



**CONSULTATION ON EXPOSURE DRAFT
REGULATIONS & EXPLANATORY MEMORANDUM:
ALTERNATIVE FUELS TAXATION**

Submission by:

Australian Institute of Petroleum

12 August 2011

(1) INTRODUCTION

Thank you for the opportunity to provide our views to Treasury through this Submission on behalf of the Australian Institute of Petroleum (AIP).

About AIP:

AIP was established in 1976 as a non-profit making industry association. AIP's mission is to promote and assist in the development of a sustainable, internationally competitive petroleum products industry, operating efficiently, economically and safely, and in harmony with the environment and community standards.

AIP is pleased to present this submission on behalf of the following member companies:

BP Australia Pty Ltd
Caltex Australia Ltd
Mobil Oil Australia Pty Ltd
The Shell Company of Australia Ltd.

This submission has been developed to assist with the Treasury consultations on the exposure draft regulations giving effect to the Government's Alternative Fuels Taxation policy announced in the 2010-11 Federal Budget and in subsequent detailed Government announcements. AIP is happy for our submission to be made publicly available on the Treasury website.

Should Treasury have any additional questions or information requirements in relation to this Submission or the implementation of Alternative Fuels Taxation, please contact Mr Nathan Dickens, General Manager – Policy of AIP, on (02) 6247 3044 or ndickens@aip.com.au.

The Role of AIP Member Companies in the Transport Fuels Market:

AIP member companies play a significant role in the fuel supply chain.

- In relation to conventional petroleum fuels, AIP member companies operate all petroleum refineries in Australia and supply around 90% of the transport fuel market with bulk/wholesale petroleum fuels.
- In relation to gaseous fuels, AIP member companies are the major suppliers of bulk LPG to the domestic market, representing around 2/3 of the market.
- In relation to biofuels, AIP member companies are the largest suppliers of ethanol blended fuels and blended biodiesel to the Australian market.

AIP member companies are also:

- very significant excise and customs duty collectors for the Government – totalling around \$15 billion in 2009; and
- have total assets valued at over \$16 billion dollars, and typically invest around \$1 billion each year to keep fuel reliably supplied to the Australian market.

AIP member companies therefore have a very strong interest in any changes to fuel taxation, including alternative fuels tax. Fuel tax legislation and regulation changes have direct financial and business implications for AIP member companies, including future excise and customs obligations and the resulting investment needed in systems and controls to fully comply with these obligations.

Against this background, AIP would like to make the following comments and recommendations in relation to the exposure draft regulations for Alternative Fuels Taxation.

(2) OVERVIEW: AIP VIEWS ON THE EXPOSURE DRAFT REGULATIONS

AIP supports the Government's announced 'tax policy' for all transport fuels of neutral tax treatment consistent with energy content. The exposure draft regulations give effect to this policy and its supporting legislation, and deal with matters of direct importance to the industry. Specifically, they outline how the legislation will be applied in practice to specific fuels (eg. blended fuel products) and also continue to provide the important link between excise payment/relief and meeting relevant fuel quality standards under the *Fuel Quality Standards Act 2000*. The regulations also determine, among other things, the nature and extent of the systems changes that AIP member companies will need to make to comply with the new excise arrangements and the specific financial and working capital implications for their businesses from 1 December 2011.

In AIP's Submission of 11 November 2010 on Alternative Fuels Taxation, AIP emphasised that the draft regulations need to be released well in advance of the proposed start date and should:

- align with the legislative framework and achieve the Government's policy objectives;
- be workable from an AIP member company perspective; and
- not create unintended consequences and additional (unmanageable) compliance and administration costs for AIP member companies.

AIP considers that the exposure draft regulations largely achieve these objectives, and are generally consistent with AIP's advice and recommendations on technical matters outlined in our Submission of 11 November 2011.

In particular, AIP supports:

- **the introduction of a 'notice requirement' for supply of LPG to which LPG remission applies (section 49AAA of draft *Excise Amendment Regulations 2011*);**
 - AIP does, however, recommend a slight change to the 'content' of the notice requirement to better integrate with existing company systems – see Section (3) below.
- **the standardised LPG conversion approach and applicable rate for the calculation of duty liability (s49AAC of draft *Excise Amendment Regulations 2011*);**
 - We note that Treasury has used an LPG conversion rate for a typical Autogas mix (50% propane and 50% butane) and we consider this rate is appropriate.
 - This LPG conversion rate is proposed instead of a conversion rate representing an average between this typical Autogas mix and 100% propane (which is typically supplied to many regional areas for mixed use applications). In this context, we support the proposal in the Explanatory Memorandum for the conversion rates to be subject to 'periodic review' to ensure they continue to accurately reflect physical characteristics of gas supplied in the Australian market.
 - AIP would support a regular review every 12-18 months to ensure there are no unintended behaviour changes in the market (eg. creating a bias towards gaseous products with a certain composition).
 - We note that the periodic review requirement and its relevant details is not explicit in the regulations themselves, and we recommend this occur.
 - However, AIP recommends an amendment to s49AAC(1) to better reflect current supply operations in practice and to ensure consistency between the calculation of excise to be paid to the ATO, and the excise amount to be recovered from customers – see Section 3.
- **the taxation and fuel tax credit approach for blended fuel products.**
 - AIP member companies consider that the regulations concerning fuel tax credit entitlements for biofuel blends will operate as intended.

However, consistent with our longstanding position, AIP opposes a remissions based taxing approach for gaseous fuels based on intended use.

- The draft regulations propose ‘automatic remissions’ be available for prescribed classes of gaseous fuels (ie. no duty will be payable for LPG, LNG or CNG used in a range of non-transport uses) and propose other ‘intended use’ provisions for LPG used in non-transport applications.
- AIP does not support a ‘remissions based’ (and intended-use) taxing approach for gaseous fuels, for the reasons outlined in AIP’s previous submissions to Treasury on Alternative Fuels Taxation.
 - Primarily, it is unreasonable for a bulk supplier of gaseous fuel to be expected to know how a gas may be used once it is sold to a customer and determine whether or not to apply tax based on the intended use of the customer; we note that some gas products, like propane, can be used in a range of applications varying from automotive use to domestic heating and cooking.
 - For these reasons, AIP has strongly recommended that the existing process for liquid fuels of applying excise as fuels enter home consumption, then applying fuel tax credits as appropriate, has proved to be exceptionally robust in protecting the revenue base for Government, with an acceptable compliance and administration burden on the impacted parties; AIP still considers there is a strong case for applying the same robust and efficient excise arrangements to gaseous fuels from the start date.
- However, we acknowledge the efforts by Treasury to seek to reduce the risks noted above in this remissions approach and previously identified in AIP Submissions.
 - In particular, we support the notification regime in principle, the legislative provisions dealing with the tax treatment of gaseous fuels in ‘mixed-use’ applications and situations, and the proposed penalty regime which will apply.
 - **We do recommend, however, that the tax treatment of gaseous fuels in ‘mixed-use’ applications outlined in the legislation and supporting memorandum (ie. ‘no remission will apply for LPG supplied for a mixed use’) should also be detailed in the regulations themselves and in their supporting material. For example, through a dedicated section dealing with “Circumstances in which a remission will not apply”.**
- Despite these provisions and controls, AIP member companies will still be required to consult extensively with their legal advisors on existing and new supply contract requirements for gaseous fuels to ensure that business risks are mitigated to the greatest extent possible.
- AIP emphasises, once again, the need for ongoing strict controls over remissions, as well as a robust ATO and Customs compliance program, to ensure that potential Government revenue leakage and any industry compliance problems are minimised.

Finally, AIP notes that the proposed regulations will create compliance difficulties and administrative complexities for AIP member companies (largely as a result of the remissions based approach for gaseous fuels), but these issues appear manageable and will not inhibit the ability of AIP member companies to meet the 1 December 2011 start date for the new excise arrangements.

(3) AIP RECOMMENDATIONS: SPECIFIC AMENDMENTS TO REGULATIONS

AIP considers the following amendments could be made to the draft regulations to ensure they operate as intended and do not create unintended consequences.

DRAFT EXCISE AMENDMENT REGULATIONS 2011:

SECTION 49AAA

Currently reads:

*“Notice requirements for sales or supplies of LPG to which LPG remission applies — content
(1) For paragraph 77L (3) (b) of the Act, a notice to which subsection 77L (2) of the Act relates must include the following words:*

‘Not for transport use. Penalties apply if used or supplied for transport use’.

*Note: The notice is to be given by a person (described in subsection 77L (2) of the Act as a **supplier**) who sells or supplies LPG to another person.*

(2) The words must be included on the first page of the tax invoice provided by the supplier.”

AIP recommends an important change to wording requirement in (1), namely:

“ ‘Not for transport use. Penalties apply if used for transport purposes’ “.

Comment: In AIP member company SAP systems, the text is limited by the number of characters in a text field, and succinct wording for new text is less likely to create integration problems with existing systems. More broadly, we understand the intention of Section 49AAA is for penalties to apply to those entities who, under the remission arrangements, supply tax free LPG to customers for transport purposes. We therefore suggest the tighter wording above which will better meet system requirements and is more consistent with the nature of intended ‘use’ provisions and penalties.

SECTION 49AAC (1)

Currently reads:

“Conversion of measurements of LPG and compressed natural gas

(1) For the purposes of the Excise Acts, and for the purpose of determining a person’s liability to pay duty, if a quantity of LPG:

(a) is entered for home consumption as a quantity measured in kilograms; and

(b) is not measured using volumetric measurement equipment in the course of being entered; the quantity of LPG may be converted to litres at the rate of 1 kilogram of LPG to 1.885 litres of LPG.”

AIP recommends the removal of (1b) in total (as it is too generalised and unnecessary in practice to deliver on the intent of the provision) or it be amended to the following:
“(b) volumetric measurement equipment is not used to determine the quantity being entered”.

Comment: The custody transfer measurement and billing processes of AIP member companies are based entirely on the ‘mass’ of LPG loaded onto a truck at a truck loading facility. The calculation of this ‘mass’ is performed via the calibrated weighbridge at the facility. While volumetric meters may be present in ‘the process of loading LPG’, these meters are typically not calibrated (with no master meter on site to allow calibration to occur) and they play no role for AIP member companies in the accurate determination of how much LPG has been sold to the customer. As a result, any volumetric meters cannot and should not be relied upon for determining excise liability. AIP considers that this recommendation will also ensure there is consistency between the calculation of the amount of excise to be paid to the ATO, and the excise amount that is recovered from customers.

DRAFT CUSTOMS AMENDMENT REGULATIONS 2011:

SECTION 126E

AIP recommends the same amendment to Section 126E as proposed for Section 49AAC(1) above.

(4) AIP RESPONSES TO THE TREASURY FOCUS QUESTIONS FOR INDUSTRY

Treasury has indentified nine questions for Industry on the Taxation of Alternative Fuels Exposure Draft Regulations. These questions, together with AIP responses, are outlined below.

1. Does industry consider that the automatic remission will operate effectively?

NO. AIP member companies consider that automatic remissions on the basis of intended use have been proven to be an ineffective implementation approach for taxing fuels (see [Section 2](#) above). We note however, that Treasury has introduced legislative provisions (for ‘mixed use situations’) as well as new notification and penalty regimes to seek to manage the risks inherent in this approach and help to ensure they operate as the Government intends. An automatic remissions approach has also necessitated a higher level of compliance complexity and administrative burden for AIP member companies.

AIP Recommendation: Apply excise on all fuels entering home consumption from licensed premises, then apply fuel tax credits as appropriate (ie. for non-transport uses).

2. Does industry anticipate any issues in identifying when an automatic remission will apply?

YES. As noted in [Section 2](#) above, it unreasonable for a bulk supplier of gaseous fuel to be expected to know how a gas may be used once it is sold to a customer and determine whether or not to apply tax based on the intended use of the customer; we note that some gas products, like propane, can be used in a range of applications varying from automotive use to domestic heating.

3. How does industry anticipate gaining assurance that liquefied petroleum gas (LPG) and liquefied natural gas (LNG) that is delivered is going be used for non-transport use and therefore subject to automatic remission?

As noted in [Section 2](#), AIP member companies will be consulting extensively with their legal advisors on existing and new supply contract requirements for gaseous fuels to ensure both business risks are mitigated to the greatest extent possible and fuel is not diverted from remission into transport use. AIP notes that the existing supply contracts of AIP member companies are fundamentally ‘supply’ agreements and contain no specific provisions for ‘intended use’.

4. Will the proposed regulations concerning fuel tax credit entitlements for biofuel blends operate as intended?

YES. AIP member companies consider that the regulations concerning fuel tax credit entitlements for biofuel blends will operate as intended.

5. Does industry consider that the proposed content of notices for duty free LPG is appropriate?

YES, AIP member companies believe the proposed content of notices for duty free LPG would be appropriate, subject to a minor amendment to better integrate with existing systems, see [Section 3](#).

6. Will the proposed requirements result in any compliance difficulties for existing invoicing systems?

NO, AIP member companies consider that the proposed requirements will not result in any significant compliance difficulties for existing invoicing systems subject to the AIP proposed amendment noted in [Section 3](#) being made.

7. Will the proposed length of the text for notices cause any difficulties for existing invoicing systems?

NO, subject to the AIP proposed amendment to the text (noted in Section 3) being made.

8. Is the conversion rate for LPG from kilograms to litres appropriate?

YES. AIP supports the standardised approach for converting LPG from kilograms to litres (as being the most administratively simple and practical approach) and considers the proposed conversion rate for a typical LPG Autogas mix (of 1kg of LPG equals 1.885 litres) to be appropriate. AIP supports the proposal in the Explanatory Memorandum for the conversion rates to be subject to 'periodic review' to ensure they continue to accurately reflect physical characteristics of gas supplied in the Australian market. In this context, we support regular review every 12-18 months and for this review requirement to be made explicit in the regulations.

9. Is the conversion rate for Compressed Natural Gas (CNG) from megajoules to kilograms appropriate?

NO COMMENT. AIP makes no specific comments in relation to CNG conversion rate identified in the regulations, as it is not applicable to AIP member companies.