Australia's Fuel Tax Credits and the debate over fossil fuel subsidies

The Fuel Tax Credits Scheme costs the Federal Budget nearly $10 billion per year and largely benefits iron ore and coal miners. Researchers at the OECD, IEA and IISD describe it as a fossil fuel subsidy. The OECD has called for its elimination. Australian Government and mining industry representatives dispute the use of the term subsidy, but not its cost to government or benefit to miners.

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INTRODUCTION

Australia's fossil fuel subsidies, particularly the Fuel Tax Credits Scheme (FTCS), are controversial. They have major fiscal and climate impacts and, back at the 2009 G20 forum, Australia committed to phase them out.

In 2010, Australian public servants identified 17 fossil fuel subsidies, worth $8 billion per year, that were relevant to the G20 pledge, including the FTCS. The public servants' estimates of Australia's fossil fuel subsidies were only made public later, following a Freedom of Information request. The Rudd Labor Government overrode the public servants' work and instead informed the G20 that no such subsidies existed.[1] To this day, Australian Governments acknowledge the cost of the FTCS and other budget items, but simply avoid the term 'subsidy'.

[1] Tingle (2011) *Swan under pressure over fossil fuels*, https://www.afr.com/policy/energy-and-climate/swan-under-pressure-over-fossil-fuels-20110228-il2j3

Australia has not only failed to deliver its G20 promise to end 2009 fossil fuel subsidies, but it continues to introduce new ones. The latest Federal Budget commits $1.5 billion to support new gas exports through Darwin. Again, the Australian Government acknowledges the cost but refuses the term subsidy, even though documents, again obtained under Freedom of Information laws, describe the government's funding as a 'key enabler' of new gas development.[2]

This briefing note explains the basics of fossil fuel subsidies, the FTCS and summarises the views of international and Australian researchers on the scheme and its categorisation as a subsidy.

WHAT IS A FOSSIL FUEL SUBSIDY?

According to the World Trade Organisation (WTO), of which Australia is a member, a subsidy exists when, among other things:

(i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);

(ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits);

Using the WTO definition of a subsidy, The Australia Institute estimates that Australian Governments, state and federal, provided $14.5 billion in fossil fuel subsidies in 2023-24, the most expensive of which was the $9.6 billion Fuel Tax Credits Scheme.[3]

In addition to The Australia Institute, international organisations that specifically include Australia's FTCS in their calculations of fossil fuel subsidies include the OECD, the International Energy Agency (IEA), the International Institute for Sustainable Development (IISD), Overseas Development International (ODI) and Oil Change International. Their work is described in more detail below.

[2] Davies (2023) *How is Australia trying to sell a major gas expansion? By badging it 'sustainable'*, https://www.theguardian.com/australia-news/2023/may/19/how-is-australia-trying-to-sell-a-major-gas-expansion-by-badging-it-sustainable

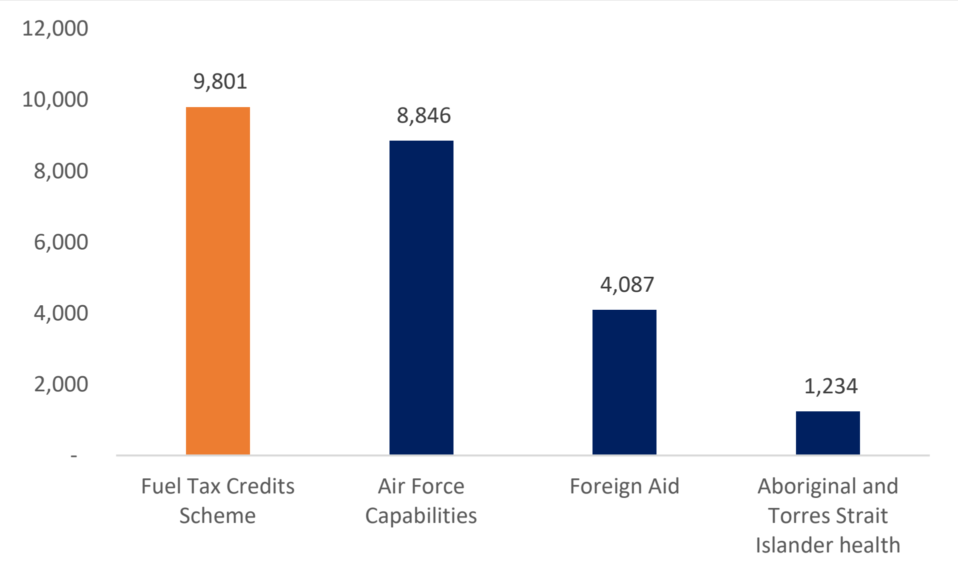
[3] Campbell et al (2023) *Fossil fuel subsidies in Australia 2023*, https://australiainstitute.org.au/report/fossil-fuel-subsidies-in-australia-2023/

WHAT IS THE FUEL TAX CREDITS SCHEME?

Australia charges a fuel tax (also called fuel excise) of around $0.47 per litre for diesel, petrol and most commonly used fuels.[4] This tax will raise around $20 billion in 2023-24, a significant source of revenue for the Australian Government.[5]

The Fuel Tax Credits Scheme (FTCS) refunds fuel tax paid by certain fuel users – mainly businesses using diesel for machinery, vehicles not on public roads and heavy vehicles that do use public roads.[6] The FTCS is budgeted to reduce Australian Government tax receipts by $9.6 billion in 2023-24, making it the 18th largest cost item in the Federal Budget, more than on the Royal Australian Air Force (Figure 1).[7]

Figure 1: Fuel Tax Credits Scheme and other programs, 2023-24



Source: Treasury (2023) *Budget Paper No. 1: Budget Strategy and Outlook*

The overwhelming beneficiary of the FTCS is Australia's mining industry. The benefits of the FTCS are over $1 billion each year to both the iron ore and coal industries, as shown in Figure 2.

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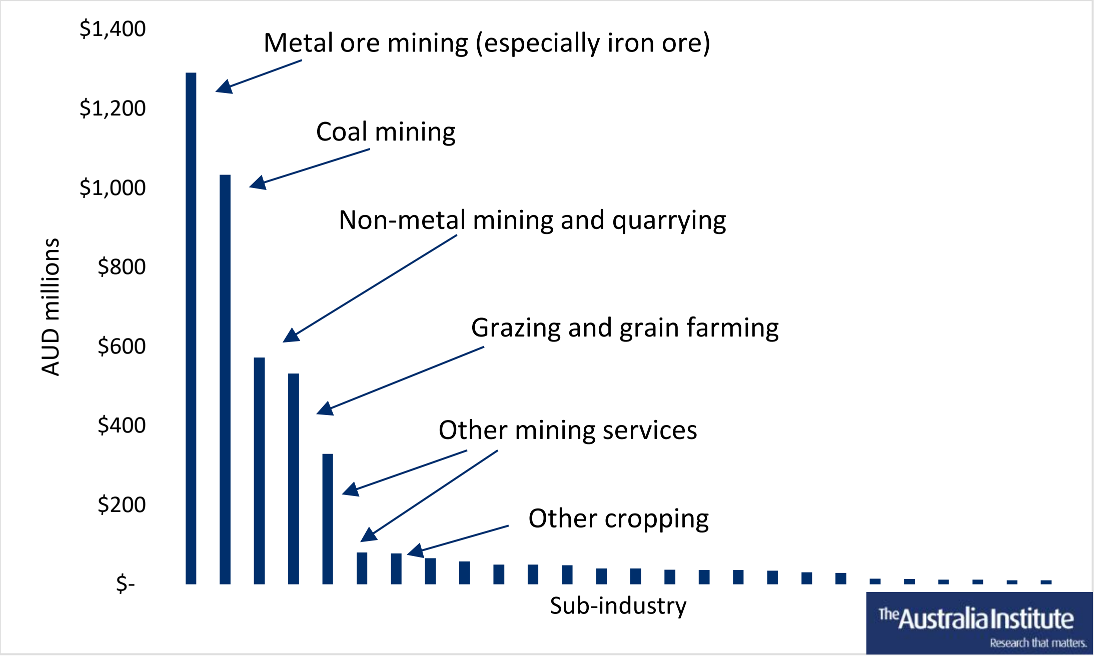
4 ATO (2023) *Excise duty rates for fuel and petroleum products*, https://www.ato.gov.au/Business/Excise-on-fuel-and-petroleum-products/Excise-duty-rates-for-fuel-and-petroleum-products/

5 Australian Government (2023) *Budget Paper 1: Strategy and outlook*, https://budget.gov.au/content/bp1/index.htm

6 ATO (2023) *Fuel tax credits – business*, https://www.ato.gov.au/Business/Fuel-schemes/Fuel-tax-credits---business/

7 Australian Government (2023) *Budget Paper 1: Strategy and outlook*, see Table 6.3.1.

Figure 2: Fuel Tax Credits Scheme – benefit by selected sub-industry



Source: Australian Tax Office (2022) Taxation Statistics – Excise Table 4: Excise and fuel schemes

Figure 1 shows that while some parts of the agricultural sector are significant beneficiaries of the FTCS, the vast bulk of the benefit goes to the mining industry.

None of these facts or figures are in dispute. What makes the FTCS controversial is that many researchers label it as a subsidy to fossil fuel users and, in the case of the coal industry, a subsidy to production of fossil fuel. This description as a subsidy has been widely reported in the media and plays a significant role in the debate around Australia's approach to climate policy.[8] The Australian Government, mining industry representatives and some researchers reject the term 'subsidy', adding to the controversy.

There is also an argument that maintaining access to the FTCS will delay the uptake of newer, lower-emissions technologies in the mining sector. Then-chairman of Fortescue Metals, Dr Andrew "Twiggy" Forrest argued in 2021 that the FTCS was a fossil fuel subsidy, and that miners should lose access from the FTCS from between 2025 to 2030, thereby encouraging the deployment of alternatives to diesel fuel.[9]

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[8] See for example Glenday (2021) *Calls to phase out fossil fuel subsidies after speculation about net-zero emissions target*, https://www.abc.net.au/news/2021-04-26/scott-morrison-climate-change-fossil-fuel-subsidies-net-zero/100094506

[9] Ker (2021) 'Forrest says diesel rebate should go after 2025', *Australian Financial Review*, https://www.afr.com/companies/mining/forrest-says-diesel-rebate-should-go-after-2025-20211123-p59bfk

IS THIS ABOUT ROAD FUNDING?

Defenders of the FTCS commonly claim that fuel excise funds roads and that the FTCS is justified because the fuel use of mining and agriculture is largely off-road. For example, National Party Leader David Littleproud described the Scheme in 2021 as “a rebate to those users that don’t use public roads”. “If you don’t use those roads and you’re fuelling up your machinery with diesel”, he continued, “then the excise would go to building those roads, we are giving you a rebate because you’re not using them". On this basis, Mr Littleproud claimed that the tax was “not a subsidy”.[10]

The view that companies that do not use public roads should not pay fuel tax relies on a link between fuel tax and road building that is heavily exaggerated. Road funding in Australia has not been based on fuel tax since 1955. Since then, road funding has been based on assessed need and funded from general revenue, aside from some minor, and usually temporary, arrangements.[11]

The only exception is the Fuel Indexation (Road Funding) Special Account. This was established in 2015 following the Abbott Government’s decision to reintroduce regular updates to fuel excise in line with inflation. The portion of collected fuel excise that comes from this ‘re-indexation’ decision goes into a special account that is required to be given to the states for road projects as approved by the Federal Infrastructure Minister.[12] In 2023, this account received and disbursed just over $1 billion,[13] or 5% of the total fuel tax collected, or 8% of the net fuel excise revenue.

To be clear, 95% of fuel tax revenue does not go into any dedicated road infrastructure fund. Like almost all tax revenues, fuel tax goes into “consolidated revenue”, which facilitates the funding of the full range of government expenses.

[10] Evans (2021) *Mining and farming industries savage Andrew Forrest’s bid to phase out fuel credit system*, https://www.theaustralian.com.au/business/mining-energy/mining-and-farming-industry-savage-andrew-forrests-bid-to-phase-out-fuel-credit-system/news-story/c9a1048816640cd1d88189451ccf038c

[11] For discussion of these exceptions see Terrill et al (2023) *Fueling Budget Repair: How to reform fuel taxes for business,* Box 5: Fuel tax is not used to pay for roads, https://grattan.edu.au/wp-content/uploads/2023/02/Fuelling-budget-repair-Grattan-report.pdf

[12] Australian Government (2015) *Fuel Indexation (Road Funding) Special Account Act 2015*, https://www.legislation.gov.au/C2015A00103/latest/text

[13] Australian Government (2023) *Special accounts balances and cash flows report*, https://www.finance.gov.au/special-appropriations-special-accounts

Further, the FTCS is not limited to fuel used off road.[14] Heavy vehicles (over 4.5 tonnes) on public roads also receive part of the rebate – or to be precise, they receive a FTC but also pay a road user charge.[15] However, heavy vehicles using public roads cause damage to public roads far in excess of the road user charges that they pay.[16] In this case, the view of the FTCS as a reimbursement for avoided road costs clearly does not apply.

Regardless of any link between road funding and the fuel tax system, taxpayers do not pick-and-choose which taxes they pay to governments based on which services are accessed. In other words, tax is not a user-pays system. Whether an individual or company uses or does not use a particular government service – for example, childcare, aged care, or disability support – has no bearing on whether they ought to be taxed for its implementation. As discussed below, The WTO and other international agencies are clear on this point.

WHO CALLS THE FTCS A SUBSIDY?

In addition to the Australia Institute, a range of Australian and international researchers have either specifically labelled the FTCS a subsidy, include it in their calculation of Australian fossil fuel subsidies, or consider it a support measure in need of reform.

Organisation for Economic Cooperation and Development (OECD)

The OECD publishes regular research on fossil fuel subsidies. It specifically mentions Australia's FTCS and considers it a subsidy,[17] following the World Trade Organisation's definition of a subsidy that includes where "government revenue that is otherwise due is forgone or not collected (e.g. fiscal incentives such as tax credits)."[18] The OECD has

[14] Australian Taxation Office (2023) *Travelling on Public Roads,* https://www.ato.gov.au/Business/Fuel-schemes/In-detail/Heavy-vehicles/?anchor=Travellingonpublicroads#Travellingonpublicroads

[15] National Transport Commission (n.d.) *Road user charges*, https://www.ntc.gov.au/laws-and-regulations/road-user-charges

[16] Grattan Institute (2023) *Fueling Budget Repair: How to reform fuel taxes for business.* See also National Transport Commission (2022) *Heavy vehicle charges consultation report*, https://www.ntc.gov.au/sites/default/files/assets/files/Heavy%20vehicle%20charges%20consultation%20report%202022%E2%80%9323.pdf

[17] OECD (2023) *Fossil fuel support – Aus*, https://stats.oecd.org/Index.aspx?DataSetCode=FFS_AUS

[18] OECD (n.d.) *OECD work on support for fossil fuels*, https://www.oecd.org/fossil-fuels/methodology/

called on Australia to "reduce or eliminate fuel tax exemptions for heavy vehicles and machinery."[19]

International Energy Agency (IEA)

The IEA's recent Energy Policy Review of Australia follows the OECD's approach:

> Fuel tax credits are applied to heavy vehicles for gasoline and diesel and heavy oil use in industry and electricity fuels. Fuel tax credits provide businesses with a rebate of the tax embedded in the price of fuel. In 2020-2021, fuel tax revenue was AUD 19.78 billion and businesses claimed AUD 7.6 billion of fuel tax credits, net of road user charges. This is counted as an indirect fossil fuel subsidy by the OECD…[20]

International research organisations

The International Institute for Sustainable Development (IISD), Overseas Development International (ODI) and Oil Change International consider Australia's FTCS to be a fossil fuel subsidy:

> Australia's fossil fuel companies currently benefit from significant tax breaks through the Petroleum Resource Rent Tax (PRRT) and fuel tax credits, among other measures. Recent reforms have done little to decrease these subsidies.[21]

International Monetary Fund (IMF)

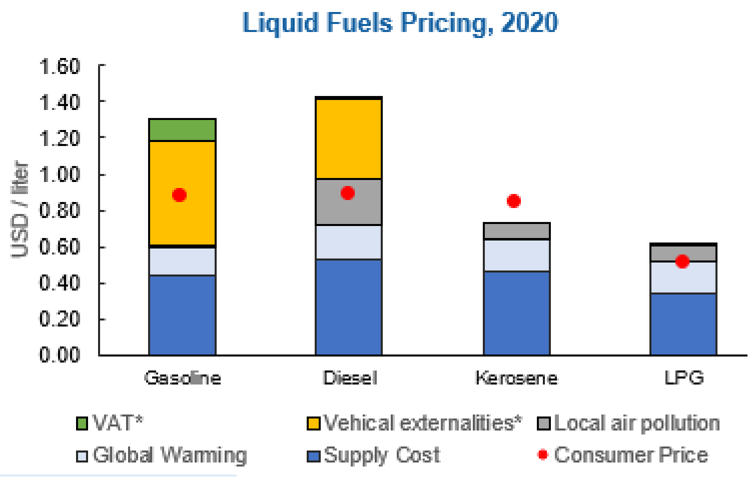
IMF research on Australia's fossil fuel subsidies does not mention the FTCS specifically. The IMF methodology compares the total market and environmental cost of fossil fuels with the consumer price, as shown in Figure 2 below:

[19] OECD (2024) *Achieving the transition to net zero in Australia*, https://www.oecd.org/economy/achieving-the-transition-to-net-zero-in-australia-9a56c9d2-en.htm

[20] IEA (2023) *Australia 2023: Energy Policy Review*, https://www.iea.org/reports/australia-2023

[21] IISD, ODI, Oil Change (2020) *G20 Scorecard of Fossil Fuel Funding: Australia*, https://www.iisd.org/publications/g20-scorecard-australia

Figure 3: Extract from IMF workbook on Australian fossil fuel subsidies



Source: IMF (2021) Still Not Getting Energy Prices Right

The IMF estimates fossil fuel subsidies by the difference between the consumer price (the red dots) and the environmental and supply costs of the fuel (the stacked bars).[22] The FTCS reduces consumer prices for both gasoline (petrol) and diesel, increasing the difference between price paid and total cost, increasing the value of the subsidy under the IMF's approach.

World Bank and World Economic Forum

These organisations do not mention Australia's FTCS specifically, but adopt a definition of fossil fuel subsidy that would certainly include it:

> Nature of [fossil fuel] subsidy and subsidy delivery mechanism:
>
> 4. Reduction of taxes paid. Examples include exemptions or reductions from taxes normally applied, such as VAT, tax holidays for petroleum profit tax or corporate income tax, and tax credits…[23,24]

[22] IMF (2021) *Still Not Getting Energy Prices Right: A Global and Country Update of Fossil Fuel Subsidies*, https://www.imf.org/en/Publications/WP/Issues/2021/09/23/Still-Not-Getting-Energy-Prices-Right-A-Global-and-Country-Update-of-Fossil-Fuel-Subsidies-466004#:~:text=IMF%20Working%20Papers&text=Globally%2C%20fossil%20fuel%20subsidies%20were,percent%20of%20GDP%20in%202025.

[23] Kojima and Koplow (2015) *Fossil Fuel Subsidies: Approaches and Valuation*, https://documents.worldbank.org/en/publication/documents-reports/documentdetail/961661467990086330/fossil-fuel-subsidies-approaches-and-valuation

[24] See also Kojima (2015) *What exactly is a fossil fuel subsidy*?, https://www.weforum.org/agenda/2015/04/what-exactly-is-a-fossil-fuel-subsidy/

Grattan Institute

The Grattan Institute is a prominent Australian research organisation, with a well-regarded energy and climate research program. Grattan urges reform of the FTCS "to help repair the budget and reduce carbon emissions," noting that the policy is "out of step with the government's climate goals" which include "the phase-out of inefficient fossil-fuel subsidies."[25]

WHO DOES NOT CALL THE FTCS A SUBSIDY?

The Australian Government and its agencies do not consider the FTCS to be a subsidy. Representatives of the mining industry are also opposed to this description.

Productivity Commission

The Australian Government's Productivity Commission has written:

> One of the largest components of both the OECD's and the Australia Institute's estimates of assistance to the fossil fuel sector is fuel tax credits (FTCs). However, whether FTCs should be considered industry assistance is ultimately a question of the appropriate 'baseline' — what might be regarded as 'normal' policy settings — against which the design and effects of Australia's fuel excise and FTC system should be assessed. The Commission does not regard the baseline used in the OECD's and the Australia Institutes methodologies as a compelling approach to identifying industry assistance for the [Trade Assistance Review].[26]

In our view, just because the FTCS has become 'normalised' does not make it any less of a subsidy under most definitions. Regardless, the Productivity Commission's views are influential on publications from other Australian federal agencies, with one researcher from the Parliamentary Library concluding:

> In summary, the rebate for excise paid on fuel that eligible businesses use as inputs is not a subsidy to fuel use. Rather, the rebate is designed to relieve businesses of input taxes that can reduce output and living standards. The

[25] Terrill et al (2023) *Fuelling budget repair: How to reform fuel taxes for business*, https://grattan.edu.au/report/fuelling-budget-repair/

[26] Productivity Commission (2021) *Trade and Assistance Review 2020-21*, https://www.pc.gov.au/ongoing/trade-assistance/2020-21

> Productivity Commission does not consider the rebate to be a form of assistance.[27]

It is worth reiterating here that to 'relieve business of input taxes', as put by this researcher, falls squarely within the WTO definition of a subsidy. Here again, the disagreement is around the use of the word subsidy, or 'assistance', compared to 'tax relief'. What is not contested is the substantial cost of the FTCS, and the disincentive to decarbonise that flows from this policy.

Minerals Council of Australia

As the main lobby group for the mining industry, the Minerals Council is defensive of the FTCS:

> The credit is not a subsidy, it does not lower the price of fuel paid by users.
>
> There is no cost to taxpayers; it does not equate to spending by governments in other areas.
>
> Just as the GST is rebated on business inputs, the credit removes what is an additional tax on a business input. Budget papers rightly note this for transparency.
>
> Any change to the credit would be an increase in tax.
>
> The repetition of the word subsidy is wrong and misleading.[28]

The Minerals Council is incorrect to claim there is no cost to taxpayers. This cost is significant and quantified in the Federal Budget every year, as discussed above. The key point in contention is around the use of the word subsidy rather than the cost of the policy.

The Minerals Council statement quoted here makes no mention of road use. A separate Minerals Council site focuses exclusively on the debate around the FTCS and road use.[29] That site uses the term "diesel road tax" rather than fuel excise, which it claims "is intended for heavy road vehicles such as large trucks". This ignores the fact

[27] Webb (2012) *Fuel tax credits: are they a subsidy to fuel use*?, https://www.aph.gov.au/About_Parliament/Parliamentary_Departments/Parliamentary_Library/FlagPost/2012/May/Fuel_tax_credits_are_they_a_subsidy_to_fuel_use

[28] MCA (2023) *Fuel Tax Credit is not a subsidy*, www.minerals.org.au/resources/fuel-tax-credit-is-not-a-subsidy/

[29] Fuel Tax Credit Alliance (2022) *Road taxes are for road users*, www.roadtaxesareforroadusers.com.au/

that fuel excise applies to fuels other than diesel and that it is light vehicles that pay the full rate of excise, unlike heavy vehicles that receive partial fuel tax credits.

Further, the comparison to GST is spurious. The GST is explicitly designed as a tax on consumption, hence the exclusion of costs which go into production.

Though it is important to note that the entire minerals sector does not hold the view of the MCA – Dr Forrest, as cited above, has argued that the maintenance of the FTCS subsidy is actually slowing innovation in the mining sector.

CONCLUSION AND CONTEXT

The Fuel Tax Credits Scheme is one of Australia's most expensive government programs, expected to cost $9.58 billion in 2023-24.[30] In comparison, the Australian Government has committed to spend significantly less on Official Development Assistance, which sits at $4.77 billion for the 2023-24 year,[31] which includes:

$44 million allocated to Fiji,

$50 million allocated to Vanuatu,

$11.4 million allocated to Tuvalu,

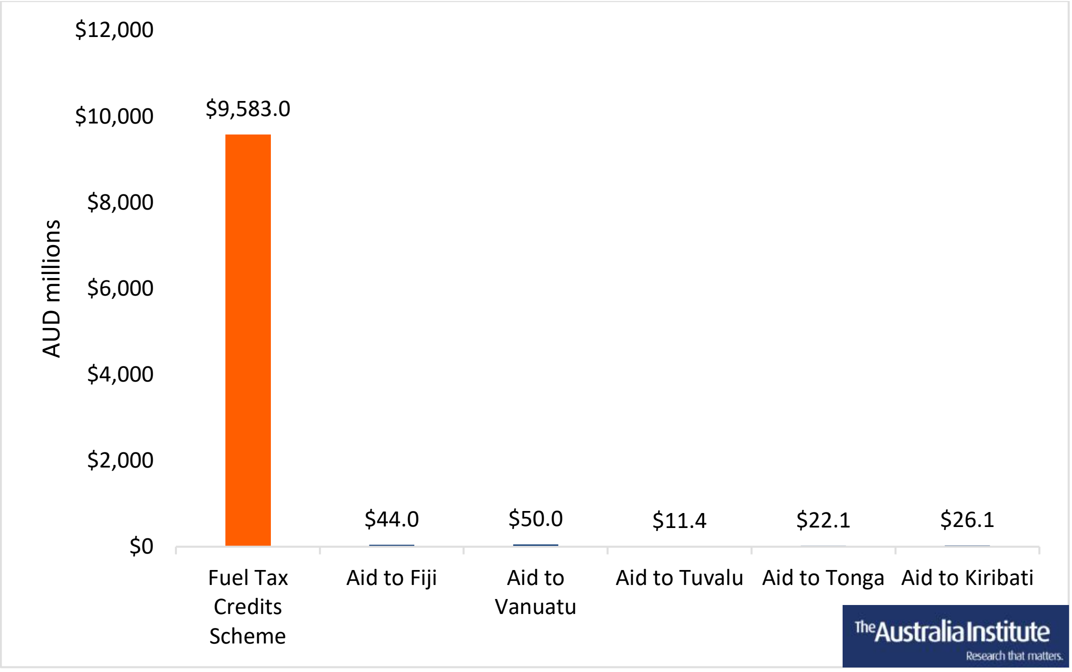
$22.1 million allocated to Tonga, and

$26.1 million allocated to Kiribati (Figure 4).

[30] Listed as the 18th largest expense in Australian Government (2023), *Budget Paper 1*.

[31] Department of Foreign Affairs and Trade (2023) *Australia's Official Development Assistance Budget Summary 2023-24* https://www.dfat.gov.au/about-us/corporate/portfolio-budget-statements/australias-official-development-assistance-budget-summary-2023-24

Figure 4: FTCS compared to select Pacific aid expenditure, 2023-24



Source: Treasury (2023) *Budget Paper No. 1: Budget Strategy and Outlook*; Department of Foreign Affairs & Trade (2023) *Australia's Official Development Assistance Budget Summary 2023-24*

While the government notes that "rising global pressures including climate change" are amongst its primary concerns for the Pacific region, and that it "recognises the urgency and far-reaching implications of the climate crisis", it is still allocating more funds towards subsidising fossil fuels through the Fuel Tax Credits Scheme than towards helping Pacific countries mitigate and adapt to climate change.[32]

Domestic debate about Fuel Tax Credits Scheme remains dominated by the question of whether the scheme counts as a fossil fuel subsidy. However, at least internationally, the debate is settled: the Fuel Tax Credits Scheme is labelled a subsidy by the OECD, the International Energy Agency, the International Institute for Sustainable Development, the Overseas Development International and Oil Change International. Other organisations adopt a definition of subsidy which would include the FTCS.

The Fuel Tax Credits Scheme acts as a disincentive for major fossil fuel users to decarbonise. This portion of forgone government revenue could otherwise be spent on domestic or international efforts to decarbonise or mitigate the effects of climate change. From both a fiscal and environmental point of view it is a damaging policy in need of urgent reform.

[32] Department of Foreign Affairs and Trade (2023) *Australia's Official Development Assistance Budget Summary 2023-24*