

# HISTORY OF FUEL TAXATION IN AUSTRALIA

---

## 1. Introduction

The current structure of Australia's fuel taxation system has evolved as a result of the policy objectives of successive governments since Federation. This paper examines the history of fuel taxation in Australia, and sets out when and why changes have been made to the fuel taxation system, including an explanation of the rationale for:

- the introduction or removal of excises on various petroleum products;
- any major increases and decreases in excise rates;
- the various rebates, remissions and refunds<sup>1</sup> of tax for certain fuel usage and for certain users, along with associated subsidies and grants<sup>2</sup>; and
- any major changes to the administration of excise collection.

This paper should be read in conjunction with the Fuel Taxation Inquiry Issues Paper, which provides an overview of the current structure of fuel taxation and describes the related rebates, subsidies and grants.

## 2. Development of Australia's fuel tax system

Tax on fuel in Australia was first introduced in the early 1900s as customs and excise duties<sup>3</sup> on transport fuels, such as petrol and diesel, to fund the development and maintenance of Australia's road network.<sup>4</sup> The link between fuel taxes and road funding was reinforced by the provision of exemptions

---

<sup>1</sup> Within the excise system a remission refers to a circumstance where excise duty that is payable is foregone or waived. A refund and rebate are similar mechanisms whereby duty that has been paid is returned under certain circumstances. However, a refund is normally paid to the entity that has the legal obligation to remit the excise, while a rebate within the excise system is usually paid to a different party.

<sup>2</sup> Subsidies and grants include government measures aimed at reducing the cost of fuel to consumers or aimed at influencing fuel use.

<sup>3</sup> An excise is a tax on an inland step in the production or distribution of goods, which has historically been imposed on the manufacture of goods in Australia, while customs duty is levied on the importation of goods.

<sup>4</sup> Customs duty was first imposed at Federation on imported gasoline and other oils used generally as industrial solvents. It was not until cars became more common in the 1920s that the revenue from this duty was effectively a tax on petroleum products used as fuel.

(and later rebates) of fuel tax for off-road users of diesel from the late 1950s, and by concessional rates of excise where fuel is used other than as a transport fuel.

In later years, however, the principal rationale for fuel taxes has been to provide a general source of government revenue. Tax concessions have remained in the fuel taxation structure for fuel used other than as a transport fuel or for a number of uses of petroleum products other than as a fuel.<sup>5</sup> These concessions take the form of lower excise rates, remissions or refunds of excise duty and can generally be seen as mechanisms for providing tax relief to legitimate users of petroleum products for uses other than as a transport fuel.

Since the early 1980s, the emphasis on fuel excise as a significant source of government revenue has grown, along with an increase in excise evasion activities. This has resulted in an incremental approach to restructuring and extending the range of fuels to which excise applies, to protect the revenue source, and an increase in compliance provisions to detect evasion.

Box 2.1 outlines key events in the history of fuel taxation in Australia. The remainder of this paper expands on the most significant events over this time.

## 2.1 The early years: initial application of fuel taxes

Fuel was first taxed in Australia in 1901 when a customs duty was applied as a revenue measure to certain imported petroleum products.<sup>6</sup> Excise duty was not imposed at this time as oil was not refined domestically in Australia until 1928.<sup>7</sup> In 1929, when domestic refineries were established and locally produced petroleum products entered the market,<sup>8</sup> the Government of the day introduced an excise on petrol<sup>9</sup> at the rate of 1 penny per gallon - 0.18 cents per litre (cpl). This excise was hypothecated to road funding.<sup>10</sup>

---

<sup>5</sup> Such as use as a solvent or as an input to manufacture, for example paint manufacturing.

<sup>6</sup> These products were kerosene, naphtha, benzine, benzoline and gasoline. Kerosene was generally used for lighting at that time, while the other products were used mainly as industrial solvents.

<sup>7</sup> This information can be found at the Australian Institute of Petroleum website, which can be accessed at <http://www.aip.com.au>.

<sup>8</sup> Australia currently has eight main refineries owned by the four major oil companies (Caltex, BP, Mobil and Shell). These major refineries have a total capacity of around 860,000 barrels per day (as at Dec 1998, AIP website). There are also a number of mini refineries located around Australia.

<sup>9</sup> Referred to as motor spirit, or as gasoline in relevant Customs and Excise legislation.

<sup>10</sup> Denis James, "Beer and Cigs Up!": A Recent History of Excise in Australia", Background Paper No. 5 of 1995-96, Department of the Parliamentary Library, p. 4. This paper is available on the Internet at <http://www.aph.gov.au/library/pubs/bp/1995-96/96bp05.htm>.

**BOX 2.1: KEY EVENTS IN THE HISTORY OF FUEL TAXATION**

Year	Event	Government Policy Objective
1901:	Customs duty imposed on imported petroleum products (generally used for heating and lighting or as industrial solvents).	Revenue
1929:	Excise on domestically produced petrol introduced.	Revenue - hypothecation to road funding
1931:	Excise introduced on coal tar and coke oven distillates.	Revenue
1940:	Rates of excise increased and an excise introduced on heavy fuel oil.	Revenue - assist financing Australia's war effort
1940:	Excise rate decrease for liquid fuel produced from indigenous shale and coal.	Diversify Australia's liquid fuel supplies
1940:	Assurance given to Australia's petrol producers for protection against imported petrol for fifteen years.	Industry assistance
1957:	Excise on diesel introduced for on-road use only. Exemption certificate scheme put in place for off-road diesel users.	Revenue - hypothecation to road funding
1957:	Excise on aviation turbine kerosene (AVTUR) introduced.	Revenue - fund aviation infrastructure
1959:	Formal hypothecation of fuel taxes abolished so that excise was now a form of general revenue.	Greater flexibility in budgetary process
1961:	Excise on domestically produced petrol was increased to the same rate as customs duty for imported petrol.	Eliminate margin between Australian and imported petrol
1965:	Petroleum Products Freight Subsidy Scheme introduced.	Reduce fuel prices in regional locations
1975:	Crude oil and LPG production excise introduced to ensure the community reaped some of the benefits of increased world oil prices.	Revenue
1979:	LPG for road vehicle use declared free of excise duty to encourage use of LPG.	Diversify Australia's liquid fuel supplies

1980:	Fuel ethanol declared free of duty and 'experimental' licensing arrangements put in place to encourage research into use of ethanol as a fuel.	Diversify Australia's liquid fuel supplies
1982:	Diesel Fuel Rebate Scheme introduced to replace off-road exemption certificate scheme. All off-road users required to buy duty paid fuel, with some eligible to claim a partial or full rebate.	Revenue and administrative change
1982 – 1988:	Surcharge of 1 cpl added (2 cpl from 1983) to establish a roads program under Australian Bicentennial Road Development Trust Fund.	Revenue – hypothecation for road funding
1983:	Six monthly indexation, in line with CPI, introduced.	Revenue – maintain real value of excise collections
1983:	Excise introduced for heating oil, fuel oil and kerosene.	Revenue
1986:	Refined petroleum products excise raised to compensate for crude oil excise revenue decrease.	Revenue
1989:	Provisions introduced to ensure that petroleum products are taxed according to stated end-use.	Revenue
1994:	Excise differential introduced for leaded petrol.	Environmental
1997:	High Court cast doubt on the constitutional validity of State business franchise fees ( <i>refer Section 2.7 – Administration changes to fuel taxation system</i> )	New administrative arrangement
1997:	Range of measures announced to address fuel substitution activities.	Revenue
1998:	<i>A New Tax System (ANTS)</i> proposal to replace the Diesel Fuel Rebate Scheme with the provision of diesel fuel credits, with partial extension of this credit to rail and road transport.	Reduced cost of business input
1999:	<i>Measures For A Better Environment</i> package announced including some measures specifically concerning fuel taxation. <sup>11</sup>	Environmental

<sup>11</sup> These include an excise differential for low sulphur diesel (to be introduced 1 January 2003), the Product Stewardship (Oil) Scheme (refer section 2.8), the Energy Grants (Credits) Scheme which is intended to replace the Diesel and Alternative Fuels Grants Scheme and the Diesel

2000:	Diesel Fuel Rebate Scheme maintained and extended to include 'like fuels' and to provide full rate of rebate to all categories - but proposed extension under <i>ANTS</i> limited to road and marine transport. Diesel and Alternative Fuels Grants Scheme introduced to reduce costs for road transport, but benefit made less available to urban areas. Intention that Energy Grants (Credits) Scheme replace both schemes on 1 July 2002.	Reduced cost of business input / environmental
2000:	Excise rates on petrol and diesel cut by 6.656 cpl with the introduction of <i>The New Tax System</i> .	Offset GST impact on fuel prices for both consumers and business
2000:	Fuel Sales Grants Scheme introduced.	Maintain regional and metropolitan fuel price relativities on GST introduction
2001:	Excise rate cut by a further 1.5 cpl and indexation of petroleum products excise rates abolished.	Alleviate impact of high petrol prices

Various increases to excise rates for these products were implemented over the next few decades for a variety of reasons. Some were specific rate increases and decreases, or excises on new petroleum products introduced with a specific purpose. Other changes were for budgetary purposes to ensure that revenue collected was in line with the funding needed to maintain the increasing network of roads in Australia.

In both 1931 and 1940 the petroleum products excise base was extended as a revenue measure. In 1931, an excise on coal tar and coke oven distillates was introduced as a measure to ensure the Government's revenue base, as these products were possible substitutes for petrol.

---

Fuel Rebate Scheme from July 2002. The full list of measures is described at the following Internet address [http://www.pm.gov.au/news/media\\_releases/1999/changes3105.htm](http://www.pm.gov.au/news/media_releases/1999/changes3105.htm).

An excise on heavy fuel oil was added in 1940, along with a general excise rate increase, specifically as part of the Government's increases to taxation 'as a means to assist in the financing of Australia's war-time requirements'.<sup>12</sup>

A specific purpose excise rate change also occurred in 1940 when a rate decrease was applied for liquid fuel produced from both indigenous shale and coal to encourage and speed up the production of liquid fuel in Australia. An assurance was also given at this time to producers of these products for protection against imported petrol for a period of fifteen years – via continued lower excise rates compared to customs duty rates on imported petrol.<sup>13</sup> This protection via the excise system for domestically produced petrol remained until 1961 when excise rates were increased to the same rate as customs duty – and have remained the same rate since that time.<sup>14</sup>

## 2.2 1957: diesel and aviation fuel excise

One of the most significant expansions of fuel excise occurred in 1957 when an excise on diesel was introduced to ensure that operators of diesel vehicles contributed to the maintenance of roads. It was at this time that the first exemption for excise was introduced, as diesel excise was only applied for on-road uses of diesel. This was because a formal policy of hypothecating excise revenue for road construction was still in place.

At the same time as announcing the excise on diesel fuel, the Government imposed a specific duty on both imported and locally produced aviation turbine kerosene (known as AVTUR). This was in response to the increase in preceding years of new jet planes as part of commercial airline fleets. These planes used AVTUR which was tax free, whilst older piston driven aircraft used aviation gasoline which was subject to fuel tax.<sup>15</sup> The Government saw that it was therefore 'equitable that commercial airlines using aviation kerosene should make a further contribution to the heavy costs of providing airport and air-route facilities'.<sup>16</sup>

---

<sup>12</sup> House of Representatives *Hansard*, 8 September 1939, p. 340.

<sup>13</sup> Senate *Hansard*, 7 April 1948, p. 580.

<sup>14</sup> House of Representatives *Hansard*, 16 August 1961, p. 87.

<sup>15</sup> Prior to March 1956, aviation gasoline was excisable at the same rate as motor spirit. However, when announcing an excise increase on motor spirit at that time, the Government maintained aviation gasoline excise at its existing rate. The nexus between AVGAS and motor spirit excise ceased to exist from that date. Dennis James, "Beer and Cigs Up!", p. 8.

<sup>16</sup> House of Representatives *Hansard*, 13 September 1957, p. 255.

Excise on aviation gasoline (AVGAS) and AVTUR<sup>17</sup> has since primarily been linked to funding for the aviation sector. The excise rates have varied over the years according to the charging mechanisms of relevant aviation bodies, as these charges also contributed to funding the aviation industry. Since 1995, excise rates for aviation fuels have been set according to funding requirements of the Civil Aviation Safety Authority and Airservices Australia for provision of aviation services such as traffic control and air safety regulation.<sup>18</sup>

### 2.3 1959: the end to formal hypothecation

In 1959 the Commonwealth Government announced the termination of the hypothecation arrangements for road funding. In the second reading speech for the *Commonwealth Aid Roads Bill 1959*, the Government stated that:

- the tax did not only fall on motorists since a large amount of fuel tax was paid by commercial transport operators who passed the cost onto consumers;
- it is an unsound practice to allocate the proceeds of any one tax for any particular expenditure – taxes should contribute to an overall tax pool to be used for any expenditure purposes deemed desirable; and
- there were significant annual fluctuations in fuel tax receipts which would lead to irregular funding for roads, hence making forward planning difficult for road authorities.<sup>19</sup>

This saw the end of any formal link between fuel taxes and road funding until 1982 when the Government introduced the *Australian Bicentennial Road Development Trust Fund Act 1982* (ABRD Act) establishing a roads programme to be funded by a surcharge of 1 cpl on the excise of petrol and diesel. The surcharge was raised to 2 cpl in 1983.<sup>20</sup> The ABRD surcharge ended in 1988 when the programme was replaced by the *Australian Land Transport Development Act 1988*. This Act, which is still in place, provides for a share of

---

<sup>17</sup> AVTUR is commonly known as 'jet fuel' and derives from kerosene. It is generally used in larger aircraft (eg. by commercial airlines). AVGAS is a form of gasoline and is currently generally used by small single engine aircraft, and is not used in larger jet aircraft.

<sup>18</sup> The Australian Competition and Consumer Commission also receives a small percentage of the revenue from aviation fuel excise because of its role in monitoring the aviation industry.

<sup>19</sup> Denis James, "Revenue Before Rhetoric: A Critique of Fuel Taxation in Australia", Current Issues Brief No. 50 of 1994-95, Department of the Parliamentary Library, p. 2. This paper is available on the Internet at <http://www.aph.gov.au/library/pubs/cib/cib94-95.htm>.

<sup>20</sup> The *Australian Land Transport (Financial Assistance) Act 1985* (ALT Act) contained provisions hypothecating a proportion of existing excise rather than imposing additional excise. The *Australian Land Transport Development Act 1988* replaced both the ABRD and ALT Acts on 1 January 1989.

excise on petrol and diesel to be paid into a trust fund (now Special Account) for expenditure under the Act.<sup>21</sup> However, provision was made for this share to be varied by the Government of the day.

Since 1991-92, successive Governments have set road funding in the budget process, discontinuing the practice of hypothecating a proportion of fuel excise to roads.

## 2.4 1970s and 1980s: the effects of changing world oil prices on the fuel taxation structure

No significant changes were made to the structure of fuel excises during the 1960s and early 1970s.<sup>22</sup> However, in the mid 1970s as world oil prices rose, the Government introduced an excise on crude oil and LPG production. The objective of this excise was to redistribute to the community some of the gains producers received from the increased oil prices,<sup>23</sup> given that the Australian community is the ultimate owner of Australia's petroleum resources.

The levying of this tax basically introduced two levels of fuel taxation: a production tax - at the point the fuel is produced or 'extracted' from the ground; and a refined product tax (ie. the existing excise on petroleum products) after the oil has been refined into an end use petroleum product.<sup>24</sup>

The revenue from crude oil and LPG excise reflected the amount of oil produced each year and world oil prices. Hence the revenue collected from refined petroleum products was more stable than that collected from the production excise.

This was evident in 1986 when world oil prices began to decline, resulting in lower excise collected from crude oil. Because of its importance as a general

---

<sup>21</sup> This Act provides for Commonwealth expenditure on a wide range of land transport projects - eg. roads, rail and public transport, although it currently only funds the National Highway, Roads of National Importance and Black Spot programmes.

<sup>22</sup> However, a fuel related subsidy scheme was introduced in 1965 - the Petroleum Products Freight Subsidy Scheme - with the intention of reducing the price of eligible petroleum products in remote locations of Australia by reducing the freight component of the purchase price of fuel.

<sup>23</sup> Richard Webb, "Crude Oil Excise and Royalties", Research Note No. 29 of 2000-01, Department of the Parliamentary Library, p. 1. This paper is available on the Internet at <http://www.aph.gov.au/library/pubs/rn/2000-01/01RN29.htm>.

<sup>24</sup> The costs of the crude oil excise had no real effect on retail petroleum product prices as the costs were designed to be absorbed by producers (ie. by reducing otherwise 'supernormal profits'). The economic incidence of the refined petroleum products excise however, is effectively passed on to consumers.

revenue source by then, the Government offset most of the loss of crude oil excise revenue by increasing the excise rates on refined petroleum products. The Government indicated it would reduce excise rates on refined products, however, if oil prices rose and crude oil excise collections increased. This occurred throughout 1986 and 1987 as the rates of excise for petroleum products fluctuated as world oil prices varied.<sup>25</sup>

This linkage was broken when, in December 1987, the Government introduced the Petroleum Resource Rent Tax (PRRT) - a profit based tax system that replaced the crude oil excise and Federal and state royalties systems for offshore oil projects.<sup>26</sup> Since this time, as a result of these new crude oil arrangements, the level of revenue from crude oil excise has been significantly lower. A more substantial reliance has therefore been placed on refined petroleum products excise as a significant source of government revenue.

Chart 2.1 shows that excise collections for refined petroleum products as a percentage of government revenue rose from an average of 4% in the early 1980s (around \$3 billion in 1985-86) to a consistent average of around 7.5% for the years since 1986 (or nearly \$12 billion in 2000-01). In comparison, revenue from the PRRT and crude oil excise are highly variable. The PRRT contributed \$419 million in 1998-99 and nearly \$2.7 billion in 2000-01, while crude oil excise contributed \$31 million in 1998-99 and around \$510 million in 2000-01.

Crude oil excise and the PRRT systems fall outside the Inquiry's terms of reference.

## **2.5 1982: the Diesel Fuel Rebate Scheme**

In 1957, an exemption certificate scheme was set up to provide an exemption of excise for all off-road users of diesel fuel. This continued after the 1959 end to formal hypothecation of petrol and diesel excises to road funding.

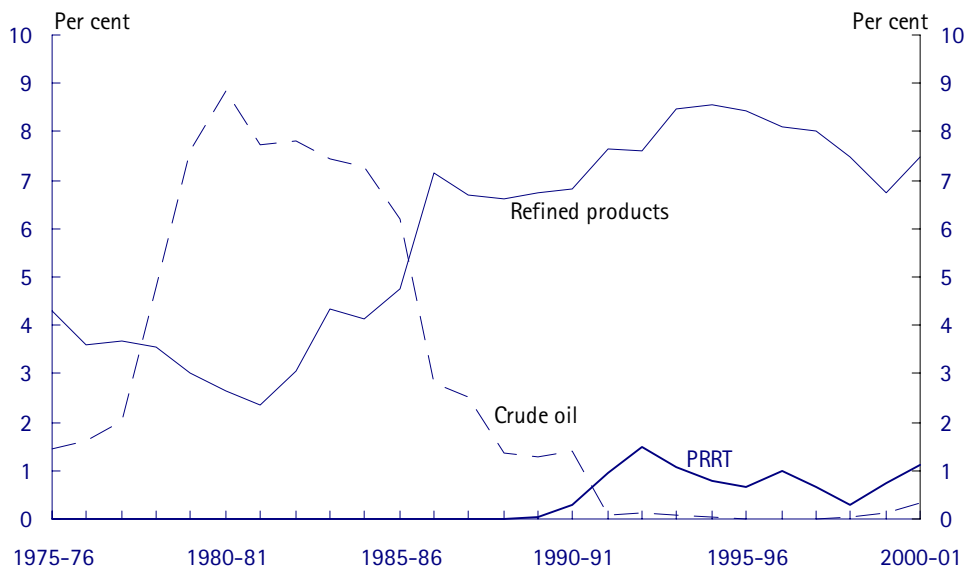
In 1982, the Government abolished the exemption certificate scheme due to alleged abuse of the system, whereby on-road users were obtaining diesel that had been purchased duty free via the exemption certificate system.

---

<sup>25</sup> Denis James, "Beer and Cigs Up!", p. 4.

<sup>26</sup> Except for the North West Shelf. On shore oil fields and the North West Shelf still operate under the crude oil excise and Federal/state royalties systems.

Chart 2.1: Percentage of Commonwealth revenue from crude oil excise, refined petroleum products excise and the PRRT, 1975-76 to 2000-01



Source: *Budget Paper No. 1 2001-02*, AusInfo, 22 May 2001, and prior year budget papers.

The Diesel Fuel Rebate Scheme (DFRS) was introduced to replace this scheme. This effectively did two things:

- all users of diesel fuel were required to purchase duty paid fuel, with eligible users then being able to claim a rebate equivalent to the excise for certain off-road usage; and
- the rebate was limited to primary producers, miners, users of diesel for heating, lighting, hot water, air-conditioning and cooking for domestic purposes and for diesel fuel used at hospitals, nursing, and old-aged persons homes. It further restricted eligibility within these categories to only certain activities, for example, mining did not include quarrying.<sup>27</sup>

In introducing changes to the scheme some years later (in 1996), the Minister for Small Business stated that the scheme provided 'rebate of duty on diesel fuel for certain activities, mainly in the mining and agricultural industries. Its primary purpose is to maintain competitiveness in these key export industries,

<sup>27</sup> Denis James, "Beers and Cigs up!", p. 6 and Richard Webb, "Fuel Price Subsidy Schemes", Research Note No. 24 of 2000-01, p. 1. This paper is available on the Internet at <http://www.aph.gov.au/library/pubs/rn/2000-01/01RN24.htm>.

in a manner consistent with the Government's broader fiscal objectives. The scheme also has a very limited number of community and social welfare objectives'.<sup>28</sup>

## 2.6 The 1980s: protecting the revenue

Two major changes occurred to the excise system in the 1983 Budget – the introduction of an excise duty on heating oil, kerosene and fuel oil and the introduction of indexation of excise rates with the CPI.

### Extension of excise to heating oil, kerosene and fuel oils

The significance of the application of an excise on heating oil, kerosene and fuel oil is that the rates applied were significantly lower than the rates for diesel and petrol – effectively creating a parallel system within the excise tariff structure to the Diesel Fuel Rebate Scheme for the provision of excise relief for certain users of fuel.

In the 1983 Budget it was announced that these products would attract the same excise rate as diesel and petrol (9.027 cpl). Effectively these additional excises were imposed to protect the revenue base from fuel substitution in response to differential excise rates.

However, after considerable opposition<sup>29</sup> in the few days after the Budget the Government lowered this excise rate by 7.155 cpl (the benefit provided by the diesel fuel rebate) to 1.872 cpl and created a concessional rate of duty for these products when used otherwise than in an internal combustion engine.<sup>30</sup> Over the years since 1983 the benefit provided via this concessional system did not remain aligned to the benefit provided by the DFRS.<sup>31</sup>

### Indexation

The 1983 Budget also saw the introduction of six monthly indexation of excise rates. The Government stated that the indexation arrangements were designed to eliminate problems associated with past discretionary increases – both for

---

<sup>28</sup> House of Representatives *Hansard*, 12 December 1996, p. 8429.

<sup>29</sup> Representations were received by the Government that the new excises would impose severe hardship upon industry and households. Senate *Hansard*, 16 November 1983.

<sup>30</sup> Denis James, "Beer and Cigs up!", p. 7.

<sup>31</sup> That is, industries using kerosene, heating oil and fuel oils at the concessional rate of excise now pay around 7.5 cpl, whereas fuel users eligible for a diesel fuel rebate effectively pay no excise.

government and industry - by maintaining the real value of excise collections and providing a greater degree of stability for consumers and industry.<sup>32</sup>

Indexation remained until March 2001 when the Government abolished indexation for petroleum products excise rates<sup>33</sup> as part of a package of decisions relating to fuel taxation.

## **2.7 The 1990s: addressing fuel substitution, implementing administrative changes and considering the environment**

### Fuel substitution measures

As the rate of excise on petrol and diesel increased over the years, there has been a corresponding growth in excise avoidance and evasion activities. Typically, these involved fuel substitution activities whereby fuel subject to a lower or free rate of excise duty is substituted for fuel commonly used in internal combustion engines on which a higher excise applies. Compliance problems such as fuel substitution generally stem from the structure of the excise system that imposes tax on the basis of intended consumption, an act that occurs after the taxing point.

In March 1989, the Government announced the first of a number of changes to the petroleum products excise system to address duty avoidance practices. This change introduced a system whereby products would be dutiable according to stated end-use.<sup>34</sup> The Customs and Excise tariffs were amended to include differential rates for products used: as a fuel in an internal combustion engine; as a fuel other than in an internal combustion engine (eg. for heating); or other than as a fuel (eg. as a solvent).

There have been a number of other measures introduced over the past decade or so to address excise avoidance practices. These include:

---

<sup>32</sup> For government the problems were claimed to be that past increases in excise rates had not been enough to maintain rates with inflation levels. For industry the past increases were said to prove disruptive and having an adverse effect on the sales patterns of relevant industries, in addition to imposing sudden and large price increases on consumers. House of Representatives *Hansard*, 9 November 1983, p. 2466.

<sup>33</sup> Indexation continues to apply for tobacco and alcohol products and for petroleum based oils and their synthetic equivalents.

<sup>34</sup> Treasurer, Press Release No. 19, 3 March 1989.

**Blended petroleum products** - in 1993 measures were announced to ensure that blended petroleum products<sup>35</sup> were subject to the highest appropriate rate of excise. The Government's intention at the time was that where a petroleum product was blended with another product, the whole product was to be subject to excise at the appropriate rate.<sup>36</sup>

**Light fuel oil** – at the time of the 1995 Budget, the characteristics of fuel oil were redefined in the existing *Excise Tariff Act 1925* in order to exclude light fuel oil from concessional treatment under the tariff. These measures were intended 'to address the tax-driven substitution of 'light' fuel oil for diesel which is taking place at some cost to economic efficiency and the environment'.<sup>37</sup>

**Topped crude oil** - the rate of excise for topped crude<sup>38</sup> was increased in 1995 from the concessional rate to the rate applying to diesel. This was also intended to remove a potential diesel fuel substitution problem that existed due to the differential excise rates.

**Marker regime and Penalty Surcharge legislation** – at the time of the 1997 Budget, changes to the excise system were announced that introduced the addition of chemical tracers to concessional fuels<sup>39</sup> - now commonly known as the 'marker' system. Several Penalty Surcharge Acts complemented the marker system to allow for the imposition of a penalty surcharge where fuel that has been paid at the concessional rate and marked with the chemical marker is subsequently used or sold for use in an internal combustion engine, or blended with an unmarked fuel.

---

<sup>35</sup> Fuel blends that contained products with no excise or a concessional rate of excise and were capable of being used as substitutes for excisable products.

<sup>36</sup> Additionally, all premises where blending was undertaken were required to be licensed as an excise manufacturer – as, under the excise legislation, blending of petroleum was now constituted as manufacture.

<sup>37</sup> Budget Speech, May 1995, p. 12.

<sup>38</sup> Topped crude is crude oil from which the light ends (the more volatile products of petroleum refining such as butane, propane and gasoline) have been removed by a simple refining process.

<sup>39</sup> Certain products, which were excisable at rates below the rate for on-road fuels, were not required to be marked. This included all concessional fuels in packages not exceeding 210 litres (ie. drum and retail stock) and where it could be proven that the addition of the marker would affect the performance of the product – eg. aviation fuels.

The 1997 measures saw a marked decrease in the clearance of substitutes such as heating oil. However, further improvements were required to be made to the system in the following years.<sup>40</sup>

### Administration changes to fuel taxation system

In August 1997, a High Court decision<sup>41</sup> cast into doubt the laws allowing collection of state business franchise fees on petroleum products (and alcohol and tobacco products). The Commonwealth therefore collected all fuel taxes immediately following the High Court decision.<sup>42</sup>

The other significant change to excise administration occurred when responsibility for excise duty – but not customs duty – was transferred to the Australian Taxation Office (ATO) from the Australian Customs Service (Customs) in 1998 as part of machinery of government changes following the 1998 federal election.<sup>43</sup>

### Environment

In 1994, an excise differential was introduced on leaded petrol and coal tar and coke oven distillates effectively as an environmental measure. This was the first such inclusion of an environmental mechanism within the excise system.

---

<sup>40</sup> These changes included a restructure of the excise tariff that removed provisions allowing heating oil to be unmarked in packages not exceeding 210 litres, and removed mostly all concessional rates for petrol and diesel.

<sup>41</sup> Relating to tobacco - *Ha and Lim v State of New South Wales and ors; Walter Hammond & Associates v State of New South Wales & ors*, High Court of Australia, 5 August 1997, Matter No. s45 of 1996.

<sup>42</sup> At the request of the States, the Commonwealth adjusted excise rates (on tobacco and petroleum products) and wholesale sales tax (on alcohol) to fund revenue replacement payments to the States for the loss of business franchise fees. Whilst revenue replacement payments were formally abolished from 1 July 2000, as part of *The New Tax System*, the States still receive the equivalent amount of revenue from the fuel revenue replacement payments as they did prior to taxation reform. This is because the Commonwealth guaranteed that in each of the transitional years following the introduction of taxation reform, the States would be no worse off than had the reforms to Commonwealth-State financial relations not been implemented.

<sup>43</sup> These changes included repositioning non-core functions of the Australian Customs Service to other agencies.

## 2.8 The new millennium: The New Tax System

Various changes relating to fuel taxation were made as part the Government's tax reform changes in July 2000. In the original *A New Tax System*<sup>44</sup> package proposed in 1998 the Commonwealth Government announced a number of reforms to diesel fuel excise and rebate arrangements, to be implemented as a single diesel fuel credit. This would partially extend the benefit provided by the Diesel Fuel Rebate Scheme (DFRS) to the transport industry but deliver it via *A New Tax System* in the form of a single tax credit. The DFRS was therefore to be abolished.

Following the announcement of the *Measures For a Better Environment* package in May 1999 (refer footnote 11), and further parliamentary amendments to the Government's original tax reform proposal, the final arrangements included the retention of the DFRS and the introduction of three new schemes – the Diesel and Alternative Fuels Grants Scheme, the Fuel Sales Grants Scheme and the Product Stewardship (Oil) Scheme.

### Changes to the Diesel Fuel Rebate System

Under the final tax reform package of *The New Tax System*, the DFRS was retained and extended to rail and marine transport. Rebate rates, which varied according to activity until 1 July 2000, were made equal for all eligible activities (and extended to a full rebate of excise duty). The rebate was also extended to cover like fuels.<sup>45</sup>

### Diesel and Alternative Fuels Grants Scheme

This scheme replaced the proposed diesel fuel credit for transport operators under *The New Tax System*. It primarily aims to reduce transport costs for business (particularly in regional and rural Australia) and also to address environmental concerns relating to emissions from diesel use within metropolitan areas.<sup>46</sup>

---

<sup>44</sup> *A New Tax System* was the proposed tax reform package put forward in August 1998. *The New Tax System* was the package of changes implemented in July 2000.

<sup>45</sup> Like fuels are fuel oils, kerosene, heating oil, and any other petroleum products that can be used in an internal combustion engine and therefore attract the same rate of rebate as diesel.

<sup>46</sup> This was addressed by limiting the grant to vehicles over 4.5 tonnes and excluding metropolitan use for certain vehicle sizes and types.

## Fuel Sales Grants Scheme

This scheme was introduced as part of *The New Tax System* to maintain regional and metropolitan price relativities on the introduction of the GST.

## Product Stewardship (Oil) Scheme

This scheme was introduced as part of the *Measures For A Better Environment* package, and became effective on 1 January 2001. Its objective is to encourage the environmentally and economically sustainable reuse of waste oils by taxing lubricants and by providing a benefit to oil recyclers for the appropriate treatment of waste oil products. This effectively means that the excise system is being used for purposes other than to generate government revenue.

## 2.9 The future: the growth of alternative fuels

As mentioned in section 2.4, an excise on the production of LPG was introduced in 1975 along with the crude oil excise.<sup>47</sup> There was also an excise imposed on LPG for vehicle propulsion between 1974 and 1979. This tax was imposed via the *Liquefied Gas (Road Vehicle Use) Tax Collection Act 1974* and varied from 2.0 cpl in 1974 to 2.125 cpl in 1979. The rationale for the introduction of this tax was to ensure those users of LPG contributed to road maintenance as did other road users. The tax was eliminated in 1979 when the then Government committed to a five year guarantee on the excise-free status of alternative fuels, including LPG and CNG, with at least a one year notification of any change to that status.<sup>48</sup>

Ethanol was also given a duty free status in 1980 and an exemption in 1994 from excise when blended with petrol. A new class of distilling licence was also introduced in 1980, known as an 'experimenters' licence that authorised the distillation of spirits from any material for the purposes of research into the production of ethanol for use as a transport fuel. These measures were intended to encourage the diversification of Australia's domestic fuel supply.<sup>49</sup>

---

<sup>47</sup> The provision for this excise was repealed by the *Excise Tariff Amendment Act 1993*.

<sup>48</sup> Industry Commission, *Petroleum Products*, Report No. 40, 5 July 1994, p. 252.

<sup>49</sup> House of Representatives *Hansard*, 28 February 1980, pp. 507-508.

### 3. Current fuel taxation structure

After studying the history of the fuel tax structure in Australia it becomes clear that the current structure has evolved from an incremental policy framework.

The current structure is summarised in Table 3.1. It shows the current rates of excise for petroleum products along with specific other fuels that have been listed in the tariff with a zero rate of excise. It also highlights where a refund, rebate or remission may apply. These remissions and refunds have been incorporated into the system over the years as the excise base has expanded - to relieve certain parties of either whole or part of the excise applying to fuel use for a range of government policy reasons.

The Fuel Taxation Inquiry will be examining this current structure (including the various state fuel rebate arrangements that have not been described in this paper) and will report on the options available to Government to:

- reduce or eliminate any adverse effects of the current system; and
- reduce the cost or improve the effectiveness of the administration of the current and proposed arrangements.

The Inquiry Committee welcomes comments from members of the public.

Table 3.1: Fuel excise rates as at 1 August 2001 (cents per litre)

Product	Burner Use rate	Other use	Other use rate	Refund or remission provision(a)	Excise due after refund / remission
Petrol and shale oil – leaded / unleaded	40.516 / 38.143	Other use	40.516 / 38.143	- Diplomatic(b) - Naptha produced from shale oil - Petroleum / shale spirit (not a gasoline) for solvent or any other use other than fuel	0.00 0.00 0.00
		Aircraft fuel	2.808		
		Other	38.143	- Manufacture of explosives - Used as a solvent - In road construction - As a mould release agent - Any other use (other than as a fuel) - Manufactured by waste oil refining process (from 31.12.1995 – 1.1.2006)	0.00 0.00 0.00 0.00 0.00 Volume x 0.38143 x 0.80
Kerosene	7.557	Drummed – other than fuel use Bulk:	0	- Used in gas turbine engine to generate electricity	7.557
		- other use containing marker	0	- Use by a business in an ICE for propulsion of a marine vessel	7.557
		- other Aircraft fuel	38.143 2.845		
Heating Oil	7.557	Other use Use other than fuel and containing marker	38.143 0	- Used in gas turbine engine to generate electricity - Foreign government use - Status of Forces agreement	7.557 0.00 0.00
		7.557		- Nickel and cobalt production - Use as chemical reactant for refining bauxite into alumina (where natural gas is not available or supply interrupted)	0.00 0.00
Fuel Oil(c)	7.557	7.557			
Condensate	7.557	Other For use as a refinery feedstock	38.143 0	- Used in gas turbine engine to generate electricity	7.557

Stabilised crude	7.557	Other For use as a refinery feedstock	38.143 0	- Used in gas turbine engine to generate electricity	7.557
Topped crude	7.557	Other For use as a refinery feedstock	38.143 0	- Used in gas turbine engine to generate electricity	7.557
Other refined products	7.557	Other use: - drummed - bulk containing marker - other	0 0 38.143	- Used in gas turbine engine to generate electricity - Use in diesel engines operating <1000 rev/min in power station not connected to electricity transmission grid and generating in excess of 5.5 megawatts of electricity	7.557 0.00
Other recycled petroleum products	0	Other use	0		
Coal tar and coke oven distillates (leaded / unleaded)	40.516 / 38.143	Other use	40.516 / 38.143	(Identical to petrol)	
Petroleum based oils and lubricants (not for fuel use)	(d)		5.299	- Recycled oil not covered under the Product Stewardship (Oil) Scheme	0.00
LPG	0		0		N/A
CNG	N/A		N/A		N/A
Ethanol(e)	0		0		N/A

(a) A number of rebate, subsidy and grant schemes also apply to these fuel products. The Fuel Sales Grants Scheme applies to petrol and diesel; the Diesel Fuel Rebate Scheme applies to diesel and 'like fuels' (which are fuel oil, kerosene, heating oil, and any other petroleum products that can be used in an internal combustion engine and therefore attract the same rate of rebate as diesel); the Diesel and Alternative Fuels Grants Scheme applies to diesel, ethanol, compressed natural gas (CNG) and LPG; and the Petroleum Products Freight Subsidy Scheme applies to petrol diesel and aviation fuels. For further details on these schemes refer to the Fuel Taxation Inquiry Issues Paper, Table 5.4 Overview of Commonwealth fuel rebates, subsidies and grants, p. 27.

(b) Diplomatic refund applies to all products listed in the tariff.

(c) Fuel oils are typically heavy fuels not suited for use in vehicle engines. The properties of fuel oil for the purpose of excise are defined in subsection 3(4) of the Excise Tariff Act 1921.

(d) The excise rate for these products only applies to use other than as a fuel (eg. as a lubricant)

(e) Other alternative fuels are currently being developed and their excise status under the current legislation is being determined.

Source: Australian Taxation Office information drawn from Excise Tariff Act 1921, The Schedule.