to remove all anti-ethanol references, all stakeholders endorse renewable transport fuels, and the federal government make an immediate announcement of participation in a major E10 trial.

5.5 Similarly, the Australian Biofuels Association noted that during the debate on ethanol fuel used in vehicles, all parties accepted that a 10 per cent ethanol blend was proven worldwide as a safe and reliable fuel that was warranted for use in new vehicles, and almost all of the Australian vehicle fleet. However, there remains pressure from vested interest groups for the selective and discriminatory labeling of ethanol on fuel pumps.<sup>1</sup>

5.6 This position was reiterated by Mr Gordon from the Australian Biofuels Association in the hearing on 7 October 2003. Mr Gordon noted that E10 has been used safely and reliably in the United States, Brazil and Europe for the last two decades, and that there is a clearly discernable move in countries such as India, China,

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1 Submission 14, The Australian Biofuels Association, p. 5.

Japan, Mexico and New Zealand towards biofuels as a means of ameliorating the impacts of petroleum fuel.<sup>2</sup>

### **Additional Assistance to the Ethanol Industry**

5.7 In its written submission, Equitox Management Pty Ltd argued that biodiesel is biodegradable and non-toxic, and is therefore particularly suited to use in confined spaces, the marine environment, and anywhere else that spillage is likely. Accordingly, Equitox Management Pty Ltd suggested that the grant on biodiesel should be increased to allow for biodiesel to compete in specific areas of national interest such as health and the environment. Examples would be the Great Barrier Reef and underground mining.<sup>3</sup>

5.8 In addition, Equitox Management Pty Ltd suggested the following initiatives to help producers of bio-fuels:

- Federal and state government initiatives to purchase biofuels;
- Advertising campaigns supporting the benefits of biofuels;
- Nationally recognised symbols or labels attached to fuels; and
- Labelling of fuels to include the benefits of the fuel.<sup>4</sup>

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2 *Transcript of Evidence*, Gordon, p. E2.

3 Submission 2, Equitox Management Pty Ltd, p. 3.

4 Submission 2, Equitox Management Pty Ltd, p. 4.

# CHAPTER 6

## CONCLUSIONS AND RECOMMENDATIONS

### **The Provisions of the Energy Grants (Cleaner Fuels) Scheme Bill 2003**

6.1 The Committee notes from the outset that the Energy Grants (Cleaner Fuels) Scheme Bill 2003 specifically provides for:

- a) the payment of a grant to offset the excise on biodiesel from 18 September 2003; and
- b) the payment of grants to encourage the introduction of low sulphur fuels.

6.2 The Committee considers that the payment of the grant to offset the excise payable on biodiesel from 18 September 2003 is a matter of considerable urgency. The Committee notes that the ATO is currently deferring the collection of duty on biodiesel via an administrative arrangement until the bill is given Royal Assent.

6.3 The Committee also notes that the move in the bill to promote the production or importation of low sulphur fuels received unanimous support from industry representatives during the inquiry.

6.4 Accordingly, the Committee recommends that the Energy Grants (Cleaner Fuels) Scheme Bill 2003 and the Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003 be agreed to immediately.

#### **Recommendation 1**

**The Committee recommends that the Energy Grants (Cleaner Fuels) Scheme Bill 2003 and the Energy Grants (Cleaner Fuels) Scheme (Consequential Amendments) Bill 2003 be agreed to.**

#### **The Final Excise Rate or Rates**

6.5 The Committee understands that the final fuel excise rate or rates will be announced later in the 2003 calendar year, in accordance with the Treasurer's Press Release on Budget night. However, the Committee wishes to comment on the following issues relating to the final fuel excise rate or rates.

### Consultation with the Industry on the Energy Reforms

6.6 The Committee acknowledges concerns that there was a lack of consultation with the industry prior to the announcement of the move to tax neutral treatment of competing fuels in the 2003-04 Budget. The Committee understands that industry parties continue to have the opportunity to make submissions to the Energy Task Force prior to the announcement of the final excise rate or rates, and encourages parties to contribute to this process.

### The Means of Determining the Final Excise Rate or Rates

6.7 The Committee notes concerns expressed by parties to the inquiry that the separate petroleum, LPG, biodiesel and ethanol industries have been indiscriminately grouped under the umbrella of a single final excise rate, to be based solely on the energy content of individual fuels.

6.8 The Committee understands that this matter is currently being assessed by the Energy Task Force, and that the Task Force will give consideration to a broader range of factors than simply energy content when recommending the final fuel excise rate or rates.

### The Impact of Current Uncertainty Regarding the Excise Rate or Rates

6.9 The Committee notes concerns that the current uncertainty over the final fuel excise rate or rates is placing investment in the biodiesel/ethanol and LPG industries at risk, and has caused the immediate cessation of various projects.

6.10 As indicated above, the Committee understands that the final fuel excise rate or rates will be announced later in the 2003 calendar year, which should bring some certainty to the industry. Regrettably, however, until this announcement is made, the Committee acknowledges that a number of parties remain in a difficult position.

## **The Timing of the Government's Energy Reforms**

6.11 The Committee notes the concerns of many parties that the Government's energy reforms place in jeopardy the future of alternative fuel industries in Australia.

6.12 In relation to the biodiesel and ethanol industries, it was argued that the five-year window until 30 June 2008 during which the grant will be provided to offset the excise on biodiesel and ethanol is insufficient for industry players to achieve a competitive market position. Many parties argued that a more appropriate time period would be a ten-year excise free period.

6.13 In relation to the LPG industry, parties expressed concern that the incremental imposition of an excise over five years from 1 July 2008 could potentially lead to the destruction of the LPG industry in Australia. Put simply, it was argued that the LPG industry needs Government support, and that without it, LPG would be uncompetitive in the marketplace.

6.14 Given these considerations, the Committee believes that there would be merit in the Government re-examining the so-called ‘five-by-five’ excise arrangements to determine whether additional time should be given to the alternate fuel industries to adapt to the Government’s energy reforms.

### **Recommendation 2**

**The Committee recommends that the Government re-examine the so-called ‘five-by-five’ excise arrangements to determine whether additional time should be given to the alternate fuel industries to adapt to the Government’s energy reforms.**

### **Other issues**

6.15 The Committee notes evidence in relation to the poor market environment for ethanol blended petrol, and particularly the recent controversy in Australia about the impact of ethanol on engines. The Committee recognises the importance of this issue, but does not believe that it is within the scope of this inquiry.

SENATOR GEORGE BRANDIS  
Chairman



# DISSENTING REPORT BY THE AUSTRALIAN DEMOCRATS

## Senate Economics Committee into the provisions of the Energy Credits (Cleaner Fuels) Scheme Bill

The purpose of the bill is to:

- set up an excise and grant framework for 'cleaner fuels' which will both encourage the production and/or importation of biodiesel and ultra low sulphur fuels, the latter, two years ahead of the dates by which they will be mandated,
- establish an immediate excise and offsetting grant system for ultra low sulphur diesel and ethanol
- provide the necessary regulatory arrangements for implementing the Government's May 2003 budget announcement that excise is to be applied to all alternative fuels commencing in 2008 and fully implemented by 2012.

The Government argues that the 'reforms establish a broad sustainable taxation framework for fuels by addressing a number of anomalies in the current fuel tax system and providing increased long term certainty for investors, while meeting government commitments and providing time for industry to adjust.'

However, evidence presented to the Committee suggests that the 'cleaner fuels' industry is unlikely to survive under the new excise scheme.

The Second Reading Speech states that the aim of the Bill is to:

"...to encourage conversion from the dirtiest fuels to the most appropriate and cleanest fuels for a new century." which is at odds with evidence provided by Treasury during the Committee's inquiry which makes it clear that the Bill seeks 'tax neutrality'. Treasury officials stated that the effect of tax neutrality would be to ensure that the resulting fuel stock mix in the market would be determined by market forces.

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.

### **Other related bills**

In June 2003 the *Energy Grants (Credit) Scheme* passed with the only measure for cleaner fuels being the excise differential on all petrol from 2006 to ensure the production of premium-unleaded petrol with less than 50 ppm sulphur. The Democrats did not support the legislation because it did not fulfil the Government's commitment in 1999 that *This scheme will be developed jointly by the Government and the Australian Democrats. It will ... provide price incentives and funding for conversion from the dirtiest fuels to the most appropriate and cleanest fuels.* Whilst the Democrats welcomed the earlier introduction of ultra low sulphur petrol, that fuel is not the 'most appropriate or cleanest fuel' for which incentives should be provided.

The *Customs Tariff Amendment Bill (No. 2) 2003* imposes an excise on fuel ethanol blended with petrol at the same rate as the excise on petrol, offset by an equivalent production subsidy. The bill imposes an equivalent customs duty on imported ethanol. This bill awaits debate in the Senate.

### **Basis for determining Grant Rates**

Alternative fuel industry witnesses argued persuasively that the application of excise (calculated according to calorific value) or 'competitive neutrality' will bring end to the use of LPG, CNG, LNG and biofuel as a transport fuel in this country because grant rates will not, by all accounts, be determined on criteria that would foster the local alternative fuels industry.

No evidence was provided by the Government - indeed it was advised that no modelling and no consultation had been conducted that would discover whether or not the industry could 'adjust' to the burden of excise by 2008 or by 2012. Nor has a sound case been advanced for applying an excise which does not measure or take into account the relative environmental, health, resource security or other merits of alternative fuels, relative to petrol or diesel, nor economies of scale, job or development opportunities. It is a 'cleaner fuels scheme' in name only unless these are taken into account.

Calorific value is not a useful base for determining excise because it does not reflect actual performance in petrol and diesel engines which is dictated by the efficiency of petrol and diesel engines in extracting the inherent energy in these fuels during the combustion process. Furthermore, oxygenates such as ethanol deliver extra oxygen to petrol, thus increasing the efficiency of the combustion process.



In the view of the Democrats, the bill should explicitly state that the objectives of the 'energy credits cleaner fuels scheme' include but are not limited to providing:

- a. economic incentives for the establishment of a sustainable 'cleaner fuels' industry,
- b. incentives for the establishment of a diversity of fuel stock types in the Australian fuels market;

The bill should set out the key criteria which will need to be taken into consideration when determining the rates at which the cleaner fuels excises and grants will apply to various fuels including:

- a. Environmental and greenhouse considerations;
- b. Energy security and diversity of fuel stocks in the market;
- c. Public health
- d. Economic development opportunities
- e. Investment and timeframe requirements in developing infrastructure, distribution and economies of scale.

A more transparent process is also required outlining how these criteria were addressed and how the rates were arrived at.

### **Additional Comments:**

The Committee's main report refers to 'the benefits of low sulphur fuels to the environment'. These are outlined in section 2.13 of the report.

Whilst there are significant benefits in using low and ultra low sulphur petrol and diesel, it is important to note the following points:

- The prevailing argument that clean diesels and new diesel engines eliminate the need for alternative fuels is invalid because sulphur content reductions do not necessarily deliver reductions in other toxics and where the same engine technology applies, alternative fuels can demonstrate better environmental outcomes.
- 10 ppm diesel fuel is likely to be at least 10 years away (if implemented at all) whereas alternative fuels can deliver at least equivalent benefits now.
- The CSIRO *Comparison of transport Fuels, Stage 2 study of Life-cycle Emissions Analysis of Alternative Fuels for Heavy Vehicles 2001* indicates that greenhouse gas, particulate matter, oxides of nitrogen and air toxic emissions

are significantly lower for CNG, LNG, and LPG than for ultra low sulphur diesel (ULSD).

- Scores for biodiesel and ethanol varied according to feedstock however all have lower emissions than low sulphur diesel. (See appendix 1). A more recent lifecycle study of ethanol shows significant reductions in CO<sub>2</sub> in both petrol-ethanol and biodiesel blends.
- It is a commonly held view that greenhouse emissions from gas vehicles are higher than diesel due to the relative inefficiency of the gas engine compared to diesel. In terms of efficiency, there is some validity to this argument when comparing gas vehicles with current diesel technology, however, low sulphur diesels and new diesel engines are in some cases less efficient and produce more greenhouse emissions than current diesel engines. As the production process for low sulphur diesels is also more energy intensive, this results in an increase in greenhouse emissions relative to old diesel. Euro 3 LPG systems are now demonstrating life cycle performance for greenhouse better than low sulphur diesel with the promise of improving this with a further 8% to 10% with the emerging technology.
- Gas-powered trucks are already meeting stringent Euro 5 emissions and will be significantly cheaper to maintain than diesel trucks beyond Euro 2 because of the exhaust after-treatment required.
- ULSD is not due to be mandated until 2006.

### **Legislated timeframes**

The Legislation allows the Government to establish an excise rate and a timeframe within which period that rate will have effect. Although the Government has indicated that no effective excise will apply for the five years between 2003 and 2008 and be phased in between 2008 and 2012, this will be determined by the regulations.

Evidence provided to the inquiry by Australian Biofuels Association, the Australian Coalition for Ethanol, Equinox Management Pty Ltd demonstrates that the 'five plus five' timeframe is far too short and takes no account of the establishment barriers for these transport fuel industries. Chapter 4 of the Committee's main report outlines these arguments and further supporting evidence was provided by Mr Gordon appearing before the Committee.

[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.

Whilst the Democrats oppose the 'one size fits all' approach to imposing excise on alternative fuels, preferring that targets are set for production and excise applied progressively as agreed targets are met, at the very least, the 'five plus five' timeframe should be extended and the excise-offsetting grant should not be scaled back for at least 10 years after establishment of the scheme.

### **Unfair to future entrants to the biofuels market**

The Democrats are concerned about the affects this legislation will have on producers who may not yet exist or have commenced production.

[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..?

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 3&half; 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.

A serious flaw in the concept of reducing a grant for all producers over a set time frame is its effect of preventing future competitors from entering the market. Existing entrants will have a significant competitive advantage having received the grant for a longer time frame during the initial establishment phase of the business.

As the volume of ethanol expected to be produced by projects known to be planned or already underway is relatively low as a proportion of the overall fuel market and falls short of the Prime Minister's target of 350ML by 2010, the exclusion of future entrants is unfair and counterproductive.

The Democrats hold the view that the periods for which a grant will be provided to producers should be uniform, regardless of the time of commencement of production..

## **Regulations**

Since excise and grant rates will be vital to the survival of the alternative fuels industry, the Australian Democrats do not support passage of this legislation without proper examination of and consultation on the regulations which will stipulate those rates.

Evidence provided by Treasury suggests that, despite public comments to the contrary, excise rate decisions have already been made and the Regulations have been drafted.

[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?

It is the opinion of the Democrats that the Draft Regulations should be made available prior to debate on the Energy Grants (Cleaner Fuels) Scheme Bill.

## **Importation**

In its written submission to the Committee the Australian Biofuels Association recommends that the provisions in the Bill to apply the cleaner fuels grant to imported biodiesel under part 2 section 5 of the Energy Grants (Cleaner Fuels) Scheme Bill 2003 be removed. The Democrats concur with this recommendation.

As acknowledged in chapter 2 of the Committee's main report, the Australian Biofuels Association argues that this provision would result in production subsidies being paid to foreign producers at the cost of local investment and job creation. Furthermore, the ABA argues that Brazilian ethanol is already subsidised and an additional subsidy would aid Brazilian importers in establishing a significant presence in the Australian

market at a time when Australian Producers were at a crucial stage of developing a local industry. The Australian Democrats believe that such a situation is against the interest of Australian producers, investors, jobs and therefore the Australian economy.

The Democrats will move amendments to the bills addressing issues raised in this report.

Senator Lyn Allison  
Australian Democrats



# Appendix 1

## Submissions Received

**Submission  
Number**

**Submittor**

- 1 Victorian Autogas Supplies
- 2 Equinox Management Pty Ltd
- 3 Australian Liquefied Petroleum Gas Association Ltd
- 4 Elgas Limited
- 5 Australian Coalition for Ethanol (ACE)
- 6 The Treasury
- 7 BP Australia Limited
- 8 Australasian fleet Managers Association (AfMA)
- 9 Adrian Lake
- 10 Caltex Australia Limited
- 11 Australian Institute of Petroleum
- 12 Australian Renewable Fuels Pty Ltd (arfuels)
- 13 The Natural Gas Vehicles Group Pty Ltd
- 14 Australian Biofuels Association





## **Appendix 2**

### **Public Hearing and Witnesses**

**Tuesday, 7 October 2003 Canberra**

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

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

FLETCHER, Mr Les, Director, Manildra Park

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

GORDON, Mr Robert, Executive Director, Australian Biofuels Association

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

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

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

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

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

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

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

