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Dear Secretary

**Review into Australia's Future Tax System
Heavy vehicle charges and road pricing**

Following the release of the La Trobe University paper into the reform of taxes related to roads and transport, the Australian Trucking Association (ATA) would like to provide your review with some input into the area of heavy vehicle charges.

Professor Clarke and Dr Prentice's paper addressed the need to adequately recover costs from heavy vehicles and ensure sufficient infrastructure supply, and the potential of the excise system to charge for road use and externalities like congestion and greenhouse gas emissions.

Unfortunately, the paper did not incorporate any industry input. It therefore lacked practical insight into the feasibility of mass-distance-location pricing using telematics.

In the trucking industry's view, mass-distance-location pricing using telematics is not a viable option. It is not, as the paper suggested, a low cost option. For example, the cost and difficulty of assigning the road network to charging categories has been completely overlooked.

Instead, the ATA would like to put forward an alternative charging tool: fuel-based charging.

The current fuel tax credit system is easy to administer, user friendly and allows operators to distinguish between different vehicle uses.

We propose expanding this system to increase the road user charge paid by the trucking industry, with the charge struck at different levels for local and other vehicles. At the same time, truck registration costs would be reduced, achieving the goal of accounting more directly for the specific costs imposed by road users. The total amount recovered from the trucking industry would remain the same.

This alternative fuel-based charging mechanism would be linked to improvements in road expenditure and infrastructure supply.

Road reform as directed by COAG is still in the early stages, with fundamental research and feasibility analysis still to be conducted, especially around mass-distance-location charging. Infrastructure supply reform, arguably the most critical area for pursuing productivity benefits, has been neglected so far in the reform process.

Road related expenditure should provide sufficient maintenance and capital investment funding to operate the optimal amount of road infrastructure. To do this, charging regimes should be transparent and set as accurately as feasible. Under fuel-based charging, revenue generated from heavy vehicle use could be hypothecated towards future heavy vehicle related infrastructure spending. Funding could be directly available to all levels of government and related to the type of road access provided.

Under this model, local government could be direct funding recipients, in contrast to the current system and the mass-distance-location pricing model currently under consideration.

Our proposed reform would be an important step forward, because improving heavy vehicle access to local roads is a fundamental key to productivity advances. The reform would ensure sufficient funding for infrastructure supply, giving road owners an incentive to maintain and upgrade infrastructure to optimum levels related to use.

I have attached an ATA staff paper outlining a possible fuel based charging system. It reflects the ATA's broad policy approach, although its details have yet to be approved formally. I believe, however, that it offers a better and more practical way forward than the existing proposal to use mass-distance-location pricing based on telematics.

I would like to meet with you to discuss this important and practical tax reform proposal. My office will contact your staff to see if it might be possible to arrange a mutually convenient opportunity.

Yours sincerely



Stuart St Clair
Chief Executive

17 August 2009

ATA's Fuel-based Charging Mechanism policy proposal overview

This paper examines the option of rebalancing heavy vehicle charges by increasing the variable cost component of the charge. This is through a shift in registration charge to fuel excise.

Currently, heavy vehicles are charged through registration fees and the road user charge, where the road user charge is directed into Commonwealth income with the states retaining the proceeds of the registration charges. Under the fuel-based charging mechanism, heavy vehicle road user charges are modified to comprise a greater fuel cost component, with the registration charge component being reduced to a base charge that closer matches car registration cost. The fuel based cost recovery charge would be based on the PAYGO calculation and be collected within the taxation system on the same basis as the existing fuel related road user charge.

This is a highly efficient and cost effective charging mechanism that will refine road user charges and deliver infrastructure supply side reform. Increasing the weight of the variable charge is likely to change business behaviour, improving the efficiency of how the freight task is carried to the economic benefit of the nation.

A distinct feature of this system is the restructuring of infrastructure funding arrangements. Revenue distribution to state and local government is tied to heavy vehicle related expenditure. Funding is divided into two parts, with a minimum payment for maintenance and an additional amount for capital investment that is linked to road classification.

There are two classifications of vehicles:

Local: 2 axle rigids, special purpose vehicles and buses.

Heavy: 3 axle rigids and all articulated vehicles.

Dividing the vehicle fleet creates a stronger link between the associated cost and the type of vehicle paying for it. Local classification vehicles can access almost all roads, require less infrastructure investment and have a lower impact on roads. Heavy classification vehicles demand greater infrastructure provision, and more impact on roads, so should be charged accordingly. Fuel consumption between the classes varies significantly, with different efficiencies and loads, as well as average distance travelled.

To link road use and subsequent funding, as well as promote network expansion, the national road network will be classified into sub networks based on access arrangements and maximum vehicle class capacity. This is consistent with COAG's directive to road agencies to classify the road network. There are eight potential classifications, based on the Performance Based Standards classifications plus B-triple routes. These are GA, BD, long BD, B Triple, type 1 RT, long type 1 RT, type 2 RT and long type 2 RT.

Cost recovery

The amount required to be recovered will be based on the current PAYGO calculations. That is, based on actual past expenditure and a one year forward estimate. Heavy vehicle users should be responsible for paying the relevant additional cost of expanding road capacity and durability to cater for heavy vehicles, as is currently the case.

Road user charge

The fuel tax credit rate will be reduced, essentially increasing the road user charge to broadly replace the decrease in registration revenue. The road user charge will be a cents per litre charge representing the amount of road expenditure attributable to trucks.

There will be two different road user charges, for local and heavy classes of vehicles. The rebate amount will depend on the allocated cost amount for the two vehicle classes spread across the vehicle fleets in fuel consumption, as shown in Table 1. The road user charge would apply to all fuels consumed by heavy vehicles, including alternative fuels, which may be included in separate rebate schemes.

Table 1: Current charging system

| Estimated 2009 HV Revenue (\$m) | Fuel-based | Registration | Total |
|---------------------------------|------------|--------------|-------|
| Local | 471 | 153 | 624 |
| Heavy | 1064 | 574 | 1639 |
| All heavy vehicles | 1536 | 687 | 2223 |

Fuel projections SMVU 2006-2007, RUC 2.1c/ltr Registration revenues NTC 2007 Determination

Table 2 Current revenue composition between vehicle classes

| Revenue shares | Fuel-based | Registration | Total |
|--------------------|------------|--------------|-------|
| Local | 31% | 22% | 28% |
| Heavy | 69% | 84% | 74% |
| All heavy vehicles | 69% | 31% | 100% |

Registration charge

The role of the registration charge is condensed to serve the purpose of vehicle and responsible operator identification. Registration charges, including trailer registration, will be reduced to a minimum value, matching the cost of light vehicle registration. For all trucks, prime movers and trailers, the nominated amount of registration is \$400. It will cover the administration costs and a fundamental road access revenue contribution. Compulsory third party insurance would remain payable as it is now. Using the PayGo 2007 data registration revenue should be around \$200.3 million where registration is \$400 for all vehicles and trailers.

Table 3

| Amount to be recovered (\$m) | |
|------------------------------|------|
| Current revenue | 2223 |
| (-) FBC rego revenue | 200 |
| FBC fuel revenue | 2022 |

So, to keep total revenue the same, with reduced registration revenue to \$200.3 million, revenue from fuel excise will need to earn \$2022 million.

Using the revenue shares, the amount the needs to be recovered can be allocated by vehicle class.

Table 4 Fuel-based charging scheme

| Estimated FBC Revenue (\$m) | Fuel-based | Registration | Total |
|-----------------------------|------------|--------------|-------|
| Local | 620 | 45 | 665 |
| Heavy | 1402 | 167 | 1569 |
| All heavy vehicles | 2022 | 200 | 2223 |

Table 5 Projected fuel consumption rates

| Fuel Consumption (m litres) | 2008 | 2009 |
|-----------------------------|------|------|
| Local | 2104 | 2171 |
| Heavy | 4905 | 5075 |

Projected using SMVU 2003-2007 trend. Vehicle class shares based on 2007 PAYGO data

Table 6 Estimated new road user charge

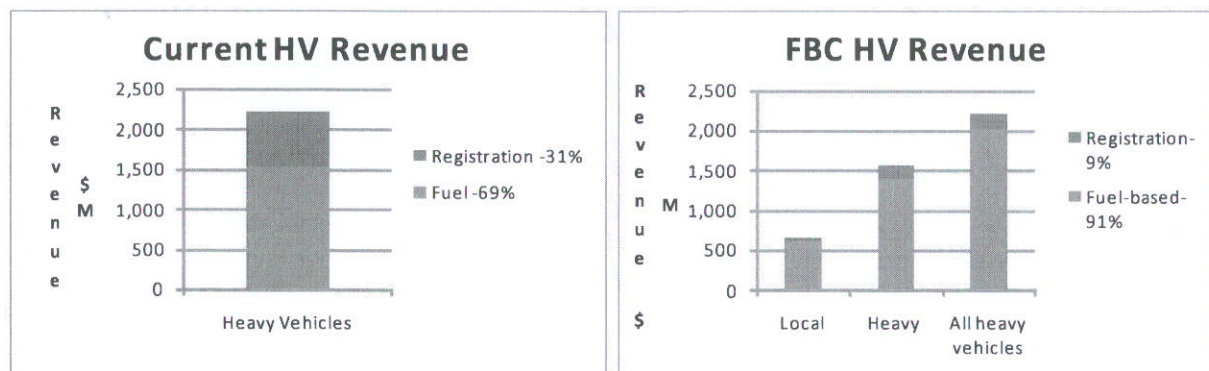
| Road User Charge | Local | Heavy |
|------------------|-------|-------|
| c/ltr | 28.6 | 27.6 |

The road user rate for local vehicles is slightly higher than heavy classed vehicles, as vehicle characteristics and average tasks contribute to fuel consumption differences. Heavy vehicles will use greater amounts of fuel to operate, and local vehicles on average do less kilometres, so have less distance to recover their allocated amount.

Revenue

As the amount to be recovered is kept constant, the overall change in the revenue total is minimal. The composition of the revenue base is what changes.

Figure 1: Revenue Composition



The proportion of fuel-based revenue and registration revenue as a portion of total revenue changes. Registration revenue decreases from 31% to 9%, and fuel-based revenue increases from 69% to 91%.

Revenue is collected in a centralised system through the efficient existing taxation system that already collects most of the heavy vehicle charging revenue. Although it differs from the current system in that revenue will be kept aside for heavy vehicle road expenditure, rather than being absorbed into general government revenue. A comparison of funding between the two schemes is shown in Table 7 Funding Distribution

Expenditure

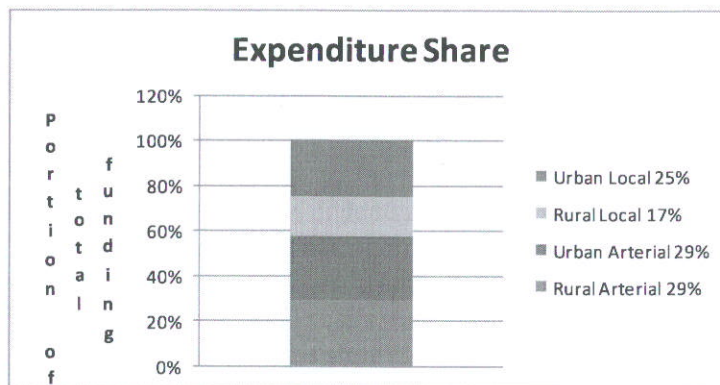
There are three avenues that revenue is directed to: recovering the heavy vehicle proportion of PayGo 'common costs', maintenance costs and some funds for future capital investments.

The proportion of common costs attributable to heavy vehicles would be financed out of the (reduced) registration revenues, collected and redistributed by the states. Revenue from fuel will be

held as a pool of funds for heavy vehicle spending, rather than being combined into commonwealth revenue.

The remaining revenue is divided at two stages. First, it is divided into state and local government funding pools. Here, this has been done using an average of where average nominal expenditure for the past seven years has occurred (NTC AA 2009). Local roads (urban and rural) are allocated to local government, and arterial roads (urban and rural) are the responsibility of state governments. The historical average of this is shown in Figure 2. Of total road expenditure, the average proportions have been 42 per cent for local road funding, and 58 per cent for state road funding. Currently, local government funding is dependant on rates and revenue distribution from states. This can be highly variable, causing funding uncertainty and giving rise to inefficient infrastructure provision.

Figure 2



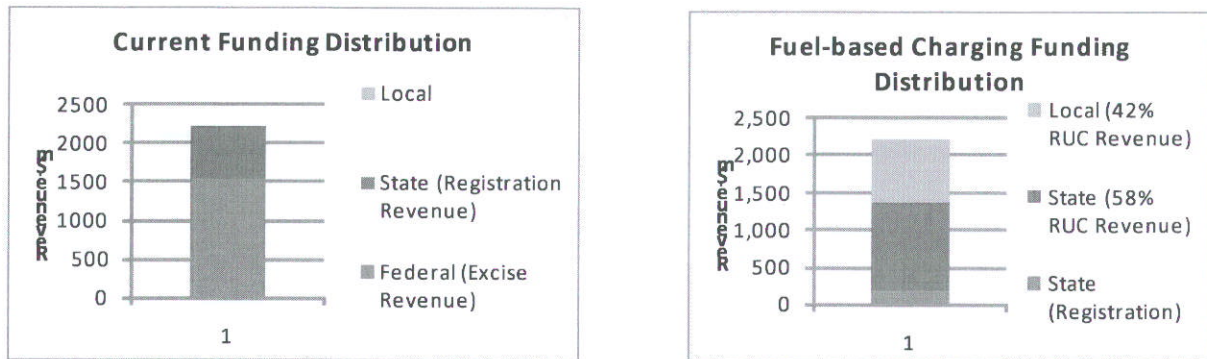
Based on average total nominal expenditure (NTC AA) 2009

The revenue drawn from heavy vehicle use is the basis for future heavy vehicle expenditure. This fund will need to be expanded as freight and infrastructure demand grows. It may increase through additional government infrastructure spending, of which a heavy vehicle proportion will be incorporated to update the road user charge. Another option is to have government contribution ratios applied to funding.

Table 7 Funding Distribution

| Current average | \$ million | Fuel-based Charging | \$ million |
|------------------------------|------------|-------------------------|------------|
| Federal (Excise Revenue) | 1536 | State (Registration) | 200 |
| State (Registration Revenue) | 687 | State (58% RUC Revenue) | 1,170 |
| Local | 0 | State Total | 1,371 |
| | | Local (42% RUC Revenue) | 852 |
| Total | 2,223 | Total | 2,223 |

Figure 3



The two pools of funds are then categorised into maintenance and capital spending needs based on past average expenditure. The average ratio of this division has been around 34 per cent and 66 per cent on maintenance and capital respectively.

Table 8

| Fuel-based Charging (\$m) | |
|---------------------------|-------------|
| Maintenance 34% | 766 |
| Capital 66% | 1457 |
| Total | 2223 |

Limited state expenditure data, 2004-05.

Under this scheme, the total amount directed to maintenance would be \$766 million and \$1457 million would be available for capital investment.

Maintenance funding will be an amount automatically distributed consistently across infrastructure providers and road networks. It would take into account network size, the volume of heavy vehicle traffic volume and the rates of impact.

Funding for assisting in capital investment will be drawn from the remaining pool of road user charge revenue, and linked directly with network type. In this scenario, fund pools available to state and local governments are \$1371 million and \$852 million respectively. Infrastructure providers from both these levels of government will have equal right to their respective pool of funds. Funds are granted upon application, based on benefit-cost analysis and take into account freight network benefits including community service obligations. This will promote investment efficiency and ensure funding goes to where it will be most effective. Funding is only available for routes above general access classifications, as heavy vehicles use of general access roads is paid for in common cost funding (through registration revenue in this case). The higher the access provided by the network classification, the greater weighting given to the application. Thus, there is a financial incentive to improve road access, and increased future use will be compensated.

Incentives

Fuel is a variable cost, and consumption will increase with distance and mass. There is an incentive for operators to use fuel efficient, environmentally friendly vehicles. Change in vehicle choice should promote the increased use of high productivity vehicles, which will have national economic and safety benefits.

To an extent, congestion will also be addressed in this scheme. Travelling in heavily congested areas is more fuel intensive, thus encouraging behavioural change. Other efforts to address congestion can

be complex and expensive. Targeting measures do not need to be in a national framework, but do need to include light vehicles.

Benefits

The scheme is efficient to administer from a regulatory perspective, and requires little industry adaptation. For this reason the implementation costs would be minimal, with low evasion opportunity due to the tax system collection mechanism using Business Activity Statements that operators are already familiar with. Additionally, the model is adaptable to forthcoming policy changes like a national registration system.

For operators, the transparency and liquidity of this scheme would improve the ease of doing business, even for operators whose overall costs increase. Reducing the financial burden of a lump registration payment will aid business' cash flow. Increasing the fuel cost component provides a way for operators to transparently pass their costs onto customers, through a fuel levy.

Though this form of cost allocation may be subject to some averaging between vehicle classes, data and technological restrictions make other charging methods unfeasible in the near future. There are significant efficiency benefits likely to flow from the fuel-based charging framework, both from lower administration and collection costs, but more importantly through improved incentives for road users and road infrastructure providers. The strength of this model is the very strong signals about use to individual operators, which is something lacking in the current PAYGO model.

Altogether, it is a simple, fair and transparent model that rewards efficiency and improves the incentives for users and suppliers of road infrastructure.