SUBMISSION BY MOBIL OIL AUSTRALIA PTY LTD

TO

THE FEDERAL FUEL TAXATION INQUIRY
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CHAPTER 1
INTRODUCTION

Mobil Oil Australia Pty Ltd welcomes the opportunity to make a submission to the Federal Fuel Taxation Inquiry.

In this submission, Mobil argues that a number of fundamental principles should underpin the development of taxation measures. These principles should be applied in both a conceptual sense, and also to administrative aspects of the taxation measure.

Mobil then argues that significant scope exists to rationalise and improve the existing fuel taxation system at both Federal and State levels in Australia, in a manner that provides for a sustainable, competitive and efficient petroleum products market.

Mobil notes that a key charter of the Inquiry is to consider the impact of taxation on environmental outcomes. In this regard, Mobil puts forward its views on the implications for tax policy and the refining industry's need for certainty in order to determine future investment plans.
1.1 Summary of Recommendations

Petroleum Products Market

• That the Inquiry Committee support the uniform taxation of petroleum products that are able to be blended, to protect Government revenue, to reduce distortions in the marketplace, and to ensure consumer welfare.

• That any changes to the fuel taxation system not undermine industry and consumer investment in auto LPG.

• That State Governments give consideration to abolishing fuel subsidies for retail customers, in favour of more direct and transparent benefits not associated with fuel consumption.

• That the Inquiry Committee support the use of the direct claim model for the delivery of all State fuel subsidies to Bulk End Users.

• That the Inquiry Committee note that, in addition to the taxation system, other non-tax regulatory barriers impede the competitive market, including the Petroleum Retail Marketing Sites Act 1980 (Cth) and the Petroleum Retail Marketing Franchise Act 1980 (Cth).

• Mobil's overall position is that the FSG scheme should be phased out altogether. However, if there is a short term requirement of Government to retain a form of the FSG scheme, the following should occur:
  
  • The FSG boundaries should be re-drawn to minimise distortions between "regional" and "metropolitan" areas;

  • The FSG payment system for BEUs should reflect the delivery method for the Queensland State Fuel Subsidy system as well as for the Diesel and Alternative Fuels Grant Scheme and the Diesel Fuel Rebate Scheme, ie. by direct claim to the paying authority (in this case the ATO), by the BEU;

  • Costs incurred by industry in administering FSG payments should be reimbursed by the paying authority.

Refining Industry

• That the Government affirm its commitment to the diesel excise sulphur differential as described in the Measures for a Better Environment statement.

• That the Inquiry Committee agree that, as 95 RON petrol is widely available in the marketplace, there is no case to introduce an excise differential for this product.
Process and Administrative Issues

- That the Inquiry Committee support a move to monthly settlement of excise to align excise remittance with the monthly Business Activity Statement cycle.

- All Commonwealth fuel taxation activities should be administered by the Australian Taxation Office.
CHAPTER 2
MOBIL IN AUSTRALIA

The Organisation

Mobil Oil Australia is a subsidiary of Exxon Mobil Corporation, an industry leader in the petroleum and petrochemicals business around the world.

ExxonMobil conducts business in more than 200 countries around the world - ranging from exploration and production of oil and gas; manufacturing and marketing of fuels, lubes and chemicals; and, electric power generation.

The Australian cluster of ExxonMobil companies operates across a variety of countries, including New Zealand, Fiji, Papua New Guinea, New Caledonia, Guam, the Marianas, and Micronesia. Exxon Mobil operates its refining and marketing activities throughout the region under the Mobil brand.

Mobil Oil Australia

Mobil Oil Australia is a refiner and marketer of a broad range of petroleum products in Australia and the Pacific Islands.

Mobil operates two petroleum refineries in Australia, one in Melbourne and the other in Adelaide, as well as seven distribution terminals, twelve coastal bulk plants and about 550 company owned or leased service stations. Mobil supplies directly, or through distributors, some 1800 other retail outlets and is a major supplier to eight major airports in Australia.

Mobil also draws some supplies of LPG from the Westernport LPG terminal located near Melbourne and operated by an affiliated company, Esso Australia Resources Pty Ltd.

As one of Australia's major industrial companies, Mobil directly employs over 1600 people and owns assets valued at approximately $1.4 billion.

Mobil is Australia's leader in lubricant sales. Other Mobil interests include asphalt production and road-making. CSR/Emoleum (Australia) Limited, a 50:50 joint venture between Mobil and the CSR Readymix Roads Group, is the largest roads-surfacing group in Australia.

The South Pacific region forms an important part of Mobil's marketing area. Mobil operates in eleven island countries in the South West Pacific as well as Guam, the Marianas and Micronesia, which are supplied by ship from Melbourne, Adelaide or Singapore.

Mobil's Australian Head Office is located in Melbourne.
CHAPTER 3
AUSTRALIAN PETROLEUM PRODUCTS MARKET

The Australian downstream petroleum market - at refining, marketing, distribution and retail levels - is characterised by intense competition and low profitability.

As the Fuel Taxation Inquiry's discussion paper of 18 August 2001 states, Australia has the lowest pre-tax petrol price of all OECD countries, and also has among the lowest tax-inclusive prices in the OECD.

Mobil supports the statement in the Inquiry discussion paper that "the Australian retail petroleum market is highly competitive." This statement is supported by empirical evidence demonstrating both the low prices paid by consumers, and the low or negative profitability of industry participants.

The competitive nature of the Australian petroleum industry is further underlined by the annual Ernst and Young Downstream Oil Industry Financial Survey, conducted for the Australian Institute of Petroleum, which shows that profits within the refiner-marketer oil industry over the last five years of the survey have been less than one cent a litre:

![Underlying Net Profit per Litre](chart.png)

While the market is highly competitive and is delivering very low prices to consumers, there are a number of distortions created by factors external to market participants, which impede an efficient allocation of resources, and which provide for unsustainably low levels of profitability.
These distortionary factors relate both to aspects of the taxation system, and to regulations that prevent all participants competing equally in the marketplace. These regulatory impediments exist at both State and Federal level.

While Mobil acknowledges that non-tax regulatory measures fall outside the scope of the Inquiry, these measures play a crucial role in preventing the industry achieving a fully efficient allocation of resources.

In particular, the *Petroleum Retail Marketing Sites Act 1980 (Cth)* and the *Petroleum Retail Marketing Franchise Act 1980 (Cth)* impose significant distortions on the retail market, by preventing all participants competing on an equal basis.

The Sites and Franchise Acts selectively target the refiner/marketer oil companies and prevent Mobil from fully optimising its operations and competing on level terms with independent fuel retailers.

Mobil therefore believes the Inquiry Committee should be cognisant of these and other non-tax regulatory barriers when considering its position in regard to the impact of fuel taxation on the efficient allocation of resources.

*Recommendation: that the Inquiry Committee note that, in addition to the taxation system, other non-tax regulatory barriers impede the competitive market, including the Petroleum Retail Marketing Sites Act 1980 (Cth) and the Petroleum Retail Marketing Franchise Act 1980 (Cth).*
CHAPTER 4
THE FUEL TAXATION SYSTEM: KEY PRINCIPLES

Mobil's position is that taxation needed to satisfy Government revenue needs should be carried out in a manner that creates the minimum distortion of all markets, including the energy market, maintains a prosperous economy, and recognises impacts on international competitiveness.

Mobil's view is that the type of taxes that create the least market distortion are generally applicable personal income taxes and broad-based consumption taxes.

While Mobil believes that petroleum products should attract no additional direct taxation over other goods and services in the economy, if Governments do wish to impose specific additional taxes on fuel products, then the following principles should apply:

**Principle 1: The tax system must provide for equity, simplicity and certainty**

These fundamental principles must apply not only to the conceptual basis of the tax measure, but also to the administration of the tax measure. As a general rule, the more open and simple the tax measure, the less opportunity for evasion and other illegal activity.

It is also important that there be consistency of policy in regard to the taxation system, to ensure that investments are not undermined. The Fuel Taxation Inquiry Committee must be conscious of investment decisions made in the context of existing tax policy, and of the implications of changes in tax policy for future investment.

**Principle 2: Tax measures to encourage investment to help achieve Government policy outcomes should not discriminate between industry participants**

Where government chooses to utililse the tax system to create a favourable investment climate to help achieve policy outcomes for environmental or other reasons, it must do so in a manner that does not discriminate or benefit some industry participants over others.

For example, Mobil believes that incentives to encourage the early introduction of low sulphur diesel, as previously announced by the Commonwealth Government, should be provided in a manner such that all industry participants are placed on an equal footing.
**Principle 3: Industry should not have to bear the costs or responsibility of delivering Government policy measures to consumers**

It is the role of Government to determine whether to provide specific benefits or assistance to certain groups in the community, for example to provide benefits to country consumers to address concerns over the relative cost of petroleum products compared to city areas. However, Mobil believes:

1. industry should not be used as the vehicle to deliver these benefits, and  
2. industry should not be expected to determine eligibility of consumers for these benefits, and  
3. such benefits should not distort the petroleum products market

Notwithstanding the above, if Government legislation requires that suppliers are to be the vehicle for the delivery of taxation related benefits, then suppliers should be reimbursed for administration costs, and should bear no liability in the administration of any benefit program.

Further, Mobil believes it is essential that the proposed Energy Grants (Credits) Scheme, incorporating the current benefits paid under the Diesel and Alternative Fuels Grants Scheme, and the Diesel Fuel Rebate Scheme, be designed to provide for claims by eligible users direct to Government.

**Principle 4: The taxation system must be accompanied by properly resourced and effective compliance activities**

The integrity of the tax system is dependent on the ability of Governments to ensure compliance with all aspects of the system.

Federal and State Governments must devote adequate resources to detect and prevent tax evasion activities, such as illegal blending of petroleum products.

**Principle 5: Taxes designed to achieve environmental objectives may be appropriate if based on sound science and cost-benefit analysis**

Mobil accepts that Governments may wish to use the tax system to effect certain outcomes to meet new policy objectives.

While tax incentives/subsidies can provide an impetus for the introduction of advanced fuels, they can also distort the market and lead to less than optimum fuel/vehicle system performance when used to promote fuels inconsistent with the current vehicle fleet.
CHAPTER 5
EFFECTIVE TAX ADMINISTRATION

Mobil believes significant opportunity exists to modernise the excise system, to increase efficiency for industry, to minimise Government exposure to revenue loss, and to provide a simpler and more accountable framework for the delivery of grants and benefits to fuel users identified by the Government as requiring such assistance.

5.1 Excise Uniformity to Prevent Illegal Blending

Mobil believes that the Commonwealth Government suffers considerable exposure to revenue loss through differential excise rates applying to petroleum products such as automotive gasoline, diesel, heating oil and solvents.

In Mobil's view there are significantly more efficient and transparent means to deliver public policy outcomes sought by Government, which are currently delivered through differential excise rates on products that can be blended.

These differential rates, delivered via excise remission or concessional rates, have been developed for users of petroleum products intended for non-transport purposes. These differential rates have created significant opportunity for unscrupulous operators to engage in illegal blending of low or no excise product with products attracting the full transport excise rate.

The consequences of this illegal blending - or fuel substitution - are felt across three main groups:

- Government suffers substantial revenue loss, as full excise has been paid on only a proportion of every litre of petroleum product sold by those engaging in illegal blending;

- Law-abiding suppliers suffer reduced margins by having to compete with those able to sell product at an artificially low price as a result of the reduced taxation component in illegally blended fuels. This has a major "ripple effect" on the metropolitan retail industry in particular, as fuel volumes are extremely sensitive to price changes, and reputable operators are forced to match the unfair competitive advantage gain by those selling illegally blended product;

- Consumers who unknowingly purchase illegally blended fuel can suffer from poor product quality, reduced energy value and fuel economy, and may potentially suffer serious engine malfunction.

Mobil believes a clear case exists to reform the excise system to remove the opportunity for illegal blending to occur. This would be achieved by replacing the current excise differentials on all relevant products with a uniform rate of excise, set at the unleaded petrol and diesel rate.
Under this proposal, Government would provide any appropriate benefits or concessions through a rebate system on excise paid. For example, a rebate mechanism to provide a benefit for users of heating oil for domestic consumption would replace the existing concessionary excise rate of 7.557 cpl.

Similarly, purchasers of solvents for use in paint manufacturing would have access to a rebate system on excise paid, which in most cases would result in manufacturers receiving a tax rebate from the ATO prior to the due date for payment to the solvent supplier.

An excise rebate system would reduce the need for resources to be devoted to compliance activities, which are focussed on breaches "after the fact", by requiring rebate applicants to establish their bona fides prior to receiving the concession.

Mobil believes the excise uniformity approach would provide substantial benefits to Government, to honest industry operators and to consumers. Mobil strongly recommends the Inquiry Committee give close and serious consideration to the excise uniformity model.

**Recommendation: that the Inquiry Committee support the uniform taxation of petroleum products that are able to be blended, to protect Government revenue, to reduce distortions in the marketplace, and to ensure consumer welfare.**

5.2 Monthly Settlement of Excise

Currently, oil companies remit excise to the Australian Taxation Office on a weekly basis, although excise liability is incurred daily, under the provisions of the *Excise Act 1901 (Cth).*

The requirement to process excise obligations and to remit the required amount on a weekly basis, creates considerable unnecessary administrative costs.

Mobil recommends that excise payments be remitted on a monthly basis, to reduce cash flow and administration costs for business, and to place excise remittance on a similar cycle to monthly submission of Business Activity Statements relating to the Goods and Services Tax.

In addition, monthly settlement of excise would allow the ATO to more closely track excise remittance with sales volumes, and further to match this data with that provided in the monthly Business Activity Statement. This would assist the ATO in its compliance and auditing processes in regard to excise collection.

**Recommendation: that the Inquiry Committee support a move to monthly settlement of excise to align excise remittance with the monthly Business Activity Statement cycle.**
5.3 State Fuel Subsidies

Mobil believes that State fuel subsidies are an inefficient and non-transparent means of State Governments delivering policy outcomes to retail consumers. Mobil recommends the abolition of these subsidy arrangements and, if State Governments believe the intended policy outcome of subsidies should be retained, then an alternative, more transparent form of delivery should be adopted.

State fuel subsidies have the capacity to impose considerable distortions on the petroleum products market, particularly in State border areas.

Many of the current subsidy arrangements also impose administrative costs on the industry, and their non-transparent nature frequently leads to unfounded and incorrect claims that suppliers retain the subsidies rather than passing the value of the subsidy through the supply chain.

5.3.1 Retail Market

While there have been improvements in subsidy system design in some States, all jurisdictions, apart from the ACT, continue to provide subsidies on petrol and/or diesel purchased at retail sites by consumers.

The Queensland subsidy is paid in advance to retailers, who calculate their forward entitlement by referring to historical sales volume patterns. In all other States, the subsidy is paid to the wholesale supplier, who is then obliged to pass on the value of the subsidy to the retailer, who in turn is expected to pass the value of the subsidy through to the retail customer.

Mobil has concerns over the administrative costs and lack of transparency associated with both wholesale and retail-based versions of the schemes.

Mobil believes that the optimal approach would be to abolish these subsidies, and for State Governments, if they choose, to provide a benefit equivalent to the subsidy via alternative means. An example would be a reduction on annual motor vehicle registration charges. Such an approach could apply generally to all retail fuel users or selectively, depending on each jurisdiction’s policy intentions.

Recommendation: that State Governments give consideration to abolishing fuel subsidies for retail customers, in favour of more direct and transparent benefits not associated with fuel consumption.

5.3.2 Bulk End Users

Following the introduction of the New Tax System, there have been some improvements in the design of certain State fuel subsidy schemes relating to Bulk End Users (BEUs).
Bulk End Users are those users who purchase product directly from an oil company or distributor, rather than obtaining fuel from a retail site. Under the subsidy model in operation in Queensland since 1 July 2000, BEUs submit claims in arrears to the Queensland Office of State Revenue. Similar arrangements for BEUs now operate in Western Australia, Tasmania and the Northern Territory.

The move to direct payment of subsidies, based on either fuel purchased or actually used, has reduced the opportunity for abuse of the subsidy system, and has provided these State revenue agencies with a more accountable and efficient framework within which to administer their fuel subsidy schemes.

The maximum benefit arising from the direct claim model for BEUs would be achieved by aligning all State subsidy schemes to include the direct rebate model, and also by aligning the actual amount rebated.

This would reduce distortions and provide for administrative consistency for users, and potentially may allow States to share resources for processing subsidy claims.

*Recommendation: that the Inquiry Committee support the use of the direct claim model for the delivery of all State fuel subsidies to Bulk End Users*

### 5.4 Fuel Sales Grants Scheme

The Fuel Sales Grant (FSG) Scheme was introduced by the Commonwealth Government in July 2000, to offset the effect of the Goods and Services Tax on retail fuel prices in defined non-metropolitan areas.

As noted earlier, Mobil believes that industry should not be required to deliver Government policy, and that such policy outcomes should not distort the market. Mobil is concerned that the FSG scheme as it is currently structured meets neither of these criteria.

#### 5.4.1 Retail Market

The primary concern with the FSG scheme lies in the identification and placement of border areas defining "metropolitan", "regional" and "remote" locations.

The location of the borders between many "metropolitan" areas, which attract no FSG, and "regional" areas, which attract a 1 cpl FSG, has given rise to significant anomalies and marketplace distortions.

In many cases, the boundaries have been drawn such that some retail sites, which for the purposes of the FSG scheme are located in a "regional" area, are in fact actually part of the metropolitan catchment area.
This has resulted in retail sites located in metropolitan areas having to compete with sites in many outer-urban locations that have a market advantage of 1 cpl. A market advantage of this order is significant in terms of the very low or negative margins experienced at many retail sites.

Under these circumstances, retailers are forced either to meet competition by reducing margins to match the additional 1 cpl advantage of the neighbouring "regional" site, or not reduce margins and risk substantial reductions in sales volumes which may undermine site viability.

Mobil is also concerned that the delivery method of the FSG, which is paid directly to retailers, fails the criteria that the industry should not have to participate in the delivery of Government policy outcomes.

The industry has incurred significant costs in developing systems to handle the introduction of the FSG scheme, as well as in the ongoing administration of the scheme. Mobil believes these costs and obligations should properly be the responsibility of the Commonwealth Government, rather than industry.

**5.4.2 Bulk End Users**

Bulk End Users of both petrol and diesel in rural and remote areas are entitled to receive the benefit of the FSG. Unlike the BEU fuel subsidy model existing in Queensland and several other States, the FSG is delivered to BEUs through a reduction in the price charged by the supplying oil company or distributor. This requires complex and resource-intensive administration on the part of the supplier.

While the provision of this benefit is a matter for Government, Mobil notes that many BEUs eligible for the FSG benefit are also eligible for excise rebates under the Diesel Fuel Rebate Scheme, for off-road diesel usage, and under the Diesel and Alternative Fuels Grants Scheme, for on-road usage. In addition, BEUs are also likely to be eligible for full input tax credits on fuel purchased.

In addition, this situation creates a compliance difficulty for the Australian Taxation Office, as it is possible that FSG-subsidised fuel sold to some BEUs may be re-transported to metropolitan locations and sold into the retail marketplace, thus further depressing retail margins and distorting the marketplace.

**Recommendation:** Mobil's overall position is that the FSG scheme should be phased out altogether. However, if there is a short term requirement of Government to retain a form of the FSG scheme, the following should occur:

- The FSG boundaries should be re-drawn to minimise distortions between "regional" and "metropolitan" areas;
• *The FSG payment system for BEUs should reflect the delivery method for the Queensland State Fuel Subsidy system as well as for the Diesel and Alternative Fuels Grant Scheme and the Diesel Fuel Rebate Scheme, ie. by direct claim to the paying authority (in this case the ATO), by the BEU;*

• *Costs incurred by industry in administering FSG payments should be reimbursed by the paying authority.*

### 5.5 Excise and Customs Duty under One Authority

At present, there are two separate Commonwealth Government authorities with responsibility for administering excise-type taxation on petroleum products. The Australian Taxation Office has responsibility for the administration of excise for locally manufactured petroleum products, while the Australian Customs Service has responsibility for customs duty for imported products.

Mobil believes that, in line with the generally free movement of goods and services, and the capacity for significant imports of petroleum products into Australia, that a strong case exists to bring petroleum products taxation under the jurisdiction of a single agency.

Such an approach would reduce opportunity for duplication and confusion. An appropriately resourced central agency would also be in a better position to undertake compliance activities across both domestically manufactured and imported product.

As the primary Government agency responsible for revenue collection, Mobil believes it would be appropriate for the Australian Taxation Office to take responsibility for all excise and customs collections and related activities.

*Recommendation: all Commonwealth fuel taxation activities should be administered by the Australian Taxation Office.*
CHAPTER 6
SPECIFIC POLICY ISSUES

Mobil acknowledges that the Commonwealth Government is seeking to utilise the fuel taxation system as a means of helping to achieve a range of environmental policy outcomes.

In this regard, Mobil notes the Government's commitment to introducing new standards for petrol and diesel progressively through to 2006. Very substantial investment will be required in order to enable oil refiners to supply the market with these new fuels, in an environment of historically low profitability.

The development of a favourable investment environment for the industry should be based on the principle that all refiners and suppliers are to be treated equally, and that no market participants obtain a windfall gain from any Government initiative.

6.1 Diesel Excise Sulphur Differential

Mobil notes the Federal Government's Measures for a Better Environment (MBE) statement of May 1999 referred to the introduction of excise differentials to encourage the early supply of low sulphur diesel. The MBE statement proposed an effective excise differential advantage for diesel with a sulphur content of 50 parts per million or less of 1 cpl from 1 January 2003, and 2 cpl from 1 January 2004.

Mobil believes a short term excise differential measure of this nature is appropriate to provide the basis for a transition to the supply of 50 ppm sulphur diesel to the market, in the lead-up to 50 ppm sulphur diesel becoming the mandated standard.

Production costs for 50 ppm diesel are significantly higher than for existing diesel product. In the absence of an excise differential to allow 50 ppm sulphur to compete on price with existing sulphur content diesel, there would be no incentive for refiners to supply this product ahead of its mandated introduction.

Mobil is currently giving consideration to a forward investment program for its refinery assets, based on the Federal Government's policy framework for the introduction of cleaner fuels. As with all Mobil projects, any investment project in regard to the production of 50 ppm sulphur diesel will be subject to significant technical, economic, environmental and safety evaluation during its development.

Mobil's investment considerations for clean fuels are proceeding on the basis that the Government's fuel quality standards framework, including the announced taxation regime for low sulphur diesel to encourage the early introduction of this fuel, will be in place as announced in the MBE statement.
Recommendation: that the Government affirm its commitment to the diesel excise sulphur differential as described in the Measures for a Better Environment statement.

6.2 Excise Differentials for Other Petroleum Products

Mobil's planning for clean fuels production has taken place against a background of the 1999 MBE announcement, including the proposed taxation regime for low sulphur diesel.

Mobil does not support the extension of excise differentials to other fuel types, as has been suggested in relation to 95 RON petrol.

Unlike low sulphur diesel, 95 RON petrol is already widely available in the marketplace, and there is no need to provide a further incentive to produce this grade of product.

Recommendation: that the Inquiry Committee agree that, as 95 RON petrol is widely available in the marketplace, there is no case to introduce an excise differential for this product.

6.3 Taxation Treatment of LPG

Following the introduction of the GST, LPG now attracts the same level of direct taxation as most other goods and services in the Australian economy. Mobil believes this is the appropriate basis for the taxation of LPG.

Over the past thirty years the Australian oil and gas industry has made significant investments in the development of a world leading auto LPG supply and distribution network.

Around $1 billion is invested in seaboard and regional terminals, tankers and dispensing facilities at service stations. This investment has lead to the development of one of the most comprehensive alternative automotive fuel networks in the world. There are currently some 680,000 private and business LPG fuel vehicles, representing a further $1 billion investment by their owners.

It is important that any changes to the taxation system not undermine these very significant investments, made in good faith in the context of Government policy commitments to LPG utilisation.

Recommendation: that any changes to the fuel taxation system not undermine industry and consumer investment in auto LPG.