NTC
AUSTRALIA
National Transport Commission

Level 15 / 628 Bourke Street
Melbourne VIC 3000

P 61 3 9236 5000
F 61 3 9642 8922

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Australia's Future Tax System Review Panel
AFTS Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

1 May 2009

NTC Submission on Australia's Future Tax System Consultation Paper

Dear Sir/Madam

The National Transport Commission (NTC) welcomes the opportunity to make a submission on the consultation paper on Australia's Future Tax System (AFTS). The NTC is an independent agency, advising the Transport Ministers of the Australian Government and state and territory governments on land transport regulatory and operational reform. The NTC is currently responsible for updating heavy vehicle road infrastructure charges and has a significant involvement in the reforms which are focused on delivering "incremental pricing" and mass-distance location-based pricing for heavy vehicles as outlined by the Council of Australian Governments (COAG) in its road reform plan (2007).

The COAG road reform plan will deliver economic benefits over the longer term by improving the economic efficiency of heavy vehicle charges, and the AFTS Review will need to consider the implications of the change in the nature of revenue streams resulting from this reform. In addition, there are even greater potential benefits to be realised from adopting a more holistic approach by expanding the reform agenda to include light vehicle charges as part of a national people moving strategy, which would seek to address issues such as urban congestion and the right mix of public versus private modes of transport.

As part of this COAG plan, a system that involves heavy vehicles being charged based on their actual use of the roads (in terms of their mass, distance travelled and their use of different parts of the network) will, in the longer term, allow revenues from heavy vehicles to be distributed in a way that reflects road use and the costs of road infrastructure. However, an interim solution through the taxation system may be required to support those governments that do not receive an adequate return of registration revenues to enable the required investment to support current and future road usage. In addition, the lack of a direct connection between revenue from the fuel excise and road expenditure can also be addressed in the interim in order to achieve more efficient and certain funding for roads.

Finally there are a range of taxes and concessions that are associated with the ownership and use of motor vehicles which should be reviewed in the context of economic efficiency and broader government objectives such as those relating to the environment.

Should you wish to discuss the matters raised in this submission, Matthew Clarke, Senior Manager Economics can be contacted by telephone (03 9236 5028) or email (mclarke@ntc.gov.au).

Yours sincerely

Nick Dimopoulos
Chief Executive

ATTACHMENT

BACKGROUND

National Transport Policy Framework
In February 2008, The Australian Transport Council (ATC) agreed that there is a need for a national approach to transport policy and endorsed the National Transport Policy Framework (ATC 2008). ATC consists of transport ministers from federal, state and territory governments. It is the ministerial forum for the coordination and integration of transport policy issues at a national level.

At its May 2008 meeting, ATC agreed to a vision, policy objectives and policy principles in May 2008 (reproduced in the Appendix). In the context of the Tax Review, the objectives and principles agreed to by transport ministers has a strong emphasis on:

1. the promotion of a national efficient transport market place supported by national regulation
2. transparency in funding and charging to provide equitable access to the transport system, through clearly identified means where full cost recovery is not applied
3. the establishment of transport infrastructure pricing structures that send appropriate signals to ensure efficient infrastructure investments.

ISSUES

1. Need to reform the structure of road user charges

The current charging system for light and heavy vehicle users provide little, if any, signals to road users about the economic cost associated with their use of particular roads or varying levels of mass and distance travelled. Under the COAG reform plan, the inefficiencies of heavy vehicle charges will be addressed by introducing, if feasible, more cost reflective road user charges, such as mass-distance location-based pricing. Under this approach, road users would be charged on the basis of their use of the road network taking into account the mass of the vehicle, the distance travelled and the use of different parts of the network. In addition, the revenue from this system would be returned to the road network under an efficient investment framework that would link the revenues from a particular road or network of roads to infrastructure spending on those roads.

A high level assessment of the changes from the current system to a new future system is outlined in the following table:

Table 1: Approaches for Heavy Vehicle Charges – Current and Future

	Current Charging Approach	Future Approach under Mass-Distance Location Based Charging
Type of Road Charges (Heavy Vehicles)	• Registration charge (plus other charges e.g. stamp duty, insurance) • Fuel excise (via a "road user charge")	Charge based on: • Mass of vehicle • Distance travelled • Location or type of roads used
Revenue Collection & Spending	• State Government collects registration charges • Federal Government collects fuel charge	• Future institutional arrangements for a mass-distance based charging system are still to be determined. • Future arrangements would be based on linking revenue from roads to investment.

Under the COAG reform plan, the reliance on taxation measures will diminish since road charges would be based on mass, distance and location parameters and the funding for road infrastructure spending would be directly linked to the heavy vehicle charges. Specifically, this would mean that heavy vehicles would no longer be subject to the fuel excise (or "road user charge") and the amount currently recovered through the fuel excise of around $1.23 billion would be directly allocated to road spending. Nevertheless, there may still be a role for registration fees and/or fuel taxes if the revenue from variable charges falls short of the overall revenue requirement.

It is important to note, however, that the COAG reform plan does not address the economic inefficiencies inherent in the charging system for light vehicles. Currently, light vehicle charges are predominantly fixed (registration and stamp duty) in nature and provide no signals to users of the economic cost of their road usage. Consequently, there are likely to be significant inefficiencies in the choice between private and public transport modes and the timing and route decisions by light vehicle users. These inefficiencies will be greatly reduced by reducing the reliance on fixed charges and introducing variable charges for light vehicles that are more reflective of the marginal cost of road use. This marginal cost would include the impacts of congestion on the road network.

More efficient price signals will benefit society by promoting a more efficient use of the road network and investment in road infrastructure. This holistic approach to include light vehicles is very important since investments in the road network are often made taking into account both light and heavy vehicle considerations. Therefore, there may be merit in establishing an independent inquiry with the specific purpose of developing a medium to long term reform plan for light vehicle charges. However, this reform plan should also be developed in the context of a national people moving strategy which would outline a long term reform agenda for moving people. This agenda would not only strive to achieve sound economic efficiency objectives, such as through reformed light vehicle pricing and linking revenues to expenditure, but also broader transport objectives, such as achieving the right balance between public and private modes of transport and achieving stated social objectives. Therefore, this reform agenda would focus on how to achieve the best use of funds to achieve the optimal way of moving people which is cost effective and addresses broader service level objectives.

Finally, the current charging system for light and heavy vehicle users does not fully account for the external costs of road use, such as pollution, accidents, congestion and noise. The NTC supports reforming road charges to reflect external costs where the economic benefits outweigh the costs. The NTC believes that pricing reforms are a sensible approach to addressing the inefficiencies associated with carbon pollution (such as the Carbon Pollution Reduction Scheme) and urban congestion.

In particular, congestion pricing has the potential to form an important part of a national people moving strategy since it could influence private motoring decisions through time and/or location based pricing. This may result in better utilisation of the road network through encouraging private motorists to travel in off-peak times of day and encourage a better mix of private motoring and public transport through cost-reflective congestion pricing signals.

However, it may be more economically desirable to rely on supply side solutions, such as noise barriers, improvements in road design and pavement quality, rather than pricing reforms, to address accident, noise and other externalities.

RECOMMENDATIONS:

The AFTS Review should prepare the tax system for a world in which road user charges in the medium term are no longer recovered through registration and fuel revenues and are based on mass-distance location-based charges. This new world would also involve charging revenue being more closely linked to road expenditure, which could be achieved by revenue being directly allocated to the road infrastructure service provider.

The AFTS Review should recommend the introduction of a reform process for light vehicle charging and associated road investment. This reform process should be aligned, where necessary, with the COAG road reform plan for heavy vehicles and form part of a broader national people moving strategy.

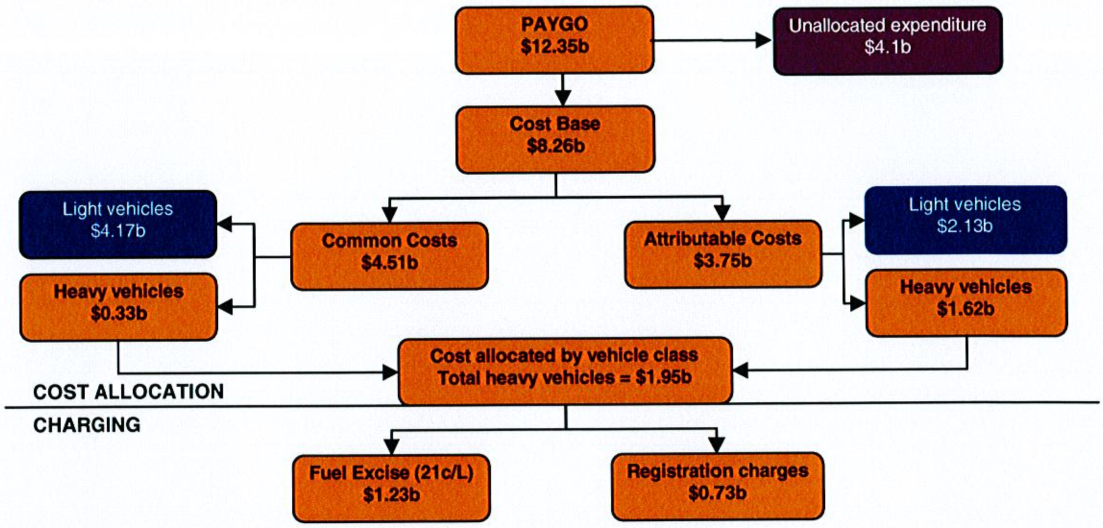
2. Need to consider interim measures to improve the link between revenue and road investments

Currently, the NTC is responsible for preparing national heavy vehicle charges and the state governments are responsible for setting light vehicle charges. Reflecting the multi-use nature of Australia's road network, the NTC calculates heavy vehicle charges and the fuel excise on the basis of a cost allocation model that covers both light and heavy vehicles. This cost allocation model allocates total road expenditure costs (the "cost base") to both heavy and light vehicles for the purposes of determining the amount of cost that needs to be recovered from heavy vehicles.

The model also makes a distinction between those costs that are directly attributable to road use ("attributable costs" – for example due to the road wear impact of vehicle use) and those that are not directly attributable ("common costs' – for example due to the impact of weather).

This is performed for both light and heavy vehicles as shown below (Figure 1), as outlined in the 2007 charging determination[1].

Figure 1: PAYGO - Annual Cost Allocation



Whilst there is a separation of costs between heavy and light vehicle charges and revenues for the calculation of charges, in reality there is not such a separation in actual expenditure. An investment in a road serves a mixed use – for both heavy and light vehicles. However, vehicle related revenues are not currently returned to the government which incurs the cost. Instead, fuel revenues are effectively redistributed to state and local governments via indirect means (such as Commonwealth Grants and Commonwealth infrastructure funds such as Auslink and the Building Australia Fund). As a result, road agencies and state, territory and local governments often hold the view that they do not recover revenues sufficiently to make the required investment for a sustainable transport network.

Improvements in the efficiency of road investment will be achieved over the longer term by reforming road user charges and institutional arrangements (although the current COAG road reform agenda limits this to heavy vehicles). However, there are two issues that can be addressed through this review in the interim:

1. State governments do not recover sufficient heavy vehicle registration revenues compared to heavy vehicle expenditure. This creates a reliance on uncertain road funding transfers for heavy vehicle road usage from the federal government in order to ensure that roads are funded in a sustainable way. This reliance is illustrated in Figure 2 which compares the current registration revenue collected from heavy vehicles by

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[1] National Transport Commission (2007), *Heavy Vehicle Charges Determination Regulatory Impact Statement Volumes I and II*

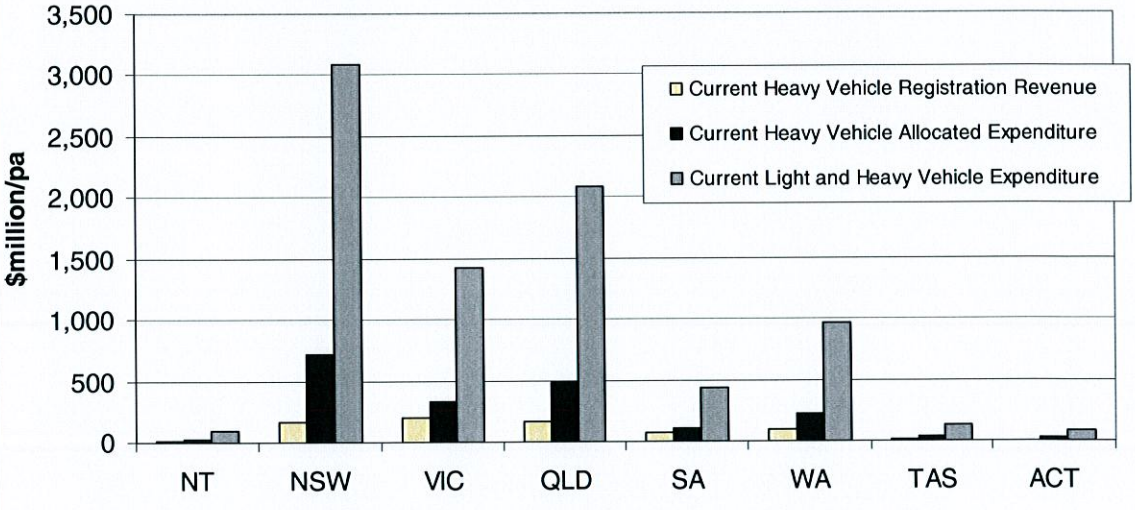
each state and territory annual road expenditure with the current estimated expenditure on heavy vehicles (as estimated under the NTC cost allocation model).

This creates a significant disconnect between revenue and expenditure and highlights the potential for distortions in road spending decisions to arise. For example, some states may not receive sufficient funds from the combination of registration revenues and transfers from the federal government in order to ensure a sustainable road network thereby restricting efficient levels of investment.

2. Heavy vehicle expenditure is a relatively small proportion of total expenditure on light and heavy vehicles – as illustrated in Figure 2. The implication of this is that the way in which light revenues are directed back to road agencies and state, territory and local governments has a significant impact on both the overall road network in a state and territory and the success of a suitable heavy vehicle road network.

   However, as the \$6.3 billion[2] of light vehicle related costs (as per Figure) are not directly recovered and allocated to road expenditure, investment in the transport network becomes more subject to political processes, despite the fact that road users make direct contributions to the taxation system through the fuel excise and registration charges. This would mean that of the approximate \$11.6 billion that is collected through light vehicle charges (state based registration charges and the fuel excise), around \$6.3 billion could be directly allocated to road expenditure which would provide certainty to state, territory and local governments about light vehicle funding for roads.

Figure 2: Comparison - Heavy Vehicle Registration Revenue & Allocated Expenditure Vs Total Vehicle Expenditure



Note that the sum of current light and heavy vehicle expenditure equates to the cost base in Figure 1 which excludes unallocated expenditure.

[2] This \$6.3 billion consists of \$4.17 billion of common costs and \$2.13 billion of attributable costs.

RECOMMENDATIONS:

As a precursor to the introduction of a mass-distance location-based charging system, the AFTS Review should consider whether there is a way, through the taxation system, to support those governments that do not receive an adequate return of registration revenues to enable the required investment to support current and future road usage.

The AFTS Review should consider how revenues from fuel excises can be better linked to road expenditure and usage.

3. Need to review motor vehicle taxes and concessions

There is also a range of taxes and concessions that are associated with the ownership and use of motor vehicles. The degree to which some of these taxes and concessions provide an incentive for greater travel may be in conflict with other broader government objectives such as those relating to the environment. They may also impact efficiency by encouraging more motor vehicle usage at the expense of public transport. For example, the fringe benefits tax concessions encourage excessive travel.

RECOMMENDATIONS:

Taxes and concessions that are associated with the ownership and use of motor vehicles should be reviewed in the context of economic efficiency and broader government objectives such as those relating to the environment.

Appendix: National Transport Policy Framework's vision, policy objectives and policy principles

Source: ATC 2008.

Vision for Australia's Transport Future

Australia requires a safe, secure, efficient, reliable and integrated national transport system that supports and enhances our nation's economic development and social and environmental well-being.

Transport Policy Objectives

To achieve this vision, Australia's Transport Ministers commit to the following policy objectives:

- **Economic**: To promote the efficient movement of people and goods in order to support sustainable economic development and prosperity.
- **Safety:** To provide a safe transport system that meets Australia's mobility, social and economic objectives with maximum safety for its user.
- **Social:** To promote social inclusion by connecting remote and disadvantaged communities and increasing accessibility to the transport network for all Australians.
- **Environmental:** Protect our environment and improve health by building and investing transport systems that minimise emissions and consumption of resources and energy.
- **Integration:** Promote effective and efficient integration and linkage of Australia's transport system with urban and regional planning at every level of government and with international transport systems.
- **Transparency:** Transparency in funding and charging to provide equitable access to the transport system, through clearly identified means where full cost recovery is not applied.

Transport Policy Principles

Australia's transport policy framework is underpinned by the following guiding principles:

- **Infrastructure pricing:** sending the appropriate signals to influence supply and demand for infrastructure;
- **Competitive markets:** establishing competitive markets wherever possible to minimise the need for regulation;
- **Private sector:** involve the private sector, where it is efficient to do so, in delivering outcomes;
- **National regulation:** a national perspective should be adopted where regulation is required;
- **National markets:** encourage national markets where possible; and
- **Customer:** Customer – focused. Equitable access for all users.