The Senate

Standing Committee on Economics

Tax Laws Amendment (Luxury Car Tax) Bill 2008

A New Tax System (Luxury Car Tax Imposition—General) Amendment Bill 2008

A New Tax System (Luxury Car Tax Imposition—Customs) Amendment Bill 2008

A New Tax System (Luxury Car Tax Imposition—Excise) Amendment Bill 2008

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Chapter 1

Introduction

Background

1.1 A New Tax System (Luxury Car Tax) Amendment Bill 2008 and three related bills[1] were introduced as part of the 2008 budget and referred to the Standing Committee on Economics on 18 June 2008, for report not before 26 August 2008.

1.2 The bill increases the rate of luxury cars tax (LCT) from 25 per cent to 33 per cent. The tax only applies to that portion of the price in excess of the LCT threshold, not to the total price. In 2008-09 the threshold will be $57 180, up slightly from the previous threshold of $57 123. The bill does not change the vehicles exempt from the tax or the threshold price at which the tax applies.[2]

Conduct of the inquiry

1.3 The committee advertised the inquiry in the national press and invited written submissions by 7 July 2008. Details of the inquiry were placed on the committee's website and the committee also wrote to a number of organisations and stakeholder groups inviting written submissions.

1.4 The committee received 18 submissions. These are listed in Appendix 1.

1.5 The reference required the committee to hold hearings in Adelaide and Melbourne, and listed some witnesses. The committee held public hearings in Adelaide (22 July), Sydney (31 July) and Melbourne (6 August). The organisations listed as witnesses in the reference appeared at the hearings.[3] The reference also referred to hearing evidence from the tourism industry, but no submissions were received from the industry and no representatives from the industry requested to appear as witnesses. The committee was also instructed to take into account the recommendations of the Bracks' *Review of Australia's Automotive Industry*. This review was only publicly released on 15 August, so its conclusions could not be

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1 A New Tax System (Luxury Car Tax Imposition General) Amendment Bill 2008, A New Tax System (Luxury Car Tax Imposition Customs) Amendment Bill 2008 and A New Tax System (Luxury Car Tax Imposition Excise) Amendment Bill 2008.

2 Exempt vehicles include emergency vehicles and vehicles specifically fitted out for transporting disabled people seated in wheelchairs.

3 The three Australian vehicle manufacturer/distributors (Ford, Holden and Toyota) appeared as witnesses, as did leading importer/distributors Audi, Mercedes and Toyota. The Federal Chamber of Automotive Industries, the Australian Automobile Association, the Victorian Automobile Chamber of Commerce and the Motor Trades Association of Queensland appeared in their own right, while the Motor Trades Association of Australia was represented by its South Australian, New South Wales and Queensland branches.

discussed at the committee's public hearings. As noted in this report, the review made no recommendations or comments about the LCT.

1.6 The committee thanks those who participated in this inquiry.

Background to the bills

1.7 The bills amend *A New Tax System (Luxury Car Tax) Act 1999* and related acts.[4] They form part of a package of measures in the 2008-09 Budget to enhance fairness in the tax system, in line with Labor party policy of reducing the tax burden on average wage earners.

1.8 The luxury car tax (LCT) was introduced on 1 July 2000 to replace the 33 per cent wholesale sales tax which had applied to luxury cars before the introduction of the Goods and Services Tax (GST).

1.9 *A New Tax System (Luxury Car Tax) Act 1999* and associated Acts imposed 25 per cent LCT on cars with a GST inclusive value over the LCT threshold, $55,134.[5] This threshold is adjusted annually when the CPI's motor vehicle purchase component has increased.

1.10 In 2007, 95 065 cars were sold that were over the LCT threshold, out of a total new car market of 815 153 vehicles, 12 per cent of the total market. Approximately 6 per cent of Australian manufactured vehicles sold in Australia incurred LCT.[6]

1.11 A car is defined as a motor vehicle that is designed to carry a load of less than two tonnes and fewer than nine passengers. Vehicles are exempt from LCT if they are:

- Over two years old at the time of supply,
- prescribed emergency vehicles,
- subject to GST and specially fitted out for carrying wheelchairs,
- a motorhome or campervan, or
- a commercial vehicle not designed for the principle purpose of carrying passengers.

1.12 The impact of the LCT rate increase is placed in some context in Table 1.1.

4 *A New Tax System (Luxury Car Tax Imposition General) Act 1999*, *A New Tax System (Luxury Car Tax Imposition Customs) Act 1999* and *A New Tax System (Luxury Car Tax Imposition Excise) Act 1999*.

5 The Car Depreciation Limit introduced in 1979 was adopted as the threshold for both the wholesale sales tax and the Luxury car tax.

6 VFACTS sales figures for Passenger vehicles and SUVs sold in Australia in 2007.

Table 1.1: LCT increase on selected models

Models	Pre-LCT Price	Sales	Fuel economy	LCT increase	
	$	Jan - Jul 08	L/100 km	$	% of overall price
(1) Toyota Corolla Conquest Hatchback	25,500	28,891	7.4	0	0
(2) Holden Commodore Berlina SA	45,290	28,229	11.3	0	0
(3) Mazda 3 MaXX Hatchback	25,500	20,297	8.2	0	0
(4) Ford Falcon FG XT sedan	37,990	18,229	10.5	0	0
(5) Toyota Yaris 5 dr 1.5	18,190	16,105	6.0	0	0
(18) Ford Territory TS Wagon 6sp (4WD)	48,990	8,294	12.2	0	0
(19) Subaru Forrester XT wagon Man 5sp (4WD)	38,990	8,136	9.3	0	0
(47) Nissan Patrol ST-L Wagon 5sp Man (4WD)	58,490	2,883	10.8	$241	0.4%
(62) Toyota Tarago GLi 6sp 3.5	54,990	1,915	10.2	0	0
Toyota Prius CVT	37,400	2,098	4.4	0	0
Holden Statesman Caprice SA 3.6i	67,990	1,193	12.2	$932	1.3%
Lexus RX350 Lux Wagon	85,900	1,546	11.2	$2,234	2.4%
Toyota Landcruiser Sahara Wagon Man (4WD)	94,990	7,119	14.5	$2,895	2.8%
Porsche 911 997 4S Coupe	243,000	258	11.0	$13,660	4.8%

Sources: Prices and fuel economy from *Top Gear Australia*, July 2008. Price excludes LCT, dealer delivery and statutory charges. LCT increase calculated as described in paragraph 1.13, assuming $2000 dealer delivery fee. Sales ranks calculated by Secretariat from Federal Chamber of Automotive Industries, VFACTS data for January – July 2008. Sales include all models for each vehicle type. The final column compares the increase in the LCT to the previous overall (LCT inclusive) price.

1.13 The LCT is calculated on the price of a car pre-GST, not the retail price of the vehicle. Therefore the LCT is calculated on the cost of the vehicle, less the LCT threshold and GST.[7] For example, a base model Holden Statesman, one of the highest-priced Australian-made cars, with a pre-LCT retail price of $67 990, with an additional dealer delivery fee of $2 000 would have incurred LCT of (69 990-57 180)*(10/11)*0.25= $2911, giving a final all up cost of $72 901. After the increase, the LCT payable would be (69 990-57 180)*(10/11)*0.33= $3843, an increase of $932.

7 Claims, such as by Mr John Chapman, Motor Trades Association of South Australia, *Proof Committee Hansard*, 22 July 2008, p. 16; and Australian Automobile Dealers Association, *Submission 13*, p. 1; that LCT is 'a tax on a tax' are misplaced.

Chapter 2

Key issues

2.1 While the bill only raises the LCT *rate* and does not alter the *threshold*, most of the submissions and witnesses devoted considerable attention to arguing for an increase in the threshold or an outright abolition of the LCT. Only Mercedes-Benz suggested an alternative source of revenue, advocating a gradual replacement of the LCT by a tax on vehicle emissions, which could also fund incentives for people to replace old polluting vehicles with cleaner ones.

Increasing coverage of the LCT over time

2.2 An increasing proportion of vehicles have been captured by the Luxury tax threshold. When the wholesale sales tax on luxury vehicles was introduced in 1986, it applied to 4.5 per cent of light vehicles.[1] In 2007, the LCT applied to 12 per cent. Unsurprisingly, this was regarded as a bad thing by the importers and sellers of cars whose voices dominated the submissions and hearings. Whether it is justified could be said to depend on whether the LCT is seen as a tax on 'luxury' or 'prestige'.

2.3 There are many 'luxury' features that were formerly only available on a very select range of cars but which are now available on many other models. Features such as cruise control, sophisticated air conditioning, ABS, multiple airbags, CD players, fuel injection, satellite navigation and reversing sensors were once only found in the most expensive cars but are now more common. On this argument, as there are more cars with luxury features, it is perfectly reasonable for more cars to be subject to luxury car tax.

2.4 On the other hand, it might be said that community standards of what is a 'luxury' have increased. It might then be argued that a car is a prestige, luxury car only if it has features and specifications substantially above the norm. This argument holds that the LCT threshold should not be tied to the current method of indexation but should have a substantial increase to reflect that view.

Indexing the LCT threshold

2.5 It was commonly argued that the increased coverage was due to an inappropriate means of indexing the LCT threshold. The LCT threshold is indexed to the motor vehicle purchase component of the consumer price index (CPIMV). As with

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1 Information provided by FCAI.

the rest of the CPI, the Australian Bureau of Statistics conducts surveys to determine actual prices paid for vehicles and weights them by sales to consumers.[2]

2.6 The most contentious aspect of the CPIMV involves the use of quality adjustment.[3] The Australian Bureau of Statistics explain:

> Whenever a specification change is made to a vehicle that affects its motoring performance, economy, comfort level, safety or durability… an adjustment is made to the car's reported price to allow for that portion of the price change that can be attributed to the quality change.[4]

2.7 There has been a steady increase in the features of car models (either adding entirely new features or features formerly available only as options at additional cost now being standard). As a result, although the listed price of a standard 'family 6' sedan has risen, the CPIMV has fallen.

2.8 While it is an effective measure of inflation, the CPIMV is arguably not an appropriate measure for indexing the value of a luxury car threshold, simply because it does not reflect actual prices paid by consumers. Many of the quality improvements that the CPIMV uses to discount car prices have no bearing on the luxury component of a car. Improvements in the safety features of all models have been prominent in the quality improvements since 1996, including technologies such as anti-lock brakes, airbags, seatbelt pre-tensioners and traction and stability control, however the fitting of these safety features to cheaper cars has contributed to the fall in the CPIMV. For example the recent decision to require electronic stability control on all new vehicles will result in a quality improvement across the board, however any associated cost increase will be discounted.

2.9 The CPIMV will continue to lag behind vehicle prices and this is likely to result in an increasing proportion of vehicles being subject to the tax over time. However, there is a large concession made to the industry in applying indexation. The threshold is adjusted only when the CPIMV *rises*. When the CPIMV falls, as is often the case, the threshold is not lowered.

2.10 Less discussed is whether the movements in car prices in general captured in the CPIMV are representative of those of luxury cars. Given that most luxury cars are imported, their prices have probably risen by less than those of the 'family 6' car in recent years as the Australian dollar has been appreciating.

2.11 Even the listed prices of cars have risen by less than the CPI as a whole and average earnings. Importers and dealers would therefore prefer that the threshold were

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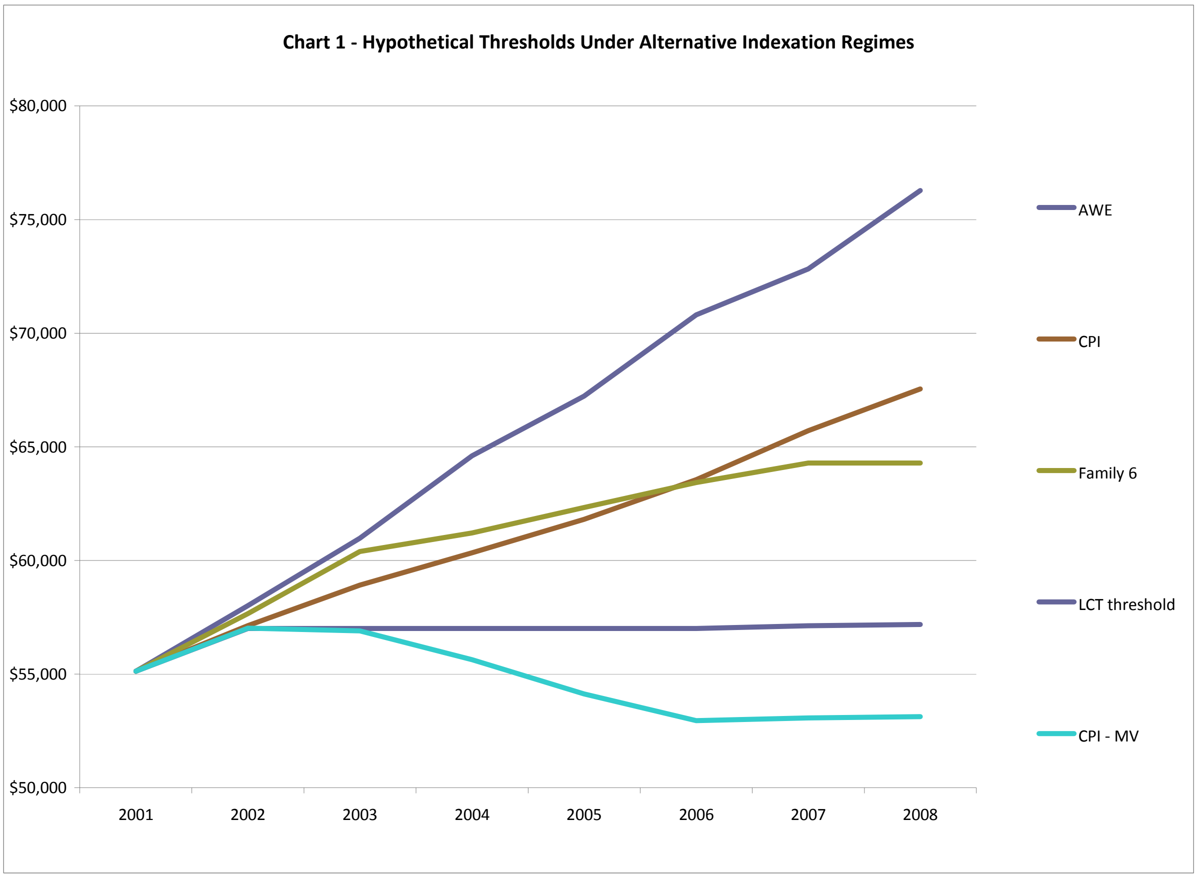
2 Accordingly, fleet sales are disregarded and luxury cars have a small weight in the basket.

3 Quality adjustments are applied in principle to all components of the CPI but are in practice more important for items such as cars and consumer electronics than for basic foodstuffs or clothing.

4 ABS, *Australian Consumer Price Index: Concepts, Sources and Methods*, 2005.

indexed to one of these measures instead, and it would be more consistent with the idea of LCT as a tax on prestige.

2.12 The actual change in the LCT threshold is compared to that under some alternative indexation regimes in Chart 1.



2.13 If the argument that the LCT threshold should have been indexed to the total CPI rather than to the pure price of luxury cars is accepted, the threshold would need to rise to around $70 000. This would lower the percentage of cars sold subject to the LCT to around 5 per cent of the market.[5]

2.14 The FCAI submission pointed out that cars priced between the current threshold and $70 000 (although being the majority of cars subject to LCT) contribute less than a fifth of the revenue raised.[6] However, not only would raising the threshold cut the number of cars subject to LCT, it would reduce the LCT raised from each of the cars still subject to the tax. Indeed, raising the threshold in this way would probably offset the additional revenue raised by increasing the LCT rate from 25 to 33 per cent.[7] (The luxury car tax threshold is equal to the car depreciation limit used to

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5 Based on FCAI figures supplied in *Submission 8b*.

6 FCAI, *Submission 8b*, p.4

7 Assuming no change in demand from 2007 sales figures.

calculate depreciation deductions. Therefore raising the threshold would also affect revenue by increasing the limit unless the two were explicitly differentiated.)

The impact on the LCT rate increase on car prices and the CPI

2.15 As the LCT only applies to the value in excess of the threshold, the price increases for cars affected by the LCT are much less than the 8 per cent increase in the tax rate (see Table 1.1). For example, if the tax increase is fully passed on to buyers the price of a $100 000 car will increase by $3 100. While car prices in Australia range up to $1.2 million for a Rolls Royce Phantom convertible, cars priced under $70 000 contribute the majority of the LCT. The additional LCT is equivalent to about 2 per cent of the average price of vehicles subject to LCT, based on 2007 sales figures.

2.16 The extent to which the tax increase is passed on will depend on the price elasticity of demand. This is likely to be considerably lower for luxury cars than for standard cars.

2.17 Around 90 per cent of new cars sold in Australia fall below the threshold, so there is no direct impact from the LCT increase. Around 95 per cent of Australian made cars sold in Australia fall below the threshold.[8] Allowing for export sales, a higher proportion of Australian made cars are not affected by the LCT.

2.18 It was suggested that the tax led to prices 'bunching' just below the threshold; 'a pricing log jam in the $50,000 to $55,000 bracket'.[9] This might suggest making the tax effect stronger would moderate prices of cars near the threshold, and that raising the threshold would increase car prices.

2.19 A simple calculation suggests the overall impact on the consumer price index will be negligible. Motor vehicle purchase has a weight of around 5 per cent in the CPI, so if the price of 10 per cent of cars sold were to increase by around 2 per cent as a result of the LCT rate increase, the total CPI might have a one-off increase of 0.01 per cent.[10]

8 Information provided by FCAI.

9 Mr Russell Scoular, Ford Australia, *Proof Committee Hansard*, 6 August 2008, p. 8.

10 ABS Cat. no. 6430.0 gives the weight of motor vehicles in the CPI as 4.9% as at June 2005. The proportion of cars affected is discussed in paragraph 1.10. Figures on revenue and volume of sales by price were provided by FCAI. A more sophisticated estimate would be likely to be even smaller. Some of the tax increase will be absorbed by manufacturers or dealers rather than passed on to consumers, and there will be a modest deflationary impact as car buyers have less money to spend on other goods and services.

The impact of the tax on sales of cars

2.20 The impact on sales will depend on the price elasticity of demand. There is general consensus that is considerably lower for luxury cars at the higher end of the market than for standard cars. Audi Australia identified their A4 models – which range from $50 000 to over $90 000 – as being price sensitive, and the company anticipates a 20 per cent reduction in overall sales, but noted that above $100 000, 'it is a different game'.[11]

2.21 A few industry spokespersons were asked for estimates of the decline they expected in sales of cars subject to LCT:

> …conservatively in the order of 18 per cent.[12]
>
> we believe, based upon our internal assumptions of price elasticity, that we will have a 20 per cent drop of cars above the luxury car threshold.[13]
>
> increasing vehicle prices in the Porsche market segments by the amount reflected with the LCT moving from 25 to 33% is likely to result in a reduction of sales of between 10 to 13% – for Porsche and its segment competitors.[14]
>
> It is very difficult to judge at this point… we have to be mindful that all of our competitors are facing the same increase.[15]

2.22 However while the market is described as price sensitive, the tax will affect all manufacturers equally, so the impact should be much lower than if just one marque increased the prices of their models. Additionally, in the price range where demand is identified as being most elastic, close to the threshold, the overall price increases will be low.

2.23 The increase in the LCT is likely to result in sales of vehicles slightly above the LCT decreasing and sales of vehicles slightly below the LCT threshold increasing. Buyers in the $65 000 - $95 000 may downgrade their purchase, or alternatively forgo optional extras. Purchasers of four wheel drives are likely to get more extra equipment fitted as aftermarket options, which will not attract the tax.

2.24 Analysis of luxury car sales provided in data sources to the Committee for July indicate that sales of vehicles subject to LCT are down compared with the same period last year. However, the results vary dramatically across market segments – with some types of vehicles showing increased sales – and sales are still higher than the

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11 Mr Joerg Hofmann, Audi Australia, *Proof Committee Hansard*, 31 July 2008, p.

12 Mr Andrew McKellar, Federal Chamber of Automotive Industries, *Proof Committee Hansard*, 22 July 2008, p. 10.

13 Mr Joerg Hofmann, Audi Australia, *Proof Committee Hansard*, 31 July 2008, p. 2.

14 Porsche Australia, *Submission 5*, p. 2.

15 Ms Vesna Katic, Toyota Australia, *Proof Committee Hansard*, 6 August 2008, p. 5.

same period in 2006. Some of the July slump just represents sales being brought forward to June to beat the LCT increase. Current economic conditions, high fuel prices and uncertainty over whether the tax increase will pass the Senate, and if so, how it will be applied are further confounding factors which prevent any meaningful conclusions being drawn from July sales on the impact of the LCT rate increase.

The impact on Australian manufacturers

2.25 Some submissions claim the LCT hits a niche market in which the Australian motor vehicle manufacturing industry specialises and it will therefore reduce the viability of Australian manufacturers. Australian manufacturers concentrate largely on large family sedans and the upper ends of the model ranges for these vehicles are subject to LCT. The submissions claim manufacturing costs in Australia are relatively high and the manufacturers rely on good domestic sales to ensure the operation is viable.

2.26 However, there are only a small proportion of Australian-made cars priced above the threshold. Furthermore, the tax does not affect exports.

2.27 The Bracks *Review of the Australia's Automotive Industry* noted the existence of the LCT but did not find it had any adverse impact on Australian manufacturers. It made no recommendations for any changes to the LCT.

2.28 The LCT increase may make Australian-made cars priced below the threshold more competitive with imported models priced above the threshold, so it may provide a fillip to domestic manufacturers. Indeed, this is apparently the view of the European Commission, which 'takes… a very dim view of the luxury car tax'.[16]

Government revenue implications

2.29 The LCT generated approximately $440 million in revenue in 2007-08, or 0.14 per cent of total Australian government tax revenue. The increase in the LCT rate is expected to raise additional revenue of $130 million in 2008-09, increasing over subsequent years.[17] Any impact on sales from the LCT increase will lead to a partial offset to the revenue raised by increasing the tax rate.

2.30 An impact on sales may lead to some reduction in GST revenue from car sales.[18] However, people who decide against buying a car, or buy a cheaper car, as a result of the increase in the LCT are likely to spend the money on something else subject to the GST so total GST revenues are unlikely to be affected significantly.

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16 Mr David McCarthy, Mercedes-Benz Australia, *Proof Committee Hansard*, 6 August 2008, p. 22.

17 *Explanatory Memorandum*, p.1

18 A point made by Mr David Purchase, Victorian Automobile Chamber of Commerce, *Proof Committee Hansard*, 6 August 2008, p. 15.

The impact on rural residents and families

2.31 A number of witnesses argued that the increase in LCT will unfairly hurt rural residents:

> For those living in rural and regional areas, access to safe, reliable and convenient family transport is absolutely essential. They often need to drive on unsealed roads, particularly during flooding in the wet season, so they need enhanced vehicle stability and durability and they need long-range fuel capacity.[19]

2.32 Large and comfortable four wheel drive vehicles have been increasing in price and levels of equipment and as a result many are now priced above the threshold, especially once options such as bullbars and winches are added. Several submissions have highlighted the fact that substantially more four wheel drive, or 'SUVs', now fall above the LCT threshold, from less than 1 000 vehicles in 1979 up to 38 000 in 2007

2.33 However, there are still many four wheel drive vehicles priced below the LCT threshold (see Table 1.1 for some examples). Both the people mover and four wheel drive categories straddle the LCT threshold for most manufacturers. For example, in Toyota four wheel drives, only the Landcruiser 200 series starts its model range above the LCT threshold. As a result, the decision to purchase a vehicle subject to LCT is still discretionary for all buyers who require these vehicles.

2.34 For purchasers who do elect to buy a vehicle at the higher end of the model range, the increase in tax is not likely to represent a substantial increase in the overall purchase price. For example, a purchaser who decides to buy a top of the range Toyota Prado, or a Landcruiser VX wagon around the $80 000 mark on the new rate will incur under $2 000 additional tax, less than 2.5 per cent of the overall purchase price.

2.35 The 'people mover' class of vehicles is similar to the four wheel drive market. According to VFACTS statistics the vast majority of people movers sold are under $55 000 and very few would exceed $80 000. Only one of the five Toyota Tarago models is priced over the LCT threshold.

2.36 The increase in the number of four wheel drives above the LCT threshold partly reflects a cultural shift in the perception of four wheel drive vehicles and a concomitant shift in their equipment and pricing. Four wheel drive sales have risen dramatically, while the rural population has been shrinking. Four wheel drive manufacturers increasingly target a more affluent demographic and differentiate their vehicles by equipment, rather than off-road performance or price. This shift in the purchasing demographic means that any attempt to differentiate four wheel drive vehicles from other luxury cars is likely to benefit more urban than rural residents.

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19 Mr Andrew McKellar, Federal Chamber of Automotive Industries, *Proof Committee Hansard*, 22 July 2008, p. 2. A similar point was made by Mr Mark Coulton MP, *Submission 17*.

The rationale for taxing luxury cars at a higher rate than other goods and services

2.37 A number of submissions and witnesses point out there is no distinguishing feature which would single vehicles out from other luxury or 'status' goods – such as private yachts, or jewellery – which do not attract a similar tax.[20] As Audi Australia argued; 'Australia is one of very few countries in the world which has something like the luxury car tax'.[21]

2.38 The replacement of sales tax with the GST was partly motivated by a desire to have a (more) uniform rate of indirect taxation which it was argued would lessen the extent to which the taxation system distorts consumption decisions. On this logic, equity considerations would be managed through the broader tax-transfer system, not through differential taxes on specific categories of goods preferred by low-income or high-income households.[22]

2.39 Some witnesses argued there are no other products subject to a tax when the price exceeds a threshold.[23] While not an exact analogy, stamp duties could be seen as a form of 'luxury home tax' as in many states (first home) purchases of cheaper houses are not taxed and the tax rate increases with the price.

2.40 In its favour, the LCT is a progressive tax which is relatively easy to collect. It is equitable in that it taxes those most able to afford it.

2.41 The LCT falls almost entirely on discretionary purchases, although views differ about whether this is a good or bad feature of a tax.

2.42 The main theoretical arguments for deviations from uniform tax rates on goods and services is addressing 'externalities' or raising revenue for the benefit of specific sectors of the community. These are the rationales underlying other deviations from uniform taxation such as the excises on fuel, tobacco and alcohol (and the future impost on carbon emissions) and various agricultural levies.

2.43 The original 1986 wholesale sales tax appears to have been a protectionist measure, designed to increase the price of European imports, while the 2000 LCT was

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20 For example, Mr John Chapman, Motor Trade Association of South Australia, *Proof Committee Hansard*, 22 July 2008, p. 16; Mr David Purchase, Victorian Automobile Chamber of Commerce, *Proof Committee Hansard*, 6 August 2008, p. 14; and Mr McCarthy, Mercedes-Benz Australia, *Proof Committee Hansard*, 6 August 2008, p. 22.

21 Mr Joerg Hofmann, Audi Australia, *Proof Committee Hansard*, 31 July 2008, p. 3. Ms Vesna Katic from Toyota reported the Philippines has a luxury car tax; *Proof Committee Hansard*, 6 August 2008, p. 5.

22 Treasury [Henry Review], *Architecture of Australia's Tax and Transfer System*, p.281.

23 For example, Mr Peter Griffin, Toyota Australia, *Proof Committee Hansard*, 6 August 2008, p. 2.

introduced to ensure the introduction of GST did not result in a sudden reduction in the price of luxury vehicles, apparently because this might erode support for the GST.

2.44 The European Union, and some importers, have criticised the LCT as a disguised form of protection for the Australian car industry. According to the European Commission, 90 per cent of vehicles subject to the LCT are imported and 50 per cent are from Europe.[24]

The effect of the LCT and the proposed increase in the LCT rate on the adoption of vehicle safety features and environmental technologies.

2.45 Because safety and environmentally friendly technologies appear first as optional equipment, they usually appear on luxury vehicles first, but gradually diffuse to standard models.[25] Some submissions and witnesses argued that the LCT discourages innovation by taxing these technologies:

> The luxury car tax is a 33 per cent tax on safety features and low-emission technologies. If a customer seeks the fitting of airbags to a vehicle priced over the luxury car tax threshold then the customer will incur a 33 per cent additional tax.[26]

2.46 It is possible that at the margin fewer buyers of luxury cars will buy these features as the price of these options has increased. It was suggested that in some cases dealers would not import models with superior safety features as the LCT increase led to buyer resistance.[27]

2.47 However, the development and production of these types of advanced technologies represents part of the core business for luxury car manufacturers and they are unlikely to remove features from more than a small fraction of their models. Mercedes stated that they never de-specify their vehicles and summarised their reason:

> This is our core value of our brand and we are very aggressive and have been over the last years to bring down the pricing as best as we can but we never take any technology, whether it is safety or environmental technology, out of our cars.[28]

24 VACC, *Submission 11*, attachment C; European Commission's submission to Bracks review.

25 Examples include airbags, anti-lock brakes and stability control.

26 Mr Tim Reardon, Federal Chamber of Automotive Industries, *Proof Committee Hansard*, 22 July 2008, p.2.

27 This point was made in general by Mr Tim Reardon, Federal Chamber of Automotive Industries, *Proof Committee Hansard*, 22 July 2008, p.5.

28 Mr Horst Van Sanden, Mercedes Benz, *Proof Committee Hansard*, 6 August 2008, p.23

2.48 In some cases buyers may be able to avoid the LCT by having additional safety features fitted after the car is bought rather than paying for them as an option from the manufacturer.

2.49 The Australian market represents too small a segment of the overall global car market – probably less than 2 per cent – to affect major manufacturers' research and development budgets. This point was conceded by Toyota:

> The tax would not impact on Toyota’s global research and development activity.[29]

2.50 There are concerns that the faster increase in listed car prices than in the threshold of the LCT may have a negative impact on sales for any future hybrid vehicles larger and more capable than those currently on the market. The Toyota Prius currently falls below the LCT threshold, while the Lexus Hybrids are above it. Future hybrids targeting the gap between these models are likely to fall around the LCT threshold in price. Toyota has argued on environmental grounds that hybrid cars should be exempt from the LCT.[30]

2.51 It has also been argued that luxury cars are safer and more fuel efficient than other vehicles and so the LCT effectively represents a tax on these features. While some luxury vehicles may be more efficient in terms of fuel used per kilowatt generated than some below the threshold, the size of the engines fitted to these vehicles, and their generally larger weight, means that very few actually burn less fuel per kilometre. The median fuel consumption for cars under the LCT threshold is under 9 litres of fuel to travel 100 kms, while the median for models subject to the LCT is over 10 litres.[31] A similar point can be seen from the examples in Table 1.1.

2.52 The fitting of vehicle safety features such as traction control to luxury vehicles is largely a marketing decision, rather than an economic one in most cases. While the technologies do increase the costs of a vehicle and will take time to appear on low end vehicles, the cost is small in comparison to model markups at the luxury end. These features are fitted to luxury vehicles rather than midrange cars in order to differentiate them from lower specification models. The LCT does not represent a tax on safety technologies, it represents a tax on a marketing decision by manufacturers.

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29 Mr Peter Griffin, Toyota Australia, *Proof Committee Hansard*, 6 August 2008, p. 7.

30 Toyota Australia, *Submission 7*, pp 5-6.

31 Secretariat calculation based on fuel economy data from *Top Gear Australia*, July 2008, and median of car models selling more than 100 vehicles in 2008, based on VFACTS sales data.

The impact on corrective services

2.53 One example cited in a submission to the inquiry is the use by the ACT Department of Justice and Community Safety of specially modified vehicles to transport persons in custody. While the baseline cost of these vehicles is below the LCT threshold, the cost of the modifications required to render the vehicles fit for their intended purpose raises them above the threshold. While emergency vehicles are exempt from the LCT, these vehicles do not qualify.

The impact on historic vehicles

2.54 While it is a tiny segment of the market, there is an anomaly in the way historic vehicles are handled. Vehicles over two years old or imported over two years ago are exempt from LCT. Some classic and vintage car enthusiasts have drawn attention to the fact that a classic or vintage car which would be exempt if purchased within Australia attracts the LCT if it is imported for sale. There is no tax on selling the cars outside Australia. Over time this may lead to a loss of Australia's motoring heritage.[32]

2.55 There may be a case to provide an exemption for vehicles over a certain age, such as more than 30 years old. Such an exemption would address the imbalance and the tiny proportion of such vehicles likely to be imported is unlikely to have any significant impact on the economic effect of the tax or revenue generated.

32 Mr John Burt, Sporting Car Club SA, *Proof Committee Hansard*, 22 July 2008, p. 13; Association of Motoring Clubs, *Submission 14*.

Chapter 3

Conclusion

3.1 The currently high inflation rate is a reason for tighter fiscal policy. Given that high income earners have got significant income tax cuts, and are probably benefiting more from the resources boom than are low income earners, the committee regards it as reasonable for them to bear the burden of higher prices for luxury imported goods, whose prices have in many cases fallen due to the stronger Australian dollar.

3.2 The committee sees some merit in the argument that it is 'unfair' that luxury cars are taxed but not other luxury purchases such as yachts or expensive artworks and jewellery. However, as there is already a luxury cars tax, there are less administrative and compliance costs in increasing it, rather than introducing new taxes on other luxury goods. Introducing any more general luxury taxes should await the Henry review of the tax system.

Recommendation 1

3.3 The committee recommends that the Senate pass the bill.

3.4 The committee was not convinced by the submissions calling for the threshold to be raised. There are many comfortable, environmentally responsible and safe new vehicles (not to mention second-hand vehicles) available priced well under the current threshold, including vehicles with four wheel drive and other features required by drivers in remote areas.

3.5 The committee thought a reasonable case had been made that the treatment of imported historical vehicles may be anomalous and would like Treasury to investigate this further.

The 'retrospective application' of the LCT increase

3.6 There has been criticism of the uncertainty generated by the tax applying to cars delivered after 1 July but the bill not having passed the Senate yet. The vendor of a vehicle is responsible for paying the tax and it is a matter of their commercial judgement whether or how they pass the tax on to their customers. Complaints about this process are effectively criticisms of tax office procedures and the decision of the Senate to conduct an inquiry and have no bearing on the merits of the bill itself.

Senator Annette Hurley

Chair

Dissenting Report from Coalition Senators

Senators Alan Eggleston (Deputy Chair), the Hon. Eric Abetz Barnaby Joyce and David Bushby

A tax grab based on the politics of envy

On Sunday 11th May News Ltd newspapers reported that the Rudd Labor Government planned to increase the rate of the Luxury Car Tax from the current 25 percent to 33 percent. The article, by Glenn Milne, was titled “hit the rich” and espoused the following Government rationale for the tax increase:

> A HEFTY tax increase on luxury cars emerged yesterday as the latest move … aimed at targeting the rich and curbing inflation.[1]

The move was confirmed as a budgetary measure later that day by Treasurer Wayne Swan, who told Laurie Oakes on Nine’s “Sunday” program:

> We think it is only fair that people who can afford these cars make a small contribution in that savings effort.[2]

In other words, the proposed eight per cent increase in the Luxury Car Tax is only about increasing the Government’s revenue stream at the expense of the so-called “rich” who drive these vehicles.

In Senate Estimates on Monday 2nd June 2008, the Minister for Innovation, Industry, Science and Research, Senator Kim Carr, confirmed that the tax was a reintroduction of class warfare:

> We had this expectation that we should go on providing assistance and various other measures to millionaires …You cannot remember saying that?
>
> Senator Carr—I think you will find that was in relation to the luxury car tax.[3]

Figures provided by the Federal Chamber of Automotive Industries reveal that almost 70 percent of cars sold annually, which are subject to Luxury Car Tax, are sold for less than $75,000 – not the cars of 'millionaires'.[4]

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1 Glenn Milne, 'Hit the rich', *Sunday Mail*, 11 May 2008, p. 1.

2 Wayne Swan, “Sunday”, Channel 9, 11 May 2008.

3 Senate Economics Committee, *Senate Estimates Hansard*, 2 June 2008, pp 69-70.

4 Federal Chamber of Automotive Industries, *Submission 8b* , p. 4

Coalition Senators note that it is incongruous for the Government to claim, as they did, that the budget will “curb inflation”, when the proposed Luxury Car Tax will increase the price of the most common “luxury” car, the Toyota Landcruiser Wagon, by almost $1,000.[5]

The sole reason Labor offers for the proposed Luxury Car Tax surcharge is to fight inflation (paragraph 3.1 in the Government Majority Report). Yet at paragraph 2.19 of their report Labor Senators acknowledge a CPI increase (albeit small) as a result of the increased tax grab.[6]

So rather than a curb on inflation, the Luxury Car Tax increase will by Labor’s own admission actually fuel inflation.

Pre-empting Bracks' Review / Henry Review

Despite appointing former Labor Premier Steve Bracks to undertake a review into Australia’s automotive industry, and Treasury Head Ken Henry to undertake a 'root and branch' review of Australia’s tax system, the Government moved to increase the rate of the Luxury Car Tax before hearing their recommendations.

In the case of Mr Bracks’s inquiry at least, there is evidence that Mr Bracks was minded to reduce, not increase the luxury car tax:

> …the increasing number of Australian-made models now subject to the LCT as the threshold has not kept pace with price increases for upper-end vehicles. In addition, the inclusion of more safety and other features in upper and luxury vehicles is also increasing their price.[7]

Coalition Senators note that the announced tax increase effectively nobbled Mr Bracks’s proper consideration of the tax increase in his review, for despite recommending that:

> States and territories should consider the harmonisation and reduction of stamp duties, vehicle registration and compulsory third party insurance to facilitate the purchase of new [or newer second-hand] vehicles…[8]

Mr Bracks did not address the Luxury Car Tax in his final report, other than to note that a bill to increase it is currently before the parliament, when the report was finally released on the 15th August, after the Committee had concluded taking evidence.

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5 Based on average 2007 selling price of $70,705 pre-LCT.

6 Labor Senators’ majority report at 2.19: “the total CPI might have a one-off increase of 0.01 per cent.”

7 Review of Australia’s Automotive Industry, *Discussion Paper*, March 2008, p. 11.

8 Review of Australia’s Automotive Industry, *Final Report*, 22 July 2008, p. 7

Coalition Senators are surprised at the assertion by Labor Senators at 2.27 of their report, that the Bracks' Review *'did not find it [the Luxury Car Tax] had any adverse impacts on Australian manufacturers'.* We cannot locate this finding in Mr Bracks' Report - unfortunately, the Labor Senators' assertion is not footnoted.

Disappointingly, a request by the Coalition for the release of Mr Bracks' report prior to the end of the Committee's hearings was ignored.

Senate inquiry

On the 18th June the Senate agreed to a Coalition proposal to refer the package of bills comprising this proposed tax increase – the Tax Laws Amendment (Luxury Car Tax) Bill 2008, A New Tax System (Luxury Car Tax Imposition—General) Amendment Bill 2008, A New Tax System (Luxury Car Tax Imposition—Customs) Amendment Bill 2008 and A New Tax System (Luxury Car Tax Imposition—Excise) Amendment Bill 2008 - to the Senate Standing Committee on Economics for report not before 26 August 2008.

The inquiry examined:

a. the incidence of the Luxury Car Tax (LCT) and the effect of the proposed increase in the LCT rate on rural and regional communities, small business, families and tourism operators;

b. the effect of the LCT increase on the prices of vehicles, the affordability of motor vehicles, the cost of living, and the consumer price index (CPI);

c. the expected impact of the increase in the LCT rate on vehicle demand and the likely consequences for government revenues including from the LCT, goods and services tax (GST) and stamp duty;

d. the growing incidence of the LCT over time and the adequacy of current arrangements for indexation of the LCT threshold, in comparison with alternative measures including the CPI, average weekly earnings and the increase in the retail price of motor vehicles;

e. the rationale for taxing `luxury' cars at a higher rate than other goods and services;

f. the effect of the LCT and the proposed increase in the LCT rate on Australian vehicle manufacturers and vehicle importers and distributors;

g. the overall taxation burden on ownership and operation of motor vehicles including customs duty, GST, LCT stamp duty and excise on fuel;

h. the effect of the LCT and the proposed increase in the LCT rate on the adoption of vehicle safety features and environmental technologies; and

i. the extent to which the LCT is viewed as a non-tariff barrier by other car exporting countries.

and held public hearings in Adelaide, Sydney and Melbourne.

Eighteen submissions were received, and evidence was given to the Committee by eleven organisations and individuals.

History of the Luxury Car Tax

The Luxury Car Tax was introduced by the Hawke Labor Government in August 1986, with an increase in the rate of tax on "luxury" vehicles from the standard 20 per cent wholesale sales tax for all vehicles to 30 per cent tax for "luxury" vehicles.[9]

Contrary to Labor spin, the tax was not introduced in 1979 by the Fraser Government – rather, this was when the luxury car vehicle depreciation limit was introduced – but it was not a tax.[10]

Having introduced the tax in the 1986 budget, its rate was increased to 50 per cent in May 1990 – when it was opposed by the Coalition Opposition at the time. The Opposition spokesman, Peter Reith, said:

> This is nothing but an envy tax without justification…while we are talking about a luxury tax, why do we not have a tax on antique clocks, surely a luxury and something of great interest to the Treasurer. We will oppose it here and we will oppose it in the Senate.[11]

In August 1990, a split tax rate was introduced with sales tax payable on luxury vehicles being the lesser of 50 per cent; or 30 per cent up to the statutory threshold and 75 per cent on the value above the threshold; with the threshold retail value for luxury tax being the same as the depreciation limit - $45,056 in 1990-91.[12]

In May 1995 this was adjusted to be 22 per cent for the first $36,995 wholesale price (corresponding to about $55,000 retail) and 45 percent on the balance above $36,995.[13]

In 2000, with the abolition of wholesale sales tax, the Luxury Car Tax was adjusted to the current situation whereby GST is applied to the purchase price PLUS a further 25 percent tax is applied to the purchase amount above the threshold, currently set at $57,180. This largely retained the status-quo of the pre-GST system and was at the request of large sections of the automotive sector.

9 Industry Assistance Commission, *Report into the Automotive Industry*, 17 December 1990.

10 Industry Assistance Commission, *Report into the Automotive Industry*, 24 June 1981.

11 The Hon. Peter Reith, *House Hansard*, 15 May 1990.

12 Industry Assistance Commission, *Report into the Automotive Industry*, 17 December 1990.

13 Productivity Commission, 27 May 1997.

Rationale for a luxury car tax

A number of submissions and witnesses to the inquiry raised concerns about the rationale for taxing cars at a higher rate than other goods.

As the Victorian Automobile Chamber of Commerce (VACC) pointed out in their submission to the inquiry:

> Other high-priced consumer goods are not taxed as luxuries, holidays, expensive homes, expensive restaurant meals, holiday homes, yachts are not taxed as luxuries. Other imported goods such as furniture, artworks, plasma televisions, jewellery, watches and antiques are similarly not taxed as luxuries. Yet vehicles are taxed as luxuries, VACC challenges the assumption that cars should be taxed as a luxury.[14]

The same argument was put rather more succinctly by Mr Andrew McKellar of the Federal Chamber of Automotive Industries:

> No other goods and services are "luxury" items according to the tax system.[15]

Evidence was presented outlining that cars are already one of the highest taxed goods in the country. Taxes applied to vehicles and their uses include:

- Tariffs;
- GST;
- FBT (on employers and employees);
- Stamp duties on new purchase and transfer;
- Stamp duties on insurance premiums;
- Registration fees;
- Compulsory third party insurance;
- Fuel excise (and GST on this excise);
- GST on repairs and maintenance;
- Road access fees (tolls); and
- Luxury Car Tax.[16]

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14 VACC, *Submission 11*, p. 4.

15 *Proof Committee Hansard*, 22 July 2008, p. 3.

16 As cited in VACC, *Submission 11*, p. 9.

Coalition Senators agree that motor vehicles already face a high tax burden and restate the Coalition's view that taxes should always be as low as possible.

Coalition Senators also note that no other comparable country has a luxury car tax. British Columbia, which is a province of Canada, has a 2-3 per cent 'luxury' car tax; Pakistan has a two percent tax on 'luxury' vehicles; and in 2007 Venezuelan leader Hugo Chavez was quoted as having plans to impose a tax on 'luxury' items such as Hummers.[17]

What defines a 'luxury' car?

During hearings, varying evidence was given as to what should define a 'luxury' car, and where the threshold for 'luxury' kicks in.

Even a Labor Senator had his own definition of what defined a 'luxury' car during the Melbourne hearing:

> You have said that you cannot tell me, but it seems to me that the LandCruiser you have put forward may have a five disc CD changer, it may have Bluetooth, it may be iPod integrated, and it may have leather seats. It could be quite a luxury model for a car.[18]

Coalition Senators disagree with Labor's view that safety items such as Bluetooth capability are a luxury in today's environment, noting that many cars which fall well under the luxury car threshold come with Bluetooth as a standard, such as the Holden Commodore.

Perhaps the most illuminating contribution as to the definition of a 'luxury' car came from Mr McKellar of the Federal Chamber of Automotive Industries, discussing how in his view a Toyota Landcruiser was not a 'luxury' vehicle, despite being classified as one by the Luxury Car Tax threshold:

> This vehicle retails at a price of around $54,000 or $55,000, but with the addition of a few options and accessories, such as air-conditioning, a bullbar and a winch, it incurs luxury car tax. For those driving on rural roads, unsealed roads, frequently having to dodge wildlife and so on, the addition of those sorts of features is quite normal. Equally, operating in high temperatures, the use of an air-conditioning system in a vehicle like that also makes good sense. It would hardly, in this day and age, be considered to be a luxury. I must say that that vehicle, which incurs increasing amounts of luxury car tax, comes standard without carpet. The interior is fitted out in vinyl as standard so that you can hose out the inside. That was the vehicle that introduced Australians to the Toyota brand back in the 1950s. The LandCruiser earned a reputation for reliability and

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17 http://edition.cnn.com/2007/WORLD/americas/10/15/venezuela.sin.tax/index.html.

18 Senator Doug Cameron, *Proof Committee Hansard*, 6 August 2008, p. 6.

> versatility during the construction of the iconic Snowy Mountains scheme, but today, according to the definitions of the luxury car tax, it is a luxury vehicle.[19]

The Toyota Landcruiser is Australia's best-selling so-called 'luxury' car, with just over 6,000 sold in Australia in 2007.

Coalition Senators note that in addition to the Toyota Landcruiser, there are a number of family vehicles and four wheel drives currently subject to Luxury Car Tax which should not be considered 'luxury' vehicles, including:

- Toyota Prado $66,874;
- Toyota Tarago $64,887;
- Mitsubishi Pajero $64,447;
- Ford Territory $62,657; and,
- Nissan Patrol Wagon $62,116

Coalition Senators note that these are all vehicles that are predominantly driven by either people in rural and regional Australia, or by those with the need for a 'people mover'.

Bracket Creep

The threshold for the Luxury Car Tax is indexed according to the CPI motor vehicles subset. The vast majority of submissions and witnesses gave evidence that this index has been inadequate in ensuring that the threshold rises at the same rate as real car prices, resulting in the number of cars captured by the 'luxury' car concept rising from 2.5 percent of all cars in 1979, to 11 percent in 2008.

In an attachment to their submission prepared by Australian Automotive Intelligence, the Federal Chamber of Automotive Industries outlined why they believed the current indexation model for the Luxury Car Tax is flawed:

> The methodology used for incorporating new vehicle price into the CPIMV has effectively reduced the price change because of the adjustment of prices for "quality" improvement in vehicles – quality in these terms can be broadly seen as changes in specifications. Over the long history of rising vehicle specifications, the CPIMV therefore does not fully reflect the increase in prices actually paid for cars.[20]

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19 Mr Andrew McKellar, *Proof Committee Hansard*, 22 July 2008, pp 2-3

20 FCAI, *Submission 8a*, p. 2.

The CPI-MV has risen only four times since 2000, from $55,134 in 2000 to $57,009 in 2002 to $57,123 in 2007 and then to $57,180 in 2008 – a 0.46 per cent annual increase when inflation has averaged around 3.3 per cent over the same period.

This has resulted in a number of vehicles previously being below the Luxury Car Tax threshold now being above the threshold. For example, the 2000 Mitsubishi Pajero was not a 'luxury' car, but the 2008 model is.

In evidence given to the Committee, the Federal Chamber of Automotive Industries contended that on current trends and on the current indexation model, up to half of all motor vehicles sold in Australia will be subject to the Luxury Car Tax by 2030.[21]

The Chamber presented evidence to the Committee showing various scenarios indexing the Luxury Car Tax threshold since 2000. These showed that while the Luxury Car Tax has increased from $55,134 to $57,180 since 2000, during the same period the threshold would be $71,106 using the CPI; $79,950 using Average Weekly Earnings; and $63,504 if indexed against the average price of the cheapest Family Six.[22]

Coalition Senators are concerned that the current indexation model for the Luxury Car Tax is not adequately reflecting real price increases in cars. This has amounted to a tax increase by bracket creep.

Recommendations

The Luxury Car Tax threshold should be indexed to the CPI, rather than the current CPI-MV subset.

The issue of the appropriateness of the current threshold of the Luxury Car Tax be further considered.

Coalition Senators note that rate of the Luxury Car Tax is currently set and indexed at the same rate as the Car Depreciation Limit.

Recommendation

That the Luxury Car Tax threshold be decoupled from the Car Depreciation Limit threshold and the issue of the Car Depreciation Limit threshold be referred to the Henry Review of Taxation.

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21 Mr Andrew McKellar, *Proof Committee Hansard*, 22 July 2008, p. 2.

22 FCAI, *Submission 8b*, p. 2. 'Family Six' refers to base model Holden Commodore and Ford Falcon.

The Australian car industry – from protectionism to discrimination

The percentage of Australian-made cars subject to the Luxury Car Tax has increased over time.

> Back in 1979, when the threshold was originally introduced, only the Holden Caprice and the Ford LTD were above that threshold. Today, all Australian-made vehicle models have variants that exceed the so-called luxury car tax threshold. So there is a much greater range in terms of Commodores, Ford Falcons, the Ford Territory, the turbo Ghia model and even Toyota's recently produced Aurion...It is not inconceivable that in the future we could see mid-range and even base-model Falcons and Commodores being defined as luxury cars under this legislation.[23]

According to the VACC, the proposed Luxury Car Tax increase will adversely affect the local manufacturing sector:

> For instance, while sales of the Holden Commodore in the $35k to $45k price bracket have fallen from 60,658 in 2005, to 41,331 in 2007, sales of models over $55k have doubled from 6,073 in 2005 to 11,990 in 2007.
>
> Similarly, while Ford has seen a fall in around 25% of sales in the $35k to $45k bracket, sales in the $55k bracket have remained constant…
>
> The tax hits a vital segment of the local manufacturing sector that has been growing or maintaining sales, while sales in other segments have been falling, and any increase in the tax will simply exacerbate this situation.[24]

This view was backed by Ford Australia during hearings in Melbourne:

> I would describe the position of the threshold, Senator, as being at an inappropriate level to today's market place and the fact that where the threshold itself is causing harm on the domestic industry.[25]

How this takes place was explained by Mr McKellar from the Federal Chamber of Automotive Industries:

> In terms of the local industry, our analysis shows that there is a significant distortion in the marketplace. If you take vehicles up to a threshold of about $70,000, more than 50 per cent—in fact, it approaches 60 per cent—of all vehicles incurring the luxury car tax fall within that range. Just below the threshold there is an equal distortion in the marketplace. The impact that that has is quite significant for the local manufacturers, because the price range of Holden Commodore, Ford Falcon, Toyota Aurion and Camry begins to push up towards that threshold. As that occurs they are moving into a space where there are more and more models, more and more brands,

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23 Mr Andrew McKellar, *Proof Committee Hansard*, 22 July 2008, p. 4.

24 Victorian Automobile Chamber of Commerce, *Submission 11b*, p. 1.

25 Mr Russell Scoular, Ford Australia, *Proof Committee Hansard*, 6 August 2008, p. 10.

> competing at the same price level as people try to minimise the tax burden that they incur upon their customers.[26]

During Committee hearings in Melbourne, Labor Senators ran the argument that this five percent of Australian-made cars subject to the Luxury Car Tax are at the top end of the model range, and therefore should be subject to an extra tax.[27]

In response, Coalition Senators note the case put forward by Mr Scoular of Ford Australia:

> …a new car model range can be considered in very much the same way as an aircraft seating plan. Airlines call it economy, business and first class. Everybody travels on the same plane but pays according to the feature comforts and amenities of their class. Numerically most of the seats on an aeroplane are at the back. However, whilst I am not an expert on the aviation industry, it is my understanding that it is the seats up front that make a greater contribution to the profitability of any flight. In the automotive industry it is a similar analogy regarding a new model range. In the case of the Ford Falcon, for example, the range of pricing in that vehicle across the various derivatives, excluding the high performance derivatives, is in the order of approximately $38,000 through to $54,000 or $55,000. What may have started life as a tax on first class travellers in effect has over time spread to business class and is now down to even what we perhaps could call premium economy…
>
> I think it is fair to say, as a rule of thumb, that the contribution to the profitability of a higher series vehicle or derivative would tend to be greater than a lower series.[28]

Coalition Senators note conflicting views put forward as to whether the Luxury Car Tax is a non-tariff barrier and harmful to Australia's international reputation.

While the Federal Chamber of Automotive Industries say that the Luxury Car Tax is harmful to the local car industry:

> When this tax was originally introduced it was a thinly veiled protectionist measure for the local industry. These days it actually adversely impacts the industry, because it means the level of competition that those local brands are facing is more and more intense.[29]

In a submission to the Bracks' Review, and presented to the inquiry by the Victorian Automobile Chamber of Commerce, the European Union said that they consider the Luxury Car Tax to be a non-tariff barrier:

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26 Mr Andrew McKellar, *Proof Committee Hansard*, 22 July 2008, p. 6.

27 *Proof Committee Hansard*, 6 August 2008, p. 9.

28 Mr Russell Scoular, *Proof Committee Hansard*, 6 August 2008, p. 8.

29 Mr Andrew McKellar, *Proof Committee Hansard*, 22 July 2008, p. 6.

> From the European Union's perspective the LCT should be seen as a non-tariff barrier, as it is discriminatory in its effect by mainly impacting imported cars, particularly from Europe; and, as recognised by the Productivity Commission, provides a form of domestic assistance.[30]

Coalition Senators note the Australian Government's stated commitment to removal of non-tariff barriers in trade, and the apparent contradiction between this and the luxury car tax. We also note the Opposition's consistent position on the Luxury Car Tax as first espoused in 1990.

Coalition Senators are concerned that the proposed eight percent increase in the Luxury Car Tax will have a negative impact on the viability of Australia's domestic automotive industry, and express our surprise that the Rudd Labor Government would propose such a tax increase which will be harmful to Australia's domestic car industry.

We also note the apparent incompatibility between these negative effects of the proposed tax increase, and Prime Minister Rudd's statements that he wants to ensure Australia is still a country which 'makes things'.[31]

A tax on innovation

Considerable evidence was given to the Inquiry how the current 25 percent luxury car tax was already a tax on innovation, and how increasing this by a further eight percent would discourage both new safety and environmental innovations in Australian cars:

> The luxury car tax is a 33 percent tax on safety features and low-emission technologies. If the customer seeks the fitting of airbags to a vehicle priced over the luxury car tax threshold then the customer will incur a 33 percent additional tax.[32]

Indeed, there is evidence of cars being 'despecified' for the Australian market in order to ensure they fall under the Luxury Car Tax threshold:

> Something I remember quite clearly from the old luxury car wholesale tax was there was a Mercedes Benz 180, I think the model was, back in 1993-94. The radio became an option on that vehicle to keep it under the threshold.[33]
>
> The other point we make is that the threshold is an artificial ceiling and it is causing all sorts of funny things to be done. It is in fact…leading to

30 VACC, *Submission 11,* attachment C; European Commission's submission to Bracks review.

31 First articulated on 16 March 2007 to John Laws and repeated numerous times since.

32 Mr Andrew McKellar, *Proof Committee Hansard*, 22 July 2008, p. 3.

33 Mr David Smith, Motor Trades Association of New South Wales, *Proof Committee Hansard*, 31 July 2008, p. 18.

> despecifying in order to come in under the threshold, and that has safety and environmental implications.[34]

Increasing the tax by a further eight percent would increase the potential for Australian vehicle purchasers being forced to purchase vehicles with inferior safety and environmental features than would otherwise be the case.

As the Australian Automotive Dealers Association noted:

> For example, a Mitsubishi Pajero 3.2 litre manual retails at $56,890. The addition of side and curtain airbags, $850 recommended retail, brings the total cost of the vehicle to $57,740, exclusive of luxury car tax or on-road costs. The luxury car tax on the vehicle, including side and curtain airbags, would equate to approximately $184.80.[35]

Evidence was given outlining how innovative safety and environmental features always appeared first at the higher end of the car market, and then work themselves down the chain over following years. For example, according to Mr Hofmann from Audi:

> The way it works is premium companies or leading technology brands have the innovation, they implement it but sooner or later it will be distributed and put into every car…Remember, twenty years ago an airbag was an exclusive feature in so-called luxury cars, now they are everywhere and Audi has eight airbags. If we penalise these technologies now this will lead to a slow down of their distribution.[36]

Running a specious argument against this claim, Labor Senators falsely sought to assert that for this argument to hold true, car manufacturers would be putting unsafe cars onto Australian roads:

> **SENATOR CAMERON**: I am sure that because of this tax Audi would not be putting any cars on the Australian roads that are unsafe. Would that be the case?[37]
>
> **SENATOR BISHOP**: Are you aware generally of cars that are produced on the international market where luxury car taxes or high rates of tax inhibit the presence of safety products in cars in this country?[38]

Coalition Senators note and fully agree with the comments in response to Senator Cameron's assertion:

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34 Mr David Purchase, Victorian Automobile Chamber of Commerce, *Proof Committee Hansard*, 6 August 2008, p .19.

35 Mr John Chapman, *Proof Committee Hansard*, 22 July 2008, p. 24.

36 *Proof Committee Hansard*, 31 July 2008, p. 4.

37 Senator Doug Cameron, *Proof Committee Hansard*, 31 July 2008, p. 8.

38 Senator Mark Bishop, *Proof Committee Hansard*, 31 July 2008, p. 19.

> …but if you had these features on board they would be ***safer*** and you would have less accidents.[39] [emphasis added].

It is not a matter of "safe" but "saf<u>er</u>"; "environmentally friendly" but "environmentally friendl<u>ier</u>." When as a country we are striving to reduce road fatalities and injuries, and drive more environmentally friendly cars, placing an increased tax on mitigation measures makes absolutely no sense.

Coalition Senators also note that Australia has a one of the oldest car fleets in the world[40], and that as stated by Mr Steve Bracks, we should be acting to encourage the purchase of newer, safer and more environmentally friendly vehicles:

> The states and territories could also consider the harmonisation and reduction of stamp duties, vehicle registration and compulsory third-party insurance…This would facilitate the purchase of new [or newer second-hand] vehicles and help reduce the average age of the in-service vehicle fleet. An added benefit would be a reduction in greenhouse gas emissions.[41]

The fact that Mr Bracks made such a recommendation about the need to reduce state taxes, but failed to address the Luxury Car Tax, highlights the extent to which the Government's pre-emption of his report by raising the Luxury Car Tax nobbled Mr Bracks's final report.

Lack of consultation

A number of submissions and witnesses, particularly those from the various motor traders and car dealers associations, raised their concerns about the Rudd Labor Government's lack of consultation over the implementation of this new tax.

As noted in the opening paragraph, the eight percent tax increase was announced not in the budget papers, nor even by Ministerial press release, but through a strategic budget 'leak' to journalist Glenn Milne two days before the budget.

The Government undertook no consultation with the car industry over this proposed tax increase before the announcement on 11th May, and have undertaken little consultation since.

While the laws formalising the Luxury Car Tax increase have not been passed into law, the Government has maintained that the commencement date for the increase is the 1st July 2008.

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39 Mr Joerg Hofmann, Audi, *Proof Committee Hansard*, 31 July 2008, p. 8.

40 As cited by Mr Hofmann of Audi, 40 percent of the car fleet are between 11 and 20 years old, *Proof Committee Hansard*, 31 July 2008, p. 3.

41 Review of Australia's Automotive Industry, *Final Report*, 22 July 2008, pp 97-8.

This has caused considerable confusion and chaos in the new car market. As the VACC noted in their submission to the Inquiry:

> New car dealers are not only disturbed by the decision to increase the tax but even more concerned by a failure to provide a well managed transition period so that both consumers and dealers were not adversely impacted by the consequences of the increase.[42]

This confusion has been heightened by the Government's lack of concern for issues surrounding the difference between the order date, and delivery date, of new vehicles.

Opposition Senators note the following evidence, which was typical of evidence given from motor vehicle dealers:

> Finally, ladies and gentlemen, a big concern for us is really the price protection of existing orders. This is another matter where we would have greatly appreciated it if the government had consulted with the industry. I read it in Andrew McKellar's statement and he is exactly right that buying an automobile is different from buying a carton of milk or a can of soup. Our cars are ordered nine months in advance. Some of our customers even order their cars 12 months in advance. You place an order at the end of last year, you enter into a contract which is a legally binding document and all of a sudden, the tax is increased, so what should we do? That person bought a car with a certain price assumption and all of a sudden …. and the dealers have to go back and say, 'Now, … it is now eight per cent more expensive and you have to give me more money.'[43]

In other words, a person could have ordered a car even before the 11th May announcement by the Treasurer of the tax increase, and if their car was not delivered before the 30th June, they would be forced to pay an extra eight percent tax.

Such is the confusion over this issue that the Victorian Automobile Chamber of Commerce commissioned their own advice from lawyers Greenwoods and Freehills regarding the Australian Tax Office's position that the tax was payable on the day of delivery, not the day of purchase. While considering that the ATO's view of the date of supply being the day of purchase for Luxury Car Tax purposes, Greenwoods and Freehills also noted:

> Based on recent court decisions, albeit in respect of similar GST concepts, we consider that it is also reasonable to conclude that the taxable supply of the luxury car could be taken to be 'made' for LCT purposes (as opposed to the timing of the LCT liability) upon entry into a contract for the sale of the car.[44]

42 Victorian Automobile Chamber of Commerce, *Submission 11*, p. 9

43 Mr Joerg Hofmann, *Proof Committee Hansard*, 31 July 2008, p. 4.

44 Greenwoods & Freehills, advice to VACC, *Submission 11*.

Coalition Senators note that if a person purchased and took delivery of a car between 11th May and 1st July (for example, if the car was on the showroom floor) they would not have to pay the increased tax; however if the car was ordered between 11th May and 1st July, but not delivered until 1st July, or later, they will, on the Australian Tax Office's advice, be required to pay this extra tax.

The confusion over the back-dating of the proposed tax increase in not just contained to purchaser and dealer but also the various state governments and vehicle financiers:

> The luxury car tax affects the price of stamp duty so the stamp duty is going to have to go up and we will have to re-issue registration papers. If you speak to the RTA, they cannot give you a straight answer as to whether the car needs to go and get a blue slip again or whether they can just re-do the registration papers. Finance contracts will have to be re-done as well as the deal contracts. Everything has to be re-done because in five years time if we are hauled up in front of someone we have to have the correct paperwork.[45]
>
> I have an understanding with the state revenue office, and people who deal with the state revenue office know it is very difficult to get a refund out of them. Once you have paid them, you have to have a very good reason. It is going to make life hard. It is increasing the complexity of the whole transaction. It is hard enough already, you are right.[46]

Coalition Senators condemn the Rudd Labor Government for their botched implementation of the proposed eight percent increase in the Luxury Car Tax and note that it is symptomatic of an ill-thought out policy put in place simply to raise revenue without any thought as to the consequences.

Recommendation

Opposition Senators recommend that, as a minimum, the package of bills be amended such that no one who ordered a new vehicle before 13th May 2008 (when the measure was officially announced) and took delivery after 30th June 2008 be forced to pay the extra eight percent Luxury Car Tax, if the tax increase is passed into law.

Loss of revenue/jobs

This back-dating has caused considerable confusion and uncertainty within the car industry, to the extent that some witnesses argued it has led to a significant downturn in sales of luxury vehicles, of up to 30 percent.

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45 Mr Allan Brink, Audi, *Proof Committee Hansard*, 31 July 2008, p. 5

46 Mr David Russell, VACC, *Proof Committee Hansard*, 6 August 2008, p. 19.

Coalition Senators note that if this downturn is reflected for the remainder of the year there is a very real possibility that the proposed eight percent tax increase, if passed into law, will actually result in a decline in Government revenue.

We also note the possibility of the tax increase having a significant impact on jobs:

> If the numbers go backwards, of course you will not have these 280 additional jobs but you also may have job cuts and people dismissed.[47]

Evidence presented in Sydney described how the proposed increase in the rate of the Luxury Car Tax did not merely result in consumers buying less expensive cars, it resulted in them deferring purchases altogether:

> The exact impact of the tax itself will probably take some time to play out, but what we are hearing through the dealers is that there is potentially some impact for this in future purchasing decisions.[48]

Given the Government's only policy rationale for the tax increase is to increase Government revenues and curb inflation, Coalition Senators question whether even this dubious outcome will be achieved. And if the revenue increase is achieved, Labor Senators concede that the impact will be not to curb inflation but exacerbate it.[49]

Historic vehicles

Evidence was given from both the Association of Motoring Clubs of Victoria and the Sporting Car Club of South Australia that as the luxury car tax also applies to second-hand vehicles imported from overseas, it is having a negative impact on the maintenance of Australia's motoring heritage by discouraging people from bringing such historic vehicles back into Australia.

Recommendation

That the Henry Review of taxation examine the possibility of exempting imported vehicles over say 30 years of age from the Luxury Car Tax.

Conclusion

Coalition Senators consider the move by the Rudd Labor Government to increase the Luxury Car Tax by eight percent from 25 percent to 33 percent to be based on naked class warfare and the politics of envy.

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47 Mr Joerg Hofmann, Audi, *Proof Committee Hansard*, 31 July 2008, p. 9.

48 Mr Peter Griffin, Toyota, *Proof Committee Hansard*, 6 August 2008, p. 4.

49 Labor Senators' majority report at 2.20: "the total CPI might have a one-off increase of 0.01 percent."

The Rudd Labor Government has put forward no sensible policy rationale for this tax increase on cars other than it being a naked grab for cash.

No comparable country to Australia has a Luxury Car Tax, and no other good has a 'luxury' tax applied to it. We also note that cars and their uses are already very heavily taxed.

On the evidence provided, it is clear that the Luxury Car Tax now applies to a significant number of cars which cannot be classed as 'luxury', particularly 'people-movers' used by large families, and four-wheel drives used again by large families and those in regional and rural Australia.

As a result, families and Australians living in rural and regional Australia will be punished by this proposed tax increase.

The proposed tax increase will be a further tax on innovation in the car industry, particularly in the areas of new safety and environmental developments, and may lead to the slow-down of their introduction into the Australian market.

It is incontrovertible that the current method of indexing the luxury car threshold is insufficient to accurately reflect real changes in prices of motor vehicles.

The Rudd Labor Government has botched the implementation of the tax by insisting it be backdated to the 1st July, with no guarantee it will pass the parliament, and failing to take account of the difference between purchase and delivery time for the vast majority of motor vehicles.

Finally, but not least, Coalition Senators note that an increase in the Luxury Car Tax at the current threshold will damage the Australian car industry and dumb it down.

The proposed eight percent increase in the Luxury Car Tax has not been supported by the evidence and will have numerous negative impacts, including its reliance on out-moded notions of class warfare and the politics of envy. It will have a negative effect on Australian families; a negative effect on those living in rural and regional Australia; a negative effect on safety and environmental innovation in the Australian car fleet; it will damage the Australian automotive manufacturing industry; and it will be inflationary.

Recommendation

Accordingly, the Coalition Senators on the Committee recommend the proposed increase in the Luxury Car Tax from 25 percent to 33 percent be opposed.

Senator Dr Alan Eggleston
Deputy Chair
LP

Senator Barnaby Joyce
LNP

Senator David Bushby
LP

Senator the Hon. Eric Abetz
LP

APPENDIX 1

Submissions Received

Submission Number	**Submitter**
1	Mr Graeme Paterson
2	Motor Trades Association of Queensland
3	GM Holden Ltd
4	Australian Automobile Association (AAA)
5	Porsche Cars Australia Pty Ltd
6	Federation of Automotive Products Manufacturers (FAPM)
7	Toyota Motor Corporation Australia
8	Federal Chamber of Automotive Industries (FCAI)
9	Ford Australia
10	ACT Corrective Services, Department of Justice & Community Safety
11	Victorian Automobile Chamber of Commerce
12	Australian Finance Conference, Australian Equipment Lessors Association & Australian Fleet Lessors Association
13	Australian Automobile Dealers Association
14	Association of Motoring Clubs Inc.
15	Mercedes-Benz Australia/Pacific Pty Ltd
16	Audi Australia Pty Ltd
17	Mr Mark Coulton MP, Federal Member for Parkes
18	Motor Trades Association of NSW (MTA NSW)

Additional Information Received

- Received on 22 July 2008, from Federal Chamber of Automotive Industries (FCAI). Presentation made to committee;
- Received on 22 July 2008, from Motor Trades Association of SA (MTA SA) and Australian Automobile Dealers Association of SA (AADA SA). Opening statement made to committee;
- Received on 31 July 2008, from Audi Australia. Presentation made to committee;
- Received on 5 August 2008, from Australian Automobile Association (AAA). Answers to Questions taken on notice at the Sydney Public Hearing on 31 July 2008;
- Received on 6 August 2008, from Mercedes-Benz Australia/Pacific. Presentation made to committee;
- Received on 6 August 2008, from Toyota Motor Corporation Australia. Presentation made to committee.

APPENDIX 2

Public Hearings and Witnesses

ADELAIDE, 22 JULY 2008

- BAULCH, Ms Chris, Director,
  Compliance and Operations, Federal Chamber of Automotive Industries
- BURT, Mr John Lloyd, President,
  Sporting Car Club SA Inc
- CHAPMAN, Mr John Clifford, Executive Director,
  Motor Trade Association of South Australia
- CHENEY, Mr Marc, Board Member,
  Motor Trade Association of South Australia
- CLARIDGE, Mr Michael, Treasurer,
  Motor Trade Association of South Australia
- McKELLAR, Mr Andrew John, Chief Executive,
  Federal Chamber of Automotive Industries
- REARDON, Mr Tim,
  Federal Chamber of Automotive Industries

SYDNEY, 31 JULY 2008

- BLUMS, Mr Aivars, Group Chief Executive,
  Motor Trades Association of Queensland
- BORG, Mr Steve, President,
  Motor Traders Association of New South Wales
- BRINCK, Mr Allan, Dealer Principal,
  Audi Retail Operations
- BURGDORF, Miss Anna, General Manager,
  Corporate Communications, Audi Australia
- DEWAR, Ms Kellie, General Manager,
  Member Services and Support, Motor Trades Association of Queensland
- GANNON, Mr Robert, Group Manager,
  Government Relations, Motor Trades Association of Queensland
- HARRIS, Mr Mike, Executive Director,
  Australian Automobile Association
- HOFMANN, Mr Joerg, Managing Director,
  Audi Australia
- SMITH, Mr David John, Senior Manager,
  Divisional Services, Motor Traders Association of New South Wales
- SOULAKELLIS, Mrs Rhonda, General Manager,
  Finance and Distribution, Audi Australia

MELBOURNE, 7 AUGUST 2008

- BYRNE, Mr John, Chairman,
  Australian Automobile Dealers Association
- GRIFFIN, Mr Peter Gerard, Corporate Manager,
  Corporate Affairs, Toyota Motor Corporation Australia
- HAUG, Ms Elly, Government Liaison Manager,
  Ford Motor Company of Australia Limited
- KATIC, Ms Vesna, Manager,
  Government Affairs and Trade Policy, Toyota Motor Corporation Australia
- McCARTHY, Mr David John, Corporate Communications Manager,
  Mercedes-Benz
- PURCHASE, Mr David, Executive Director,
  Victorian Automobile Chamber of Commerce
- RUSSELL, Mr David, Senior Manager,
  Government and Public Affairs, Victorian Automobile Chamber of Commerce
- SAVAGE, Mr Brian, Manager,
  Australian Automobile Dealers Association (Victoria) and Used Car Traders Division, Victorian Automobile Chamber of Commerce
- SCHREMPP, Mr Wolfgang D, President and CEO,
  Mercedes-Benz Australia/Pacific Pty Ltd
- SCOULAR, Mr Russell Gray, Government Affairs Manager,
  Ford Motor Company of Australia Limited
- STILWELL, Mr Christopher, Member,
  Australian Automobile Dealers Association
- Von SANDEN, Mr Horst, Managing Director,
  Mercedes-Benz Australia/Pacific Pty Ltd