

---

## 3 Selected developments in assistance

This chapter documents a number of recent developments with ramifications for Australia's assistance structure generally or for particular sectors or industries. It covers selected areas where new assistance measures have been introduced or foreshadowed, or where there have been policy reviews or changes to existing arrangements, since the last edition of *Trade & Assistance Review*. The developments covered relate to:

- drought relief;
- industry-specific assistance — for sugar production, wheat marketing, tobacco growing, forestry, wine products, the automotive industry, venture capital, alternative fuels and energy projects;
- small business;
- regional adjustment support;
- selective investment incentives; and
- anti-dumping arrangements.

### 3.1 Drought relief

Drought is a natural phenomenon that frequently affects a wide range of agricultural activities. Its occurrence has economic, environmental, social and political impacts. Its effects on primary producers depend on their production systems and management decisions, as well as on any government support provided.

A major drought event commenced in Australia in 2002. Ongoing severe drought conditions were again reported in 2006-07 for several rural regions, with forecasts of significant downturns in agricultural production activity (ABARE 2006c). Previous major droughts were recorded during 1994-1995 and 1982-1983.

Australia's National Drought Policy (NDP), agreed to in 1992 and reaffirmed in 2005 by the Australian and state governments, recognises that drought is a natural feature of Australia's variable climate and needs to be managed accordingly. The key objectives of the NDP, which among other things embodies the principle of self-reliance, are summarised in box 3.1.

---

### Box 3.1 Objectives of the National Drought Policy

- Achieve self-reliance by farmers in managing the risks stemming from normal climatic variability by providing the focus on drought preparedness.
- Provide appropriate assistance to farmers experiencing “exceptional circumstances”.
- Ensure that the provision of this assistance is equitable, efficient and timely using [the] best science and information.
- Facilitate the maintenance and protection of Australia’s agricultural and environmental resource base during periods of increasing climatic stress.
- Facilitate the early recovery of agricultural and rural industries consistent with long-term sustainable levels.

Source: PIMC (2005).

The Commission reported on aspects of drought assistance in *Trade & Assistance Review 2004-05*. This section outlines the key drought support arrangements, provides updated estimates of the assistance provided, and describes recent policy reviews and developments in the area.

### Exceptional Circumstances drought relief

The Exceptional Circumstances (EC) arrangements are the Australian Government’s primary mechanism for assisting farmers affected by drought. There are two main strands: interest subsidies and income support (box 3.2).

Estimates of EC support to agricultural industries by the Australian and state governments are shown in table 3.1 (on page 3.4). The estimates indicate that, in total, Australian governments provided \$145 million of EC drought relief in 2002-03, rising to \$420 million in 2005-06. The latter figure is equivalent to about one-third of the assistance for primary producers included in the Commission’s assistance estimates for 2005-06. The main industries receiving drought support (in 2003-04) were *grain, sheep and beef cattle farming* (65 per cent) and *dairy cattle farming* (26 per cent).<sup>1</sup> Drought relief is concentrated in New South Wales, Queensland, Victoria and Western Australia.

---

<sup>1</sup> Information on the distribution of EC Interest Rate Subsidies by agricultural commodities was provided by state rural adjustment authorities. For EC Relief Payments, estimates of the industry distribution of the funding were derived from ABARE Farm Surveys which contain data on farm characteristics and drought funding for 2003-04 (ABARE 2005).

---

### Box 3.2      **Exceptional Circumstances support**

Under EC guidelines, a drought-affected region is declared eligible for EC support if the drought event is rare (a one-in-20–25 year event), results in a severe downturn in farm incomes over a prolonged period, and is not predictable or part of the process of structural adjustment (NRAC 2006, App 1). Once an area is 'EC declared', assistance is available to eligible producers, during the drought and recovery phase, through the following programs:

- *Business support.* EC Interest Rate Subsidies of up to \$300 000 per year are available to eligible farm enterprises over five years. EC Interest Rate Subsidies are funded jointly by the Australian Government (90 per cent) and state and territory governments (10 per cent).
- *Income support.* The EC Relief Payment provides eligible farmers a fortnightly payment at a rate equivalent to the Newstart Allowance, including additional benefits (such as a healthcare card). The Australian Government funds all income support payments.

In addition, interim income support payments are available during the EC application assessment process. Under the '*prima facie*' EC arrangements introduced in September 2002, the Australian Government may provide interim income support payments for up to six months for an area that is experiencing severe drought conditions while a full EC assessment is undertaken.

Eligibility to receive EC interest rate subsidies, EC Relief Payment and interim income support is subject to an off-farm asset test and income test. The asset test for EC interest rate subsidies allows off-farm assets of up to \$458 000, but does not take into account work activity and on-farm assets, such as proceeds from the forced disposal of livestock and Farm Management Deposits.

*Sources:* NRAC 2006, DAFF 2006a.

Analysis by the Australian Bureau of Agriculture and Resource Economics (ABARE) indicates that 50 per cent of interest subsidy recipients also receive income support. In relation to interest subsidies, ABARE (2006b, p. 6) observed that:

... the farms that receive the greatest assistance from [interest rate subsidies] are farms with the most debt ... Generally, farm businesses with the largest debt are also the largest farms, have the greatest capacity to service debt and have sound long term prospects. The profile of their farm debt indicates that the majority of their farm debt is for farm expansion, farm development and investment in new technology. Often they are also operated by younger farmers in the expansionary phase of their careers. Farms with low or no debt and relatively high levels of liquid assets receive much less assistance from the [interest rate subsidies].

For both types of EC support in 2004-05, ABARE data also indicate that recipient farms have a high capital value (\$2.1 million on average) and high equity in the farm assets (84 per cent). The estimated financial rates of return on the farm capital

(which include appreciation in the capital value of the farm) were higher for recipients of EC support (8.2 per cent) than for non-recipients (7.4 per cent).

Table 3.1 **Estimates of EC assistance<sup>a</sup>**  
\$ million

	2002-03	2003-04	2004-05	2005-06
<b>Australian Government</b>	<b>140.8</b>	<b>294.0</b>	<b>220.4</b>	<b>386.4</b>
– EC interest subsidy	39.7	92.5	99.2	232.5
– Interest rate subsidy – Drought Relief Package of 2002	3.3	6.7	2.3	–
– EC Relief Payment	45.9	153.4	117.1	153.4
– Interim Income Support	52.0	41.5	1.9	0.5
<b>State Government EC interest subsidy contribution<sup>b</sup></b>	<b>4.7</b>	<b>10.7</b>	<b>11.0</b>	<b>25.8</b>
<b>TOTAL<sup>c</sup></b>	<b>145.5</b>	<b>310.3</b>	<b>237.4</b>	<b>420.4</b>

na not available. <sup>a</sup> Actual expenditure. <sup>b</sup> Estimates exclude state governments' other drought programs, such as transport, freight and fodder subsidies. Funding estimates of those programs can be found in the *Trade & Assistance Review 2004-05*. <sup>c</sup> Sum of individual funding components may not add to total funding as the total amount includes program administration costs (except for 2002-03).

Sources: NRAC (various) and data provided by DAFF.

## Agriculture-wide programs and drought preparedness

Australian governments have also introduced a range of agriculture-wide programs to directly encourage rural adjustment and improve drought preparedness. Since 1997, the *Agriculture-Advancing Australia* (AAA) package has provided assistance measures covering farm business management, education and training, income support and land use planning. For example, the AAA Farm Help program supports farming families in financial difficulty and facilitates farming exits and reestablishment.

An important support measure included in the AAA package is the Farm Management Deposits (FMD) Scheme, which provides taxation benefits designed to assist farmers to handle income variability and reduce reliance on government support in times of drought (AFPRG 2006). Eligible primary producers can claim a tax deduction equivalent to the deposits made to FMDs of up to \$300 000. The deposits are not assessable as income for tax purposes until they are withdrawn. However, for farms in EC declared areas, the deposits can be withdrawn within 12 months without losing the taxation deduction previously claimed.<sup>2</sup>

<sup>2</sup> Normally, FMD deposits must be held for at least 12 months for the tax benefits to be realised.

---

A recent review of the FMD Scheme (DAFF 2006c) identified several reasons why farmers participate in the scheme. In addition to the immediate taxation benefits, the review noted that ‘placing funds in FMDs provides farmers an option to later find a tax deduction to offset quarantined income’ (such as when the withdrawals are used as working capital, which are themselves tax deductible expenses). It also observed that ‘there is a distinct annual pattern of large net FMDs deposits in June, and net withdrawals in July, which may suggest that FMDs are used primarily as a tax planning instrument’.<sup>3</sup> Other benefits include earning market rates of interest on otherwise taxed income and the ability to “leverage up the effects of EC interest subsidies” (DAFF 2006c, p. 4).

The FMD Scheme has provided significant support over the current drought period. The tax revenue forgone under the scheme was \$410 million in 2002-03, \$245 million in 2003-04, \$95 million in 2004-05 and \$115 million in 2005-06 (Treasury 2006).

## Recent developments

In March 2005, the Australian Government Minister for Agriculture, Fisheries and Forestry commissioned the Agriculture and Food Policy Reference Group (chair: Peter Corish — former President of the National Farmers Federation) to assess policies and assistance programs affecting the agriculture and food sector.

In its report released in February 2006, the Reference Group found that EC interest rate subsidies and transaction subsidies do not lead to improved management skills and do not encourage self-reliance, and there are risks that such assistance may influence the amount of debt some farming businesses carry. According to the Reference Group, one-off programs such as EC support are likely to work against the intention of agriculture-wide programs that directly target drought preparedness and rural adjustment. In relation to the FMD Scheme, the Reference Group observed:

The FMD Scheme was developed to help reduce dependence on government support, particularly exceptional circumstance type assistance ... [It] is important that FMDs function as intended, with minimal potential to be used for other purposes, such as pure tax deferral (AFPRG 2006, pp. 177-8).

The Reference Group recommended that the Government and the agriculture sector cooperate to achieve self-reliance by:

- introducing a consistent approach to government assistance for those facing viability problems or wishing to lift their business performance;

---

<sup>3</sup> For example, FMD statistics (DAFF 2006d) indicate that (net) deposits of \$552 million were made in the quarter ending June 2005. These deposits were followed by (net) withdrawals of \$336 million in the quarter ending September 2005.

- 
- retaining the FMD scheme as a key risk management tool, informed by analysis to confirm that it is meeting its objectives; and
  - introducing new and improved measures to develop better farm preparedness (including risk management strategies) to deal with market fluctuations and climatic extremes, while phasing out interest rate and other transaction based subsidies by the end of 2010 (AFPRG 2006, p. 189).

The Reference Group also proposed that the Government continue income support payments for drought, coupled with the provision of professional advice to facilitate adjustment.

In April 2006, ABARE (2006b) released a study on drought preparation practices in the rural sector. The study is based on an analysis of farm data before, during and after the drought of 2002-03, along with a survey of farm managers' attitudes on approaches to managing drought. Among other things, the study found that:

- A number of drought preparation strategies have been used widely in the past and are likely to continue to be used widely in the future ...
- With the benefit of hindsight, the majority of farm managers in drought affected regions and industries believed that they were reasonably well prepared for the recent drought. However, a significant minority of farm managers believed that they were underprepared for drought ...
- Government assistance to the farm sector in response to past and current droughts is likely to have reduced the riskiness of farming, and reduced the incentive for individual farm managers to prepare for severe climatic events (pp. 1-4).

In October 2006, the Australian Government released its response to the recommendations of the (Corish) Reference Group (DAFF 2006b). The Government "noted" the recommendations on drought support, and said that further evaluation of the AAA package was being undertaken.

Subsequently, the Department of Agriculture, Fisheries and Forestry (DAFF 2006c) released its review (mentioned earlier) on the operation of the FMD Scheme. Among other things, the review recommended that the Government reconsider the exemption of FMDs in determining eligibility for DAFF programs such as EC support, and consider raising the maximum deposits on which the tax benefits will apply, from \$300 000 to \$365 000. It also recommended that further analysis of the scheme be undertaken when climatic conditions improve.

---

In October 2006, the Australian Government announced several measures to extend EC business and income support (Howard 2006c and McGauran 2006a). Under the new assistance package:

- Total support has been increased, with around \$900 million in funding available over two years, whereas previously \$1.2 billion was allocated over five years.
- Existing EC declarations which had been due to expire in 2006 have been extended until 2008, and EC declarations which had already ceased have been reintroduced.
- All producers within an EC region are to be eligible for support, whereas previously only certain industries and producers would qualify.
- The maximum EC interest rate subsidy per farm has been increased from \$300 000 to \$500 000 over five years. Eligibility conditions have also been relaxed by the removal of the requirement that farm businesses have not received support in two out of the past five years.
- Eligible farmers can receive grants of up to \$5000 for professional business and financial planning advice.

The eligibility conditions for depositing funds into the FMD scheme have also been relaxed. The maximum deposit to which eligible producers can gain an income tax deduction under the FMD Scheme has been increased from \$300 000 to \$400 000. In addition, the amount of income which farmers can earn from non-farm activities and still be eligible for FMD tax deductions has been increased from \$50 000 to \$65 000 per annum.

In November 2006, the Government announced more than \$200 million in funding for new drought support measures for small businesses in EC declared areas (Howard 2006d). Under this arrangement, both income support and interest rate subsidies are available to eligible small businesses until March 2008. To be eligible, small businesses must employ up to 20 people and derive at least 70 per cent of their income directly from agriculture.

The Australian and state primary industries ministers met at the Primary Industries Ministerial Council in November 2006. Among other things, the Council considered longer-term options recommended by the Reference Group's report to improve farmers' drought preparedness and to achieve more consistent drought declaration processes. The Council communiqué responded that:

... in recognising the current situation facing farmers and rural communities, Council agreed that longer-term options for improving drought preparedness should be considered further at a more appropriate time (PIMC 2006).

---

In February 2007, the Government announced that it will extend EC interest subsidies and income support to agricultural-dependent small businesses, such as agricultural machinery and equipment retailers. The EC eligibility criteria are to be widened to cover businesses employing up to 100 staff. To be eligible, at least 70 per cent of their business income must be derived directly from the provision of goods and services for farming activities in EC declared areas (McGauran 2007).

## 3.2 Industry-specific assistance

### Sugar

The Australian sugar industry, which is centred mainly in Queensland, has been subject to a range of reforms and assistance packages since the mid 1990s. In recent times, key assistance arrangements have included the Sugar Industry Reform Program (SIRP), announced in 2002, and a subsequent broader measure, the Sugar Industry Reform Program 2004. These and other arrangements were discussed in *Trade & Assistance Review 2004-05*.

SIRP 2002 originally entailed funding of \$120 million in assistance. However, in April 2004, those elements of SIRP 2002 which had not been completed were incorporated with SIRP 2004. Expenditure to date under both programs is over \$311 million.

While the majority of funding for the two packages came from consolidated revenue, the initiatives have been partly funded by a levy of 3 cents per kilogram applied to all sales of domestic and imported sugar in the retail, food preparation and manufacturing sectors. The sugar levy operated to transfer payments to sugar producers through the higher sugar input prices on food manufacturing and beverage industries.<sup>4</sup>

As at 31 January 2007, the sugar levy had raised approximately \$84 million. It had been due to expire on 31 December 2007 but, following consultation with the manufacturing activities affected by the arrangement, the Australian Government abolished the sugar levy in November 2006 (McGauran and Costello 2006). It is estimated that the levy's early termination will have reduced costs for businesses and consumers of sugar by around \$28 million (in 2006-07 and 2007-08).

---

<sup>4</sup> An exemption from the levy was available on all sugar that was produced for export and a rebate system was available for any levy paid on sugar that was ultimately exported as a component of manufactured food.

---

## Wheat marketing

The *Wheat Marketing Act 1989* (the Act) provided for the deregulation of the domestic wheat market. On the export market, amendments to the Act in 1997 and 1998 modified the existing ‘single desk’ arrangement. They effectively provided AWB International (AWBI) with the sole right to export bulk wheat from Australia — under the amendments, AWBI was permitted to exercise a statutory power to block applications by competing traders to export bulk wheat sales (the “veto power”).<sup>5</sup> AWBI is a subsidiary of the AWB Limited, which was created as a grower-owned and controlled company that has operated as a commercial company since its public listing in August 2001. AWB Limited manages a national wheat pool for AWBI.

Although the primary rationale for having the single desk is to attain higher prices for wheat exports and maximise returns to growers, the assistance implications of the arrangements are unclear. While Australian wheat exports tend to attract relatively high prices, these may be largely explained by factors independent of the single desk, such as quality and additional services provided to buyers. In the past, the Commission (2000a, p. 2) has found that any genuine price premiums that might exist are likely to be confined to a limited number of markets and probably be quite small. At the same time, the Commission considered that the single desk was likely to become costly for some exporters, particularly those supplying new or specialised varieties, and create inefficiencies by discouraging innovation and takeup of specialist services. Indeed, it is possible that the arrangements could provide negative net assistance to the wheat growing industry, disadvantage other grain traders and be an impediment to higher export sales.

In its *Review of the National Competition Policy Reforms* (PC 2005), the Commission noted further evidence that introducing competition into wheat marketing could generate benefits for Australia, and recommended that an independent and transparent review into the future of wheat marketing arrangements be undertaken as soon as practicable.

In December 2006, the Government announced a temporary arrangement to facilitate alternative marketing of export wheat sales following the Cole Commission’s *Report of the Inquiry into certain Australian companies in relation to*

---

<sup>5</sup> Although the Act established the Wheat Export Authority to control the export of wheat, sections 57(3A) and 57(3B) of the Act provide that the Authority must receive written approval from AWBI in order to grant applications by other exporters to market bulk wheat. In relation to non-bulk shipments, other companies can receive approval from the Authority to export wheat in bags and containers without AWBI consent (although the Authority is required to consult AWBI on such applications).

---

*the UN Oil-for-Food Programme*, released in November 2006. The temporary arrangement transfers the veto power on wheat exports from AWBI to the Minister for Agriculture, Fisheries and Forestry (McGauran 2006c, 2006d). The Government subsequently assessed applications from entities seeking to export wheat. Of 46 applications submitted, only two export permits were issued for 800 000 tonnes of wheat, with the bulk of export sales for the 2006-07 harvest continuing to be marketed by AWBI through the national pool. This temporary measure operates until 30 June 2007.

Under the temporary export permits, eligible wheat marketing companies are required to contribute a payment of \$4 per tonne to the national pool for each tonne of wheat exported, up to the total of 800 000 tonnes.

In January 2007, the Australian Government announced the creation of a Committee to consult with the Australian wheat industry, particularly growers, to report on their views on future wheat marketing by 30 March 2007.

## **Tobacco growing**

In recent years, the tobacco growing industry, centred in Mareeba (Queensland) and Myrtleford (Victoria), has faced significant adjustment pressures from deregulation and the decision of tobacco manufacturers to scale back their purchases of Australian tobacco leaf.

At the same time, tobacco products have been subject to high excise taxes. In a 2006 report on the Administration of Petroleum and Tobacco Excise, the Australian National Audit Office (ANAO) found a significant diversion of tobacco products into an illegal trade market. The ANAO (2006, p. 27) commented:

Illegal tobacco is tobacco that is grown and manufactured in Australia, and sold illegally to others, without excise being paid. Tobacco growers receive approximately \$700 per 1000 kilogram bale, while the excise and GST levied on the same bale is approximately \$30 000. This price disparity creates strong incentives to sell tobacco illegally. Anecdotal evidence suggests that growers may receive up to \$10 000 per 1000 kilogram bale on the black market.

Producer licenses were cancelled following the withdrawal of major tobacco manufacturers as buyers of Australian grown tobacco. The excise licences of tobacco growers in Northern Queensland were cancelled by the Australian Taxation Office in February 2004, and tobacco growers in Victoria and southern Queensland had their licences cancelled in October 2006, when the manufacturers ceased purchases from these regions.

---

In October 2006, the Australian Government announced a funding package to assist tobacco growers to restructure and move into alternative business activities. As of February 2007, the package comprises funding of \$45.9 million. Former tobacco growers in Northern Queensland are to be eligible for up to \$23.2 million, with those in Victoria and Southern Queensland eligible for up to \$21.8 million and \$900 000, respectively. The maximum grant will be \$150 000 per grower (McGauran 2006b).

## **Forest industries**

Native forests accounted for 163 million hectares (21 per cent) of Australia's land area in 2003 (BRS 2007). Of this, the vast majority is publicly-owned forests held for environmental conservation, managed for multiple uses including timber production, or are in the form of pastoral leases.

In addition, there are 1.7 million hectares of plantation forestry, comprising both softwood and hardwood species.

Together, native forests and plantations play an important role in the provision of wood products in Australia. The logs are used to make sawn timber, fibreboard, particleboard, plywood, paper and other products.

In recent times, the share of private ownership of plantations has increased, from 30 per cent in 1990 to over 57 per cent in 2005. The private plantation sector comprises plantations financed by managed investment schemes, timber producing companies, superannuation funds, farm foresters and other private owners. In 2005, most of the area given to new private plantations (92 per cent) was financed by managed investment schemes (MIS) (BRS 2006).

Historically, the principal assistance mechanism for forestry was in the form of the Softwood Forestry Agreements, in which the Australian Government made loans on favourable terms to the States to establish and maintain softwood plantations. The softwood loans contributed to the increase in plantations during the 1960s and 1970s, and subsequently became the basis for much of Australia's wood processing industry. In more recent times, forest-based industries also received support for restructuring in response to changes in the availability of forest resources — for example, through the Forest Industry Structural Adjustment Program (funding for which expired on 30 June 2006).

---

### *Tasmanian Forest Community Agreement*

Since 1992, provisions have been in place for the establishment of Regional Forest Agreements (RFA) to manage the uses of forest resources and to provide certainty for private investment. Under RFAs, the Australian and state governments establish native forest conservation reserves and provide industry access to forest resources in designated locations outside the reserve area.

In May 2005, the Australian and Tasmanian Government announced a joint funding package for the implementation of the Tasmanian Forest Community Agreement (Howard 2005a). Among other things, the agreement reserves over 170 000 hectares of forests on public and private land for environmental conservation. Additional measures include an end to the conversion of native forest to plantations on public land by 2010 and the phasing out of the clearing of native forest on private land over ten years. Measures to support the forest-based industries under the agreement include:

- *Intensive Forest Management Program* — \$115 million allocated by the Australian and Tasmanian Governments to fund the establishment of additional plantations and to improve productivity (through pruning, thinning and fertilising) in existing plantations and native forests. The measure is intended to ensure the long term supply of sawlogs and veneer logs.
- *Hardwood Timber Industry* — \$46 million of Australian Government funding to support the Tasmanian hardwood timber industry, including country sawmills.
- *Tasmanian Softwood Industry Development Program* — \$10 million of Australian Government funding to assist the Tasmanian softwood industry to establish a facility for preserving pine and to phase out the use of copper chrome arsenate.
- *Special Species and Honey Producers* — \$11 million of Tasmanian Government funding to support “special species” timber and the leatherwood honey industry.
- *Training and skills development* — \$4 million to support training and skills development of workers in the Tasmanian forest-based industries (Howard and Lennon 2005).

### *Plantation forestry tax concessions*

Prior to 1988, the general deduction provision of the income tax law (now ITAA 97 section 8-1) allowed taxpayers (including individual plantation forestry investors) to deduct all eligible prepayments on investments in the year of expenditure. In 1988, a 13 month prepayment rule was introduced to allow immediate deduction for expenditures that are incurred for services rendered within 13 months.

---

The 13-month pre-payment rule was reviewed by the (Ralph) Review of Business Taxation in 1999. Consistent with the Review's recommendations, in November 1999 the Australian Government announced the removal of the scheme with phasing-in arrangements to apply until September 2002.

In October 2001, the Australian Government announced revised concessional tax arrangements for plantation forestry (Kemp 2001).

- Under a new 12-month prepayment rule, investors in MIS schemes became eligible for an immediate deduction for the expenditures on the establishment of plantations, including those incurred from ripping and mounding, weed and pest control, and planting and fertilising.<sup>6</sup>
- In addition, under the “non-commercial losses” provisions, the Commissioner of Taxation was given the discretion to determine that investments in plantation forestry are a “business activity” and allow a loss generated from the tax deduction to be offset against any form of income. This concession was also available to non-forestry agricultural activities, including horticulture. The Government said:

This change is of particular benefit for the forestry industry, as well as other business activities, as it allows the discretion to be exercised for loss years after one-off profits have been earned from thinning operations (Kemp 2001).

The 12-month pre-payment rule provided favourable taxation benefits to plantation forestry relative to other investment classes, in which deductions can only be claimed in the year the services are rendered and income is earned. According to estimates in the Tax Expenditure Statement (Treasury 2006), the prepayment rule had a budgetary cost (in tax revenue forgone terms) of \$40 million in 2005-06. The non-commercial loss provision associated with forestry plantations and non-forestry agricultural activities has not been costed.

The forestry tax concessions have been the subject of some debate recently. In particular, the farming sector has expressed concern about the impact of the concessions on competing farm activities and land prices. For example, the National Farmers Federation (2006) has argued that MIS are driven by taxation manipulation rather than the commercial reality of the agricultural industries involved, and that the schemes have been enabled to bid from a position of relative advantage in terms of their access to capital, and have resulted in an over-supply of certain commodities. MIS forestry industry participants have disputed the nature of the concessional tax arrangements and their precise impacts on rural activities.

---

<sup>6</sup> This contrasts with general investment classes such as shares and buildings, where the purchase price of the investment cannot be claimed for an immediate tax deduction due to the capital nature of the expenditures.

---

In May 2005, the Australian Government announced that it would extend the 12 month pre-payment rule until 30 June 2008. The extension was to allow a review into support for the plantation timber industry, including:

- the commercial viability and current tax treatment of plantation investment;
- whether the operation of the *Income Tax Assessment Acts* impedes investment in longer term forest rotations which produce higher value products;
- the role of state and territory governments in plantation industry development, as investors, growers and land managers, and any implications this has for competitive neutrality with regard to tax liabilities and incentives;
- the capacity to adapt existing tax policies to contribute to achieving the Australian and state governments' desire to achieve greater integration of plantation and natural resources management policies to improve the management of salinity and water quality; and
- the relative roles and effectiveness of the tax system and expenditure programs in the delivery of assistance to industry (Brough and Macdonald 2005a, 2005b).

Detailed findings of the Review of Plantation Forestry, which was conducted by the Departments of Agriculture, Fisheries and Forestry, the Treasury, and Prime Minister and Cabinet on the above terms of reference, have not been released publicly.

However, following consultations on proposals released by the Government in May 2006, the Government announced in December 2006 that it will retain the tax deduction for forestry.

- From 1 July 2007, eligible investors in forestry MIS will be entitled to a specific statutory deduction for their expenditure. Investors will be entitled to immediate upfront deductibility for all expenditure provided that, among other things, at least 70 per cent of the expenditure is directly related to developing forestry — including the costs of planting, tending and harvesting of trees incurred at any time over the life of the investment, and the rental costs or lease payments for land.
- Investors in forestry MIS are no longer required to demonstrate that they are 'carrying on a business' in order to claim the tax deduction (Dutton and Abetz 2006).

In February 2007, the Government announced that, under a reinterpretation of the income tax law to be made by the ATO, investors in forestry and non-forestry agribusiness MIS will no longer be allowed upfront deductions from the MIS on the basis that the investor is 'carrying on a business'. The Government also announced that it would not be introducing taxation arrangements for non-forestry MIS similar to those that it had previously announced in relation to forestry MIS (Dutton 2007a).

---

In March 2007, following consultations with the agribusiness industry, the ATO announced that it will provide a transitional period for its reinterpretation of the tax treatment of non-forestry MIS. The transitional period is to ‘give industry time to adjust their financial arrangements accordingly’, and will apply to MIS arrangements entered into from 1 July 2008. The ATO also announced that, after 30 June 2008, it will not issue new product rulings for agribusiness MIS to be eligible for the tax deduction (ATO 2007a).

In April 2007, the ATO issued a draft ruling which outlines its reinterpretation of the income tax treatment of non-forestry MIS. The ATO concluded that investor contributions to MIS are capital expenditure in nature and are therefore not deductible under general income tax provisions. Accordingly, it will seek to expedite the application of the revised tax treatment through a test case in the courts (ATO 2007b).

Subject to any revisions by the courts, the upshot of these changes is that the previously favourable tax treatment for MISs will be available only for investments in forestry — not for investment in non-forestry activities, such as horticulture.

## **Wine products**

The taxation of alcohol products is designed primarily to raise revenue and to help address the health impacts of alcohol consumption. Prior to July 2000, the wholesale sales tax applied on wine products at a rate of 41 per cent, which was higher than the wholesale tax rate applying to most other, non-alcoholic products. As part of the tax reform package of 2000, the wholesale sales tax was replaced by a goods and services tax (GST) and a wine equalisation tax (WET) was introduced. The WET is levied at an ad valorem rate of 29 per cent on the wholesale value of wine sales (before GST) including on grape wine, grape wine products, fruit and vegetable wines, cider, mead and sake. The WET rate was set to ensure that, after the replacement of the wholesale sales tax with a GST levied at 10 per cent, there would be no significant changes to the price of various wine products due to the tax changes.

In the May 2004 Budget, the Australian Government announced the WET rebate scheme, under which wine producers are eligible for a refund of the WET of up to \$290 000 per year. The measure exempted \$1 million of each producer’s domestic wholesale wine sales from the WET on an annual basis. The new rebate replaced the accelerated depreciation provisions for grapevine plantings and the previous Australian and State Government cellar door rebate scheme (which provided a rebate of up to \$42 000 per year).

---

In July 2005, the Australian Government agreed to allow New Zealand producers exporting wine into Australia to claim the WET rebate without the need to be registered for GST purposes. The measure was in response to a concern raised by the New Zealand Government that the rebate arrangements breached the Australian and New Zealand Closer Economic Relations Trade Agreement.

In June 2006, the Australian Government announced that it will provide additional support to small-and medium-sized wine producers through increases in the WET producer rebate scheme (Costello 2006). On 1 July 2006, the maximum WET producer rebate was increased from \$290 000 to \$500 000 per year. The new measure effectively exempts \$1.7 million of each producer's (or group of producers') domestic wholesale wine sales from WET (compared to the previous level of \$1 million). The wine producer rebate is estimated to cost \$125 million in 2006-07 (Treasury 2006).

## **Automotive**

Although assistance to both motor vehicle producers and component suppliers has declined significantly since the mid-1980s, the automotive industry remains one of the most highly assisted manufacturing industries. This assistance derives largely from long-standing tariffs and tariff concession schemes, particularly the Automotive Competitiveness and Investment Scheme (ACIS):

- Under legislated tariff reforms, automotive tariffs were reduced from 15 to 10 per cent in 2005, but are to remain at 10 per cent until 2010, when they will be reduced to 5 per cent and remain at that level until 2015.<sup>7</sup>
- Automotive producers are eligible for ACIS transferable duty credits based on their domestic production, investment and research and development activities. The credits can be used to reduce the customs duty payable on eligible imports. The amount of ACIS duty credits for the current five year period (2006-2010) comprises a capped allocation of \$2 billion, with an additional allocation that is uncapped and not directly specified.
- Assistance to automotive producers is also available from other sources, including government procurement programs and the luxury car tax that applies mainly to imported vehicles. A specific tariff of \$12 000 also applies on imports of used (second hand) vehicles.

---

<sup>7</sup> In its response to the Productivity Commission's report on Automotive Assistance (PC 2002a), the Government announced that the Commission will undertake a further inquiry in 2008 to determine whether changes are warranted to the legislated tariff reductions in view of conditions in the international trade environment (Costello 2002).

---

In addition to formal tariff and ACIS assistance arrangements, ad hoc assistance to automotive producers is also substantial. This assistance often involves project or firm-specific support by both the Australian and the relevant state government.

For example, as noted in last year's *Review*, in May 2004 the Australian Government announced a \$50 million structural adjustment package in response to the foreshadowed closure of Mitsubishi's engine plant in Lonsdale, South Australia. The package comprised a labour market assistance program of up to \$10 million for displaced Mitsubishi workers, and investment facilitation and structural adjustment measures of up to \$40 million for South Australia. This support is in addition to funding by the South Australian Government for a workplace assistance package to assist Mitsubishi workers and a \$5 million industry development rescue package for the southern suburbs of Adelaide, where the plant is located (Rann 2004). The Australian Government also estimated that, at the then production levels, Mitsubishi could expect to receive around \$300 million in assistance from the Government's extension of ACIS beyond 2006 (Macfarlane 2004).

In May 2006, the Australian Government announced that it would provide an assistance package of \$52 million to Ford Australia to support two new projects. \$40 million is to fund the design, engineering and manufacture of the next generation of Ford Falcon and Territory vehicles in Victoria. An additional \$12.5 million will be used to fund the design and engineering of a Ford light commercial vehicle, with the manufacturing activities to be undertaken abroad. According to the Government:

These projects will secure Ford's manufacturing operations in Australia over the longer term ...

The Australian Government's assistance is conditional on Ford undertaking to provide the Australian automotive component sector with every fair and reasonable opportunity to supply the necessary components for these projects (Howard 2006a).

In addition, the Ford projects are to receive assistance from the Victorian Government, although the details of this have not been publicly disclosed.

In October 2006, the Australian Government announced that it will provide \$6.7 million over four years to General Motors Holden. The funding is earmarked for the introduction of safety and fuel management improvements and for reducing greenhouse gas emissions on Commodore vehicles. Eligible activities include research and development, as well as training to allow re-engineering on selected models. The South Australian and Victorian Governments will also provide \$6.7 million in funding to this project (Macfarlane 2006c).

---

In December 2006, the Australian Government announced the Supplier Capability Development Program, which is to be formed as a component of ACIS with funding of \$7 million from January 2007 to July 2008. Under the program, local car makers can apply for funding to enhance the capabilities of their components suppliers (MacFarlane 2006d). A steering committee, which comprises representatives from motor vehicle industry associations and the Department of Industry, Tourism and Resources, will manage the program (FAPM 2007).

## **Venture capital**

Venture capital is “high risk capital directed towards new or young businesses with prospects of rapid growth and high rates of return” (ABS 2005). A venture capital firm generally invests capital and also provides management skills to enterprises with commercial prospects, and derives returns usually in the form of a capital gain when it sells its stake in the enterprises. Alternatives to venture capital include business ‘angel’ investment<sup>8</sup> and self-financing. Venture capital firms form part of the broader private equity sector.

Venture capital activities have experienced significant growth over time. Between June 2000 and June 2006, the number of venture capital (and private equity<sup>9</sup>) funds and their aggregate investment assets increased by 80 and 124 per cent, respectively. As at June 2006, there were 229 funds, with \$6.3 billion in assets (ABS 2007).

A significant proportion of Australian venture capital and private equity firms are eligible for assistance under various government programs (table 3.2). As of June 2006, eligible firms have drawn on a total of \$386 million in funding from government sources.

The first government program introduced to encourage the development of venture capital in Australia was the Management and Investment Companies program, established in 1984. This was replaced by the Pooled Development Funds program, announced in 1992. In a series of industry policy statements since 1997, the Australian

---

<sup>8</sup> The term refers to individuals who provide capital for a business start-up, but who, unlike venture capitalists, typically do not manage the pooled money of others in a professionally-managed fund.

<sup>9</sup> Information on venture capital activities is available from an ABS survey on the use by venture capital and private equity firms of government programs (ABS 2007). The ABS survey does not differentiate between venture capital and private equity firms.

**Table 3.2 Venture capital and private equity firms eligible for government programs**

	<i>June 2000</i>	<i>June 2006</i>
VC&PE funds eligible for government support <sup>a</sup>		
– Number of funds	55	120
– Assets (\$ million)	660	2 174
VC&PE funds not receiving government support		
– Number of funds	72	109
– Assets (\$ million)	2 130	4 175
<i>Government funding as a source of funds in VC&amp;PE firms</i>		
Amount drawn down from government (\$ million) <sup>b</sup>	60	386
Unused funds (\$ million) <sup>b</sup>	61	380
Total funding committed by governments (\$ million) <sup>b</sup>	120	766

<sup>a</sup> Includes the Pooled Development Funds; the Innovation Investment Funds; Preseed Fund; Venture Capital Limited Partnerships; and the Information and Communications Technology Incubator Program. <sup>b</sup> The funding committed to venture capital and private equity firms is measured on a cumulative basis.

Source: ABS (2007), tables 1 and 10.

Government has introduced additional measures to encourage venture capital, as well as making modifications to existing programs. These programs include:

- the Innovation Investment Fund (IIF);
- the Commercialising Emerging Technologies (COMET) program;
- the Preseed Fund; and
- Venture Capital Limited Partnerships (VCLPs).

The Commission has reported on these programs in previous editions of *Trade & Assistance Review* (see PC 1999, 2000c, 2001b).

In May 2005, the Australian Government announced a review of the Australian venture capital industry. Among other things, the review's terms of reference covered "the appropriateness, efficiency and effectiveness" of existing government support for venture capital and early-stage private equity investment (Macfarlane 2005).

In the 2006-07 budget, the Australian Government announced changes to venture capital programs. Although the venture capital review report has not been publicly released, the Government noted that the proposed changes are in response to the recommendations of the review (Macfarlane 2006b; Costello 2007). In March 2007, the *Tax Laws Amendment (2007 Measures No. 2) Bill 2007* was introduced in parliament to implement the announced initiatives (Dutton 2007b; Macfarlane 2007b). The changes are outlined below.

---

## *Innovation Investment Fund*

The IIF program, which was established in 1997, provides funds to eligible venture capital firms to invest in small companies that are seeking to commercialise their technologies. The policy objectives of the IIF program are:

- to develop fund managers with experience in the early stage venture capital industry;
- by addressing capital and management constraints, to encourage the development of new companies which are commercialising research and development;
- to establish in the medium term a “revolving” or self funding scheme; and
- to develop a self-sustaining Australian early stage, venture capital industry (AusIndustry 2006a).

The IIF program affords assistance to venture capital companies in the form of an investment incentive. Until recently, the Government provided up to \$2 for every \$1 of private investment (66 per cent of the total investment). If and when a fund makes a return, the Government and the private investors receive a repayment of the capital plus interest. In relation to any additional profit from the investment, the Government receives a share of 10 per cent, whereas private investors receive a 72 per cent share, and an 18 per cent share goes to fund managers, effectively allocating the upside of the investment returns to the private sector.<sup>10</sup>

In 2002, the ANAO undertook an audit of the administration and governance of the IIF program. The ANAO (2002) found that:

Implementation of the IIF program has involved challenging and unique issues of public administration, including those arising from investment by the Commonwealth in a market traditionally regarded as high risk and the Commonwealth having dual roles of program administrator and investor. The ANAO concluded that overall management of the program is largely effective, although there are areas that warrant improvement. As well, there has been considerable development in the early stage venture capital market since the initiation of the IIF program, consistent with the program’s objectives (p. 13).

The ANAO made a number of recommendations on risk management and program delivery, which were agreed to by the Department of Industry, Tourism and Resources and the Industry Research and Development Board.

In the 2006-07 budget, the Australian Government announced a third-round of the IIF program, with funding of up to \$200 million. The revised IIF program will

---

<sup>10</sup> In March 2000, the Government announced a ‘revolving fund’ for the IIF program (Minchin 2000). Under this arrangement, if and when fund managers realise a return from their investment, the funding initially injected into the venture capital funds, plus interest, would be redistributed to the IIF program, instead of being returned to the Consolidated Revenue Fund.

---

provide funding to venture capital firms on a 1:1 matching basis between private and public funding. Each eligible fund will receive up to a maximum of \$20 million to be invested over a ten-year period. Eligible investments include companies in the 'seed', 'start-up' or 'early expansion stages' that are seeking to commercialise their technologies (AusIndustry 2006a).

### *Early stage venture capital limited partnerships (ESVCLP)*

Announced in the 2006-07 budget, the ESVCLP scheme is to replace the Pooled Development Fund program. Under the new arrangement, venture capital firms that qualify for ESVCLP status are eligible for a tax exemption on both income and capital gains realised in the sale of their investments. The tax exemption is provided under a 'flow-through tax treatment', in which an ESVCLP is taxed as an ordinary partnership rather than a corporate limited partnership. The tax exemption will be available to both domestic and foreign investors in the eligible funds (Costello 2007). The Regulation Impact Statement accompanying the *Tax Laws Amendment (2007 Measures No. 2) Bill 2007* said:

Investors in ESVCLPs will benefit from higher returns on investments as returns will be fully tax-exempt. The ESVCLP investment vehicle replaces the PDF which was subject to tax (at concessional rates) although investors were exempt from tax (Costello 2007, p. 93).

Eligibility for the tax exemption is limited to venture capital firms registering as an ESVCLP using the limited partnership structure. To qualify, the ESVCLP will have a maximum fund size of \$100 million and total assets of investee companies of not more than \$50 million immediately prior to investment. The ESVCLP must also divest itself of any holdings once the total assets of the investee company exceed \$250 million. There are also other conditions, including on the mode of investment by ESVCLPs. A provision will also disallow investors from deducting investment losses, on the basis that their income will already be exempt from tax (Costello 2007).

The tax revenue forgone under the ESVCLP measure from 2008-09 to 2010-11 is expected to be \$25 million (Costello 2007).

### *Venture Capital Limited Partnerships (VCLP)*

The VCLP regime was introduced in 2002 to provide concessional tax treatment to venture capital firms registered as a VCLP vehicle. A tax exemption is available to

---

VCLP foreign investors from certain countries on the profits and gains made from equity investments in Australian companies that have assets of \$250 million or less.

The *Tax Laws Amendment (2007 Measures No. 2) Bill 2007* introduced several measures to relax the eligibility requirements for foreign investors to access the VCLP tax concession. Among other things, eligible venture capital firms will be allowed to invest in unit trusts as well as companies, and invest (up to 20 per cent of committed capital) in similar foreign resident entities. The relaxed requirements for VCLPs will also apply to ESVCLPs.

## **Alternative fuels**

During 2005 and 2006, the prices of standard fuels such as oil and petroleum products increased significantly. In response, the Australian Government announced several programs to promote the supply and distribution of alternative fuels, including ethanol and liquid petroleum gas (LPG). These policies are in addition to existing assistance arrangements affecting the supply and distribution of alternative fuels. Previous developments in this area were discussed in *Trade & Assistance Review 2002-03*.

### *Ethanol*

Ethanol is produced from the fermentation of feedstocks such as sugar or grain materials and is blended into petrol for use as a fuel or used in industrial applications. The economic viability of domestic ethanol production depends on many factors, of which key elements are its production costs, competition from imported ethanol and the price of petrol. Ethanol is a class of 'biofuels' that also include biodiesels and diesohols.<sup>11</sup>

The domestic production and distribution of ethanol has received significant government support, particularly since the Government's announcement in 2001 of a target of at least 350 million litres of biofuels in the domestic fuel supply by 2010 (box 3.2).

---

<sup>11</sup> Biodiesel is typically produced from a reaction of vegetable oil or animal fat with an alcohol. Biodiesel feedstock can include canola oil, soyabean oil, sunflower oil, tallow and used cooking oils and fats.

---

### Box 3.3 Assistance arrangements for ethanol

- Historically, fuel ethanol received favourable treatment compared to other fuels by not being subject to fuel excise (prior to September 2002). From July 1994 to 1997, the development of the fuel ethanol industry also received support via the Ethanol Production Bounty scheme.
- A general tariff has also been applied on imported ethanol used as fuel in an internal combustion engine. Similar tariffs do not apply to imported petrol or other alternative fuels such as biodiesel.
- In 2001, the Australian Government set an objective that ethanol and other biofuels would contribute at least 350 million litres to the total fuel supply by 2010.
- In September 2002, a production subsidy was introduced for ethanol produced domestically. At the same time, an excise tax (of 38.142 cents per litre) was applied to both domestically-produced and imported ethanol. The subsidy fully offsets the excise on domestic ethanol. The effect of these arrangements was equivalent to levying an additional tariff on imported ethanol (of 38.142 cents per litre).
- In May 2003, the Australian Government announced as part of a package of fuel tax reforms that it would extend the existing production subsidy and excise arrangements on ethanol to 30 June 2008. The value of the subsidy to local producers is estimated to have been \$51 million in 2006-07.
- In July 2003, under the *Fuel Quality Standards Act 2000*, the Australian Government introduced a fuel standard for petrol, which permits up to 10 per cent of ethanol to be blended with petrol.
- In July 2003, the Australian Government also announced the Biofuels Capital Grants Program with \$37.6 million in funding for projects producing ethanol or biodiesel. Grants were provided to new or expanded projects producing a minimum of five million litres of biofuel per annum at a rate of 16 cents per litre. Grants were offered to seven biofuel projects.
- In March 2004 and in the Energy White Paper in June 2004, the Government announced that the existing production subsidy and excise arrangements on ethanol will be extended to July 2011, after which the favourable treatment of domestically-produced ethanol is to end. From July 2011, the effective rates of tax will increase annually until they reach final rates of 12.5 cents per litre for ethanol on July 2015. In energy content terms, these final rates allow for a 50 per cent discount on the rates levied on petrol and diesel. (See table 3.2).
- The Energy White Paper also foreshadowed that alternative fuels such as ethanol, that are used for business purposes in heavy vehicles on public roads, will continue to be eligible for a fuel grant under the Energy Grants Credits Scheme. However, the amount of the grant will be reduced to zero in five equal steps commencing from 1 July 2006 and concluding 30 June 2010. After July 2011, a tax credit will apply when the fuel tax applied exceeds a road user charge.

Sources: Howard (2003b), (2006b); Biofuels Taskforce (2005).

---

More recently, in August 2005, the Biofuels Taskforce released a report on the state of biofuels for transport in Australia. Among other things, the report found that:

- Biofuels cost more to produce than petroleum fuels, and barring unexpected scenarios, in the long term will generally remain uncompetitive with conventional fuels without assistance.
- The uptake of biofuels by oil suppliers and biofuel producers entails significant commercial risks and it is unlikely that the policy target of 350 million litres of biofuel production by 2010 would be achieved under the (then) existing circumstances.
- Subsidised ethanol grain plants have the potential to raise feedgrain prices in the short and medium term.
- The costs likely to be imposed on the national economy through assisted expansion of the biofuels industry to achieve the target of 350 million litres would be \$90 million in 2009-10 and \$72 million per annum (in 2004-05 terms) in the long term;
- Part of these losses would be offset by “environmental” and “regional development” benefits.

Following the Biofuels Taskforce report, in September 2005 the Australian Government reaffirmed its commitment to achieve the target of at least 350 million litres of biofuel production by 2010. A Biofuels Action Plan was announced in December 2005, encompassing volumetric goals, marketing strategies and other initiatives drawn up by oil companies and petrol retailers to encourage the uptake of ethanol. Additional initiatives announced by the Government included measures to encourage users of Commonwealth vehicles to purchase E10 (a blend of 10 per cent ethanol with petrol), vehicle testing of E5 (a blend of 5 per cent ethanol with petrol) and E10 blends, and increases in fuel quality compliance inspections to ensure ethanol blends meet fuel quality standards (Howard 2005b).

In August 2006, the Australian Government announced the Ethanol Distribution Program, with funding of \$17.2 million, to run from 1 October 2006 to 30 June 2007. The program aims to:

- increase the number of retail service stations selling 10 per cent ethanol blended petrol (E10);
- increase the volume of E10 sold; and
- encourage the sale of E10 at a lower price than regular unleaded petrol. (AusIndustry 2006b, p. 2)

---

Under the scheme, retail service stations are eligible for two types of grants to install or upgrade equipment such as tanks, fuel lines and bowsers for ethanol fuel sales:

- *Infrastructure Upgrade Grants* — eligible service stations can receive payments of up to \$10 000 to meet the costs of installing or upgrading ethanol equipment; and
- *Sales Target Grants* — additional payments of up to \$10 000 are available to service stations which already receive the infrastructure upgrade grants and meet “predetermined sales targets” to increase the amount of ethanol distributed at their sites.

In November 2006, the Government announced funding of \$7.72 million to support research into biofuel production technologies. The funding, provided under the National Collaborative Research Infrastructure Strategy, is for the construction of two pilot scale facilities and related university laboratory infrastructure to develop “novel” biofuel production technologies.

#### *Liquid petroleum gas conversion*

LPG is a transport fuel that, in Australia, is typically sold at a significantly lower retail price than regular unleaded petrol. Historically, this price differential resulted from a range of factors, including concessions on the rate at which excise tax is levied on LPG, compared to petrol.

In December 2003, the Australian Government announced an intention to progressively introduce excise tax on previously exempted fuel, including LPG. The Government also foreshadowed that, from 2008, a \$1000 subsidy will be available to consumers who buy a new LPG vehicle, to provide ‘assistance for the LPG sector to assist its transition into the excise net’ (Howard 2003b).

In June 2004, the Government released the Energy White Paper which outlined excise tax arrangement for fuel products, including LPG, (and revised the excise arrangements foreshadowed in December 2003). From July 2011, LPG is to be subject to an excise of 2.5 cents per litre, rising to 12.5 cents per litre in 2015 — equivalent to half the excise on petrol and diesel, on an energy content basis.

---

**Table 3.2 Announced excise rates for fuel products**

cents per litre

---

	1 July 2006 to 30 June 2011	1 July 2011	1 July 2012	1 July 2013	1 July 2014	1 July 2015
Ethanol	0	2.5	5.0	7.5	10.0	12.5
Biodiesel	0	3.8	7.6	11.4	15.3	19.1
LPG	0	2.5	5.0	7.5	10.0	12.5
LNG	0	2.5	5.0	7.5	10.0	12.5
CNG <sup>a</sup>	0	3.8	7.6	11.4	15.2	19.0
Methanol	0	1.7	3.4	5.1	6.8	8.5
Petrol	38.143	38.143	38.143	38.143	38.143	38.143
Diesel	38.143	38.143	38.143	38.143	38.143	38.143

---

<sup>a</sup> Rates are cents per litre except compressed natural gas which is cents per cubic metre.

Source: DPMC (2004).

In August 2006, the Australian Government committed significant funding to support the conversion of motor vehicles to the use of LPG. The LPG Vehicle Scheme provides a grant of:

- \$2000 for an approved and fitted LPG conversion of a new or used motor vehicle; and
- \$1000 for a factory-fitted LPG-dedicated vehicle.

Eligibility for the scheme is limited to passenger or light commercial vehicles of less than 3.5 tonnes Gross Vehicle Mass that have been registered for private use. Vehicles that are registered for commercial or business purposes<sup>12</sup> are not eligible for the subsidy.

The estimated cost of the LPG incentives is \$677 million over the eight year period from 2006. Because LPG is a substitute to petrol, the measure also has an impact on petroleum excise revenue. According to the Government, the total cost taking into account the loss of petroleum excise is more than \$1.3 billion over eight years.

---

<sup>12</sup> The Alternative Fuels Conversion Program, which was announced in December 1999, provides grants to operators and manufacturers of heavy commercial vehicles and buses to offset the costs of conversion to natural gas and LPG. The program currently supports key commercial fleet operators to trial selected alternatively-fuelled or hybrid diesel/electric engines in order to assess the commercial viability of these engine systems in heavy vehicles and to demonstrate their feasibility to the wider transport industry.

---

## Oil recycling

Oil recycling involves processes such as filtering, de-watering and de-mineralising used oil to produce burner fuel, including high grade industrial burning oil. There are currently around 70 businesses in Australia engaged in oil recycling activity.

Under the Product Stewardship (Oil) Program, which began on 1 January 2001, support is available to encourage oil recycling through:

- *Excise levy* — producers and importers of all petroleum-based oil or synthetic equivalents are required to pay a levy of 5.449 cents per litre. The levy is intended to offset the costs of payments to oil recyclers as an incentive to undertake increased recycling of used oil. Payments are provided at different rates — as-new re-refined base oil attracts higher payments than basic burner fuels.
- *Transitional Assistance Grants* — grants are available to encourage the recycling of used oil and to develop used oil collection sites and recycling plants. The program entailed funding of \$34.5 million from 2000-01 to 2006-07 (DEH 2005).

During 2006-07, the Government announced an additional \$40.7 million over three years for used oil recycling in the form of additional payments to oil recyclers. The Government said:

This Budget measure will ensure that the oil recycling industry will have time to adapt to the changes arising from the Federal Government's Fuel Excise Reform by adding an additional benefit for three years to the current product stewardship (oil) benefit scheme.

The extra time given to the oil recycling industry to adapt will avoid potentially undermining the success of the Product Stewardship for Oil Program in removing used oil from Australia's environment.

The measure will cease on 30 June 2009.

## Energy

In June 2004, the Australian Government released an *Energy White Paper: Securing Australia's Energy Future*, which foreshadowed new funding measures for the commercialisation of energy technologies, including greenhouse abatement measures (Australian Government 2004). The measures cover industries specialising in the production of existing energy resources (such as oil, gas and coal) as well as renewable energy sources (for example, wind and solar power). Various measures contained in the White Paper were discussed in *Trade & Assistance Review 03-04*.

---

### *Low emission technology projects*

Under the Low Emission Technology Demonstration Fund, announced in the White Paper, \$500 million has been allocated to support low emission technology projects. The assistance covers renewable energy projects, technologies to reduce the demand for energy, and ‘carbon capture’ technologies. Details of the projects supported under the Fund, as at March 2007, are shown in table 3.3.

**Table 3.3 Projects supported under Low Emission Technology Demonstration Fund**  
\$ million

<i>Eligible projects</i>	<i>Technology</i>	<i>Project</i>	<i>Australian Government funding (\$m)</i>	<i>Total project costs (\$m)</i>
Alinta Solar Systems Australia Pty Ltd	Concentrator – Photovoltaic	Large scale solar concentrator power station, Mildura, VIC	75	420
Chevron Australia Pty Ltd (Gorgon)	Geosequestration without electricity generation	Commercial scale demonstration of CCS, Barrow Island, WA	60	841.3
CS Energy Ltd	Flue Gas CO <sub>2</sub> capture	Callide A oxy-fuel retrofit demonstration, Central QLD	50	187.8
Fairview Power Pty Ltd	Electricity generation with natural gas	Demonstration of overseas commercially available open cycle gas turbine, Central QLD	75	445.6
International Power (Technologies) Pty Ltd	Drying and ultra-supercritical generation	Demonstration retrofit of brown coal drying combined with ultra-supercritical coal technology Latrobe Valley, VIC	50	360.8
HRL Limited	Integrated drying gasification combined-cycle power generation	Latrobe Valley, VIC	100	750

Source: MacFarlane (2007a).

## **3.3 Assistance to small businesses**

### **Small business capital gains tax (CGT) concessions**

Under Division 115 of the *Income Tax Assessment Act 1997* (the Act), a general CGT discount of 50 per cent is available to general taxpayers on shares and building investments.

---

In addition, small business owners are eligible for several specific concessions under Division 152 of the Act, including:

- *small business rollover CGT provision* — small business owners can defer paying tax on capital gains where the gains are used to acquire replacement business assets for expansion;
- *small business 15-year exemption* — a full exemption from capital gains tax is available if the asset was held continuously for 15 years and the relevant person is over 55 and retiring;
- *small business 50 per cent deduction* — in other cases, small businesses can apply to reduce the capital gains tax by 50 per cent; and
- *small business retirement exemption* — the capital gains tax on small businesses can be reduced up to an amount of \$500 000 if that amount is paid into a superannuation fund.

The effectiveness of the CGT concessions was reviewed by the Board of Taxation in 2005. The Board found that:

- Division 152 allowed small business owners a choice between the concessions to reduce their capital gains tax, as well as the ability to access multiple concessions at the same time.
- Many small businesses that meet the relevant asset test were not eligible for the concessions because of their business structures — this was, however, outside the scope of its review.
- The compliance costs of the CGT concessions were relatively insignificant for small business recipients, but were an important issue for tax practitioners — the cost was estimated to be about \$110 million (Board of Taxation 2005, p. 7-9).

The Board made a range of recommendations to improve the operation and administration of the small business CGT concessions.

In the 2006-07 budget, the Australian Government announced it will implement most of the Board of Taxation's recommendations and make changes to the eligibility of all CGT small business concessions to reduce compliance costs. The tax revenue forgone under this revised arrangement is expected to be around \$100 million per annum from 2007-08. Legislation has been passed by Parliament to give effect to the Government's changes.

The Government also announced that it will simplify and align various small business concessions, including the capital gains tax concessions. Any business with annual turnover of less than \$2 million will be able to access these concessions, subject to any additional criteria set out in the particular concessions.

---

Thus businesses with a turnover below \$2 million will be exempt from the net asset threshold. It was also announced that the net asset threshold that determines eligibility for the CGT concessions would be raised from \$5 to \$6 million for entities with turnover of \$2 million or more. The tax revenue forgone under the revised arrangement is expected to be \$130 million in 2008-09 (Costello and Bailey, 2006).

### **Entrepreneur Tax Offset**

In the 2004 election policy statement *Promoting an enterprise culture*, the Australian Government announced the Entrepreneur Tax Offset (ETO — sometimes called the Entrepreneur Tax Discount) concession. The ETO took effect from July 2006.

Under the ETO provisions, businesses having low turnover relative to other business classes receive a reduction on the amount of income tax payable. A 25 per cent reduction on income tax applies to businesses with an annual turnover of \$50 000 or less — this rate of reduction is phased down to zero as the business turnover reaches the level of \$75 000 a year. The *Promoting an enterprise culture* statement stated:

[the scheme] will provide further incentive and encouragement to small businesses — particularly those that set up and operate from home ... it will provide a further source of capital which can be ploughed back into a business at its most vulnerable start-up and development stage (LPA-N 2004, p. 4-5).

According to the Tax Expenditure Statement (Treasury 2006), the tax revenue forgone under the ETO is projected to be \$380 million in 2006-07, thereafter rising to \$400 million per year.

## **3.4 Regional adjustment assistance**

During 2006, the Australian Government provided relief to various industries or activities in particular regions that were adversely affected by natural disasters or adjustment pressures. These measures are outlined below.

- *Cyclone Larry Business Assistance Fund*. The fund provided \$260 million in 2005-06 to support businesses and agricultural activities adversely affected by Tropical Cyclone Larry. Eligible businesses located in the Cyclone Larry disaster area can receive a one-off and a tax-free grant of \$10 000 and those with significant losses may be eligible for an additional grant of \$15 000. The grants also assist activities associated with the recovery stage, including, for example, re-stocking, re-planting, re-establishment and clean-up. In addition, businesses

---

are eligible for a wage subsidy (\$400 per fortnight) to retain employees for recovery activities.

- *The Beaconsfield Community Fund*. Announced in May 2006, the fund supports local projects in response to the Beaconsfield Gold Mine disaster in Tasmania. To be eligible, projects must contribute to employment or enhance local facilities in the Beaconsfield community. The fund provides \$8 million in grants over two years.
- *Port Kembla Industry Facilitation Fund*. Announced in June 2006, the fund supports investment projects with potential employment opportunities in the Port Kembla area, in response to the closure of the BlueScope Steel tin mill plant in the area. Support is available for up to 50 per cent of the cost of projects that have a value greater than \$100 000. The Australian Government will provide \$5 million to the fund.

### **3.5 Selective investment incentives**

Historically, all Australian governments have provided selective investment incentives to firms, generally on an ad hoc basis. At the Commonwealth level, such assistance is provided primarily through the Strategic Investment Coordination (SIC) process, administered by Invest Australia. State and Territory governments may also provide selective assistance, potentially in competition with other State governments, to attract targeted firms to invest or locate in their particular State.

In the past, the provision of investment incentives has sometimes led to costly bidding wars among Australian jurisdictions (IC 1996 and Banks 2002). The Commission has examined issues surrounding the provision of investment incentives and reported on the provision of such incentives by governments in previous editions of *Trade & Assistance Review* (PC 1998, 2002<sup>b</sup>).

#### **Commonwealth investment attraction**

In the 1997 *Investing for Growth* statement, the Australian Government established Invest Australia as the dedicated agency for investment attraction and promotion. Invest Australia promotes industry investment opportunities by, among other things, providing market information and advice on business establishment costs, and connecting investors to government contracts. Following a review in 2001, Invest Australia's functions were broadened to incorporate the previous inward investment attraction activities of Austrade and the National Office of the Information Economy.

Invest Australia's activities were targeted at industries including information and communication technologies, biotechnology and pharmaceuticals, nanotechnology, and finance (box 3.4).

**Box 3.4 Invest Australia previous priority industries**

<i>Industries to receive extensive promotion and attraction</i>	<i>Industries to receive facilitation services</i>	<i>Industries with limited promotion</i>	<i>Other priorities</i>
Information and communication technologies	Mining	Renewable energy	Heavy engineering and infrastructure
Biotechnology and pharmaceuticals	Energy, including liquefied natural gas	Environment industry	Spatial information
Nanotechnology		Forest and wood	Film
Finance		Light metals	Food

Sources: ACG (2005) and Blackburne (2001).

The *Investing for Growth* Statement initially committed funding of \$28 million for investment attraction over the four years to 2001-02. In the 2002-03 budget, an additional \$44 million was allocated to continue Invest Australia for the four years to 2005-06.

In 2005, Invest Australia engaged the Allen Consulting Group (ACG) to evaluate the agency's activities. In its report in June 2005, ACG recommended that Invest Australia continue, but that its operations be improved in several areas, including by:

- developing further cooperation between Invest Australia and state government investment attraction agencies to improve overall effectiveness and “the division of labour between the two levels of government”; and
- narrowing the focus of existing priority industries, and giving a higher profile to other areas, such as agribusiness (ACG 2005, p xii).

In the 2006-07 budget, the Australian Government announced that it will provide \$73 million in additional funding to Invest Australia over the four years to 2009-10. The new funding for Invest Australia is to support investment attraction in new markets, including the establishment of offices and market promotion activities in India, Canada, Southern Europe, Scandinavia, Latin America, South East Asia and the Middle East. Invest Australia's existing investment attraction activities in

Western Europe, the United States of America, Japan, and China will be retained. A review of Invest Australia has been scheduled for 2008.

In December 2006, Invest Australia released its Strategic Plan 2006-08, which outlines revised industry priorities for investment attraction. The revised priorities are intended to cover additional countries and industries on the basis of “the Australian Government’s economic, social and environmental goals, industry development objectives and industry investment needs, as well as the prevailing market conditions”. Different industry priorities have been established for each targeted country, and are to be reviewed annually. The activities and industry priorities in the Strategic Plan are outlined in table 3.4.

**Table 3.4 Invest Australia’s revised priorities**

<i>Countries</i>	<i>Industries and activities</i>
<b>North America</b>	
Canada and the United States	Establish new partnerships between US and Australian companies. Attract smaller companies as their first step into the Asian region. Convince current investors to expand their operations. Maintain a focus on attracting major US financial services firms. Influence the North American market and media about Australia as an investment destination. Increased focus on Canada and additional activity in the US mid-west and south.
<b>Europe</b>	Continue previous priorities on high technology, biotechnology and pharmaceuticals, ICT, nanotechnology and environmental technologies.
<b>North Asia</b>	
Japan	ICT, biotechnology, renewable energy and environment industries and financial services sectors and promote energy, minerals and agribusiness industries.
Taiwan	ICT, energy, minerals and food.
South Korea	Energy, minerals, manufacturing, renewable energy, environmental technologies, forestry, wood products and food sub-sectors.
China	Minerals, energy and agribusiness with the focus on targeting the top 15 companies in each sector.
Hong Kong	Top 300 companies listed on the Hong Kong Stock Exchange.
<b>Rest of world</b>	
India	New priorities: financial services, minerals, shared services, biomedical biotechnology and ICT. Existing priorities: agribiotech, environmental services, automotive suppliers, film, dairy, functional foods and energy (including clean coal technologies).
Singapore	ICT, agribusiness, biotechnology and energy.
Malaysia	Food, energy and biotechnology.
Philippines	ICT, food and financial services.
Latin America	Minerals, energy, agribusiness, environmental services, ICT and shared services.

Source: Invest Australia (2006).

---

## The Interstate Investment Agreement

In recognition of the adverse effects that selective investment incentives can have on ‘efficient competition’ and ‘national welfare’, in 2003 all State and Territory governments except Queensland signed an agreement — the Interstate Investment Cooperation Agreement — to reduce cross-border bidding wars and restrict the use of financial incentives to attract investment. The agreement was due to expire in 2006.

In its *Review of National Competition Policy Reforms* (PC 2005), the Commission received submissions from some State governments on this issue and also reviewed progress in implementing the interstate agreement.

The report found that the original concerns of state governments that had led to the signing of the Interstate Investment Agreement remained significant. For instance, the Tasmanian Government suggested that investment attraction potentially becomes ‘an important issue for smaller economies, such as Tasmania, in the event that national economic growth slows and investment becomes more difficult to attract’.

The Commission’s report also found that the agreement lacked mechanisms to ensure monitoring and compliance. Accordingly, the Commission recommended that the Interstate Investment Agreement be strengthened to encourage compliance and be extended to cover all jurisdictions, including the Australian Government.

In March 2006, all State and Territory governments, except Queensland, renewed the Interstate Investment Cooperation Agreement. The Agreement largely carries forward the commitments of signatory governments under the previous Agreement for another five years, with provisions for a formal review in 2010.

### 3.6 Anti-dumping measures

Under Australia’s anti-dumping rules, local companies can apply to have anti-dumping and countervailing measures — mainly special customs duties — imposed on ‘dumped’ imports if the imports cause, or threaten to cause, material injury to the local industry.<sup>13</sup>

---

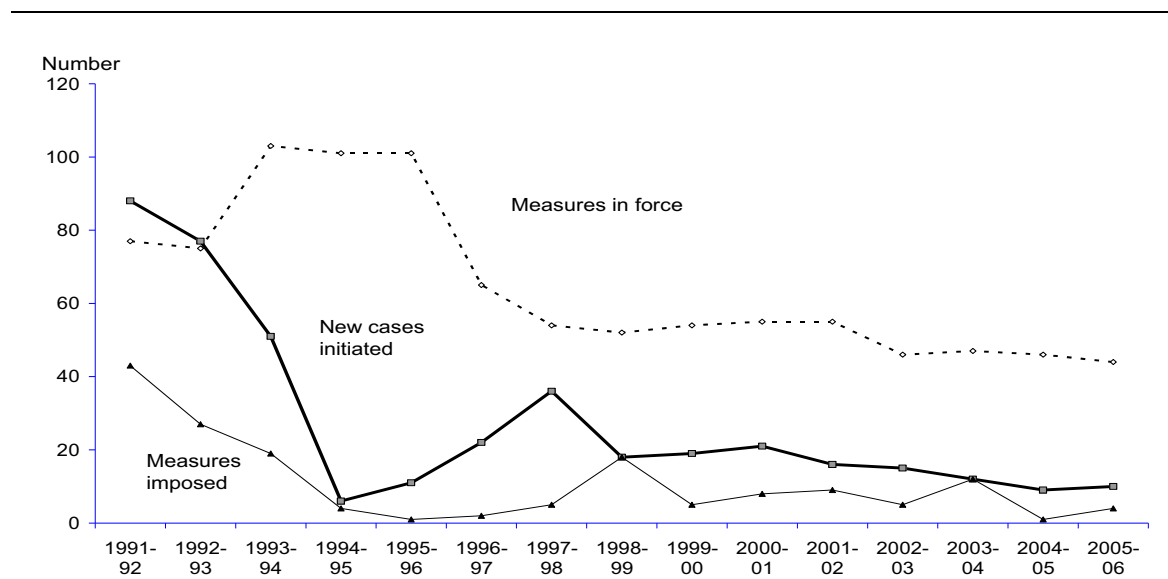
<sup>13</sup> Dumping is said to occur when a foreign supplier exports goods at a price below the ‘normal value’ of the goods in the supplier’s home market. The price of the good in the exporter’s home market is generally used to determine the normal value.

## Recent activity levels

The number of new anti-dumping and countervailing cases *initiated* in Australia has been stable and relatively low over recent years, compared with the early 1990s (figure 3.1). There were 10 new cases in 2005-06, of which half were initiated mainly by firms in *the steel manufacturing* industry. Over the ten years to 2005-06, however, the chemical and plastic products industry has been the largest initiator of anti-dumping and countervailing actions, accounting for 38 per cent of total initiations.

Four new measures were *imposed* by the government in 2005-06, compared to one measure imposed in the previous year. Even so, the number of measures *in force* remained relatively stable at around 50 (figure 3.1). More detailed information on the number and nature of recent anti-dumping cases in Australia and the level of anti-dumping activity overseas is presented in appendix B.

Figure 3.1 Anti-dumping and countervailing activity,<sup>a</sup> 1991-92 to 2005-06



<sup>a</sup> A measure or case is counted as an action applying to one commodity from one economy. If multiple economies are involved, they are counted as separate actions.

Source: ACS (various).

## Review of anti-dumping arrangements

Like other trade barriers, anti-dumping and countervailing measures provide immediate relief for the protected industries, but can restrict competition and, through higher prices, penalise consumers and domestic downstream industries.

---

Accordingly, Australia's anti-dumping regime was scheduled for review by 2000 under the legislation review element of the 1995 National Competition Policy Agreement. However, such a review has not yet taken place.

In its *Review of National Competition Policy Reforms* (PC 2005), the Commission recommended that an independent review of anti-dumping arrangements be undertaken as soon as practicable, noting that:

... the potential for the inappropriate applications of anti-dumping to jeopardise the wider benefits that trade and competition policy have delivered makes this one of the more important trade policy areas to be addressed.

In February 2006, the Australian Government announced an 'administrative' review of Australia's anti-dumping regime (the Joint Study). The joint study was completed in August 2006. The study team noted that its terms of reference was limited and specifically excluded examination of issues or the legislative basis for the anti-dumping system. Even so, a substantial proportion of submissions raised broader policy issues that fell outside its terms of reference, including the need to consider economy-wide costs and benefits (the public benefit test) of imposing dumping duties. The review recommended several changes to administrative procedures (ACS and DITR 2006).

In November 2006, the Australian Government responded to the review, noting the key recommendations to be implemented (Ellison and MacFarlane 2006). They include:

- developing Customs's assessment guidelines and applying them consistently in considering anti-dumping applications;
- improving the availability of information during an anti-dumping investigation and making the public file on the investigation available on the Internet;
- engaging external experts to improve Customs's analysis and decision-making;
- appointing a specialist Customs officer to assist small and medium enterprises (SMEs) to understand the anti-dumping system; and
- developing plain English, user-friendly guidelines for applicants.

The Government also noted that, as outlined in its response to the *Report of the Taskforce on Reducing Regulatory Burdens on Business* (RTF 2006), it will commission a comprehensive public review of both the policy and administration of Australia's anti-dumping system. The findings of the joint study will form part of the input into this review.