

1998 - 99

THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

EXCISE TARIFF AMENDMENT (AVIATION FUEL REVENUES) BILL 1999

EXPLANATORY MEMORANDUM

(Circulated by authority of the Treasurer, the Hon Peter Costello, MP)

ISBN: 0642 403457

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OUTLINE

This Bill is one in a package of three Bills to implement the Government's Budget decision to increase the customs and excise duty payable on aviation gasoline ("avgas") and aviation kerosene (commonly referred to as aviation turbine fuel or "avtur") to:

- provide funding for the Civil Aviation Safety Authority's role of fostering air safety regulation in Australia; and
- offset the Government's subsidisation of Airservices Australia operations at a number of control towers at regional and general aviation airports.

The Civil Aviation Safety Authority (CASA) was established to promote and foster air safety regulation. The main source of CASA funding is through the collection of excise and customs duty on avtur and avgas. It is estimated that there will be a shortfall of funding for CASA operations in the financial year 1998-99 which will continue in the subsequent years.

The Government decided to address CASA's long term funding problem by increasing the excise and customs duty on avtur by 0.391 cents per litre and on avgas by 0.467 cents per litre. The increases will have a small impact on the aviation community while ensuring that the aviation industry and fare paying passengers continue to make a fair contribution to the safety benefits which CASA provides.

It is estimated that the increases on aviation fuels attributable to CASA will raise \$8.6 million per annum in combined excise and customs duties.

Airservices Australia (Airservices) provides aviation services to international, national and general aviation sectors of the aviation industry. Airservices does not currently obtain any funding for its operation from duties on avtur and avgas. Although it is intended that Airservices operate on a commercial basis and charge fees based on the cost of the services it provides, the Government has decided to provide a subsidy to minimise the impact of location specific pricing at regional and general aviation airports. This subsidy is estimated to be \$11 million in 1999-2000 and \$7 million in the following year.

In order to fund this subsidy which will help maintain services to regional Australia, the Government has agreed to impose an additional 0.51 cents per litre excise and customs duty on avtur and avgas to off-set the cost to the Commonwealth of subsidising Airservices' operations. It is estimated that the increases on aviation fuels attributable to Airservices will be \$11.1 million per annum in combined excise and customs duties.

The new rate of excise and customs duty for both avtur and avgas will be \$0.0271 per litre.

This Bill increases the rate of excise duty on avgas and avtur to \$0.02710/L, on and from 12 May 1999.

The other Bills in the package are the:

- Customs Tariff Amendment (Aviation Fuel Revenues) Bill 1999, which increases the rate of customs duty on avgas and avtur to \$0.02710/L, on and from 12 May 1999; and
- Aviation Fuel Revenues (Special Appropriation) Amendment Bill 1999, which enables customs and excise duties on avtur and avgas to be appropriated to the Civil Aviation Safety Authority and Airservices Australia, in such proportions as determined by the Minister for Transport and Regional Services, and for a portion of the duties to remain in the Consolidated Revenue Fund.

REGULATION IMPACT STATEMENT

CIVIL AVIATION SAFETY AUTHORITY FUNDING

PROBLEM

The Civil Aviation Safety Authority (CASA) was established to promote and foster air safety regulation. CASA's funding comes from three sources: the Commonwealth Budget (\$28.4m for 1998-99), duty on aviation fuels (avgas and avtur) (original estimate \$46.6m; current estimate \$37.4m); and fees and charges (estimated \$2.6m). This funding allocation is based on a model developed by Andersen Consulting in 1993 which identified the beneficiaries of aviation safety regulation to be the general public, air travellers and the aviation industry. The Commonwealth Budget provides the general public component, fuel duty provides both the aviation industry and the passenger components of cost recovery, and fees and charges for CASA's services provide funding from the aviation industry.

When CASA was established in July 1995, duty on aviation fuel was set at a rate which resulted in an over-recovery from the industry. To rectify this, the rates of duty were reduced on 1 September 1996. However, CASA has produced a negative operating result over the past two years. It is currently sustaining its operations by running down its cash reserves, which are rapidly depleting.

SPECIFICATION OF THE DESIRED OBJECTIVE

To address CASA's long term funding problem excise and customs duty on aviation gasoline (avgas) and aviation kerosene (avtur) are to be increased slightly to 2.2 cents per litre (¢/l). The increase for avgas will be 0.467¢/l and for avtur 0.391¢/l.

Fuel	Estimated volume 1998/99 kl	Current rate 1/2/99 ¢/l	Propose d increase ¢/l	New rate 12/5/9 9 ¢/l	Current est revenue 1998/99 \$m	Additional revenue 1999-2000 \$m	Total est revenue 1999- 2000 \$m
Avgas	1.111	1.733	0.467	2.2	1.925363	0.518837	2.4442
Avtur	20.555	1.809	0.391	2.2	37.183995	8.037005	45.2210
Total					39.109358	8.555842	47.6652

These rates will be lower than the rates were prior to the 0.75¢/l reduction in September 1996. (Duty on Avgas was further reduced by 15.6¢/l associated with the introduction by Airservices of location specific pricing in July 1998.)

The rates for avgas and avtur were identical until November 1995 when a minor technicality resulted in avgas reverting to its previous rate. This is an opportunity to re-establish a single uniform rate.

Increasing aviation fuel duty appropriated to CASA to 2.2 ¢/l is estimated to raise an additional \$8.6m, which will provide CASA with a revenue stream of \$46m from Special Appropriations under the *Aviation Fuel Revenues (Special Appropriation) Act 1988*.

IDENTIFICATION OF OPTIONS

Two options are available.

1. Retain the levels of aviation fuels duty at the current rates.
2. Increase the levels of duty to address CASA's shortfall in revenue from aviation fuels duty.

Other options considered were the introduction of a passenger ticket tax and aircraft registration fees. Both options were rejected. The passenger ticket tax would be costly to administer, would take time to set up, required strong cooperation from industry and would be no more equitable than fuel excise. Graduated aircraft registration fees would be less equitable to industry, take time to set up and would not cover sectors of the industry which benefit from CASA's services.

ASSESSMENT OF IMPACTS

Impact Group identification

Groups directly and indirectly affected by CASA's funding arrangements and any changes to those arrangements are:

- *The Government* – in terms of implementation and administration.
- *CASA* – as the recipient of the funds.
- *The aviation industry* – as the subject of CASA's safety regulatory activity, the recipient of other regulatory services and a significant contributor to CASA's funding.
- *Air travellers* – as CASA's primary beneficiaries of safety regulation and indirect contributors to CASA's funding.
- *The general community* – as indirect beneficiaries of aviation safety regulation.

Assessment of Costs

Option 1

If no action is taken to address CASA's long term funding problem, CASA would be unable to carry out essential safety regulatory functions. This could have a serious negative impact on aviation safety in Australia, including regional Australia.

Option 2

Duty on aviation fuels is a direct cost on the aviation industry. The current rates of duty on avgas and avtur are 1.733¢/l and 1.809¢/l respectively. The current cost to the industry is in the order of \$39m for 1998-99.

Increasing avgas by 0.467¢/l and avtur by 0.391¢/l is a small increase to an already low rate of duty. It will have a small impact on the aviation community (totalling about \$8.6m per annum) while ensuring that the aviation industry and fare paying passengers continue to make a fair contribution to the safety benefits CASA provides.

Increases in aviation fuel costs may be passed on to air travellers through increased ticket prices and to other users of aviation services (eg. increased air-freight rates). If most of the increase is passed on to Australia's domestic passengers, they will pay an extra 25-30 cents per one-way ticket.

Assessment of Benefits

Option 1

If the amount of duty is not increased additional costs to the aviation industry in the order of \$8.6m would be avoided.

Option 2

The primary benefit will be the continuation of a high level of safety for the aviation industry and fare paying passengers.

Aviation fuel duty is levied on all aircraft fuel other than duty used by foreign international carriers and so is paid by regular passenger transport, regional airlines, air freight carriers and charter operators, as well as the broad general aviation sector. In effect, all aircraft sectors contribute to CASA's costs. It involves an element of cross subsidy from large operators to small operators. Compliance and administrative costs for the industry are minimal.

CASA's primary beneficiaries, fare paying passengers, contribute to CASA's costs, although it is an indirect contribution.

Although susceptible to fluctuations in aviation activity, aviation fuel duty is reasonably predictable as a revenue source.

The option will be revenue neutral to the Government. The collection and payment to CASA of aviation fuels duty is administratively simple and places no significant administrative demands on CASA. Administrative costs to the collection agency (Australian Taxation Office) and CASA are minimal.

It is a convenient cost recovery mechanism. The legislation and administrative arrangements are already in place. There will be no additional ongoing administrative costs for the Government, CASA and the aviation industry.

CONSULTATION

Discussions have been held with the aviation industry on the need to provide CASA with adequate revenue to carry out its functions and for it to have an ongoing revenue base so that it can forward plan. Aviation industry representatives consider that the current level of duty is small. Representatives have commented that if the industry is to pay more for CASA's operations, CASA has a responsibility to minimise its costs.

FUNDING OF REGIONAL AND GENERAL AVIATION AIRPORT SUBSIDY

PROBLEM

On 1 July 1998 Airservices Australia introduced terminal navigation charges for all of its tower services, including in regional areas, which were based on the costs it incurs at each location. The Federal Court ruled Airservices' charges unlawful other than on such a basis; and the Australian Competition and Consumer Commission – from which Airservices must obtain approval when it seeks to vary its charges – supports location-specific charges. The move to location specific charges was accompanied by the abolition of 15.692 cents per litre (¢/l) aircraft gasoline (avgas) duty directed to Airservices.

The full implementation of these charging arrangements under Airservices' current cost structure would result in increases in charges of up to 300% at some regional and general aviation (GA) airports, ranging from \$7.07 to \$38.22 per tonne landed, compared to the current subsidised rate of \$6.75 at these airports. An increase in charges of the kind necessary to cover costs will destroy aviation services and training facilities in regional Australia.

As some of these airports are vital to important regional centres, it was announced in the 1998/99 Budget that Government and users at the major capital city airports would subsidise the charges at these airports. However, at the time the subsidy was agreed to, it was on the basis that it was required as an interim measure. It was anticipated that Airservices would be able to contract out or privatise tower services at many of these subsidised locations, thus reducing the costs imposed on airport users, and allowing the subsidy to phase down markedly in 1999-2000; and disappear the following year.

The recent disallowance by the Senate of the contracting out regulations has meant that cost reductions through the use of alternative service providers are no longer an option in the short term. In order to ensure these essential services are provided at regional and general aviation training centres at a reasonable cost to users, the Government has agreed to maintain a subsidy.

SPECIFICATION OF THE DESIRED OBJECTIVE

In order to fund the subsidy for a further two years, a 0.51¢/l duty surcharge for both avgas, used in piston engined aircraft by general aviation operators, and aircraft kerosene (avtur), used in turbine engine aircraft, is proposed. This will be in conjunction with an increase in the excise and customs duty of 0.391¢/l for avtur and 0.467¢/l for avgas, to address the need for a sounder long-term basis for Civil Aviation Safety Authority (CASA) funding.

A 0.51¢/l surcharge is estimated to raise an additional \$11m per annum, which equates to Airservices' shortfall at non-capital city and general aviation airports.

IDENTIFICATION OF OPTIONS

Three options to fund the subsidy were available.

- A. Continue Government funding.
- B. Recover the costs from general aviation users through a duty surcharge on avgas.
- C. Apply an additional duty surcharge for all aircraft fuels.

ASSESSMENT OF IMPACTS

Impact Group identification

Groups directly and indirectly affected by the subsidy of regional and general aviation airports and the changes to the funding arrangements are:

- *Government* – implementation and administration of the subsidy
- *Airservices Australia* – financial assistance contributes to the cost recovery of services provision at regional and GA airports
- *Operators at subsidised airports* – financial assistance keeps charges capped below full cost-recovery level
- *Aviation industry* – contributing to the financial assistance to ensure that regional and GA airports continue to be part of Australia's network of airports
- *Regional communities* - threat of closure of towers or major increases in user charges removed.

Assessment of Costs

Option A

Government funding was initially considered to be the most appropriate mechanism to fund the subsidy given it was a transition mechanism to allow for the phasing in of full location specific pricing. However, the options for minimising the cost to users of providing tower services are no longer available.

The retention of Budget funding for the tower subsidy would be based on the notion that the key beneficiary of the program is the wider community, however while regional communities will benefit from an ongoing tower service at a reasonable cost to users, the key beneficiary would be the aviation industry.

Option B

Funding the tower subsidy through an additional duty surcharge on avgas would require an increase of approximately 9.9¢/l. This would be seen by the GA industry as a major reversal of the gains from location specific pricing experienced by many users in rural and regional Australia who rarely use the services provided by Airservices.

The decision to subsidise operations at regional and general aviation airports was in recognition of the fact that those directly benefiting from the provision of a tower service are unable to meet the full cost (under Airservices' cost structure) of the service. Recovering the subsidy through a surcharge on the aviation fuel used by these operators would therefore undermine the rationale behind the subsidy.

As with Option C, the actual revenue from a surcharge on fuel is subject to fluctuations in aviation activity.

Option C

If cost is recovered from applying a small duty surcharge for all aircraft fuels, the cost to major users of avtur such as Qantas and Ansett will be relatively small, but will be seen by the airlines as inconsistent with the concept of location-specific pricing.

Assessment of Benefits

Option A

Continuation of Government funding of the subsidy would ensure that tower services continue to be provided at a reasonable cost to users. The amount of the Budget contribution is transparent to taxpayers, although it is not clear what is the specific benefit derived by the general community.

Budget funding is administratively simple.

Option B

The introduction of a duty surcharge on avgas to cover the costs of the subsidy would ensure that those directly benefiting from the capped charges would be the major contributors to recovering the cost of the subsidy, however this would lead to the question of why provide a subsidy at all.

Options C

This option reflects the fact that the services provided by Airservices Australia at general aviation and regional airports contribute to the safety and efficiency of the industry as a whole. Recovering the costs across industry explicitly recognises that many of the regional subsidiaries of the major airlines use the subsidised regional airports, and the capital city general aviation airports reduce congestion at the major airports by allowing for a separation of operations between general aviation and regular passenger transport activities.

As with Option B, this option will be revenue neutral to the Government, and it is a convenient cost recovery mechanism with legislative and administrative arrangements needing only minor modifications.

CONSULTATION

The need to maintain the subsidy for tower services has been discussed with users at the regional and general aviation airports, and there is strong support.

While the option of funding this subsidy through a duty surcharge on avgas and avtur has not been explicitly canvassed with industry, aviation industry representatives have conceded that the current duty on aviation fuels is low. Representatives from the general aviation industry have supported the re-introduction of a surcharge on all aviation fuels to help contain charges at general aviation airports.

CONCLUSIONS

If CASA's funding base remains inadequate, there could be serious safety implications for the aviation industry. To do nothing is not a responsible option. The simplest solution to CASA's long term funding requirements is to have a small increase in the rates of aviation fuel duty.

The Government's commitment to maintain a subsidy for the provision of tower services at regional and general aviation airports can be met without burdening the general taxpayer. While there are benefits to the wider community in rural Australia, the key beneficiary of this Government policy is the aviation industry, and under Option C, only a small duty surcharge on aviation fuels would be required (0.51¢/l) to ensure industry as a whole meets the cost of the subsidy.

The combined impact on the aviation industry will be to add an additional cost in the order of \$19.6m for 1999-2000, and in the order of \$13.1m in 2000-01. However, this will contribute to ensuring a high level of aviation safety in Australia and that regional and general aviation airport control towers remain open without burdening the industry with excessive tower-usage charges.

IMPLEMENTATION AND REVIEW

To implement the increase in aviation duty rates, Excise and Customs Tariff Proposals and amendments to the Schedule of the *Excise Tariff Act 1921*, Schedule 3 of the *Customs Tariff Act 1995* and the *Aviation Fuel Revenues (Special Appropriation) Act 1988* are required.

Treasury and the Australian Taxation Office will monitor this taxation measure as part of its ongoing role in maintaining and reviewing the taxation system.

The 0.51¢/l increase in fuels duty to fund the subsidy for maintaining control towers at regional airports will be reviewed within the next two years.

FINANCIAL IMPACT STATEMENT

The increased rates of customs and excise duty on aviation fuels are projected to raise an extra \$8.6 million in each financial year from 1999-2000 onwards for the Civil Aviation Safety Authority, bringing its total revenue from aviation fuel duty to \$46 million.

No appropriation is to be made direct to Airservices at this time. Annual revenue from the 0.51 cents per litre duty surcharge is projected to be \$11.1 million and will remain in Consolidated Revenue Fund. This will offset the subsidy for regional airport control towers; being \$11 million for 1999-2000 and \$7 million for 2000-01.

EXCISE TARIFF AMENDMENT (AVIATION FUEL REVENUES) BILL 1999

NOTES ON CLAUSES

Clause 1 – Short title

This clause provides for the Act to be cited as the *Excise Tariff Amendment (Aviation Fuel Revenues) Act 1999* (Amendment Act).

Clause 2 - Commencement

Subclause (1) provides that, subject to the effect of subclause (2), the Amendment Act commences on the day on which it receives the Royal Assent.

Subclause (2) provides that the items of Schedule 1, which deal with increases in excise duty on aviation kerosene and aviation gasoline, are taken to have commenced on 12 May 1999.

Clause 3 - Schedules

This clause is the formal enabling provision for the Schedule to the Amendment Act. It provides that each Act specified in the Schedule is amended or repealed as set out in the applicable items of the Schedule. The Act specified in the Schedule to the Amendment Act is the *Excise Tariff Act 1921*. The clause also provides that the other items of the Schedule have effect according to their terms. This is a standard enabling clause for transitional, savings and application items in amending legislation. There are no such clauses in the Schedule to the Amendment Act.

SCHEDULE 1 – AMENDMENT OF THE EXCISE TARIFF ACT 1921 HAVING EFFECT FROM 12 MAY 1999

Item 1 - Subitem 11(A) of the Schedule to the Act

As part of 1999-2000 Budget, the Government decided to increase the excise payable on aviation kerosene to \$0.02710/L, with effect from 12 May 1999.

This item provides for the repeal of the existing rate of excise duty payable on aviation kerosene, and the substitution of a new rate of \$0.02710/L.

Item 2 - Subparagraph 11(H)(1)(a) of the Schedule to the Act

Item 3 - Subparagraph 11(H)(2)(a) of the Schedule to the Act

As part of 1999-2000 Budget, the Government decided to increase the excise payable on aviation gasoline (avgas) to \$0.02710/L, with effect from 12 May 1999.

Item 2 provides for the repeal of the existing rate of excise duty payable on aviation gasoline, in packages not exceeding 210 litres, and the substitution of a new rate of \$0.02710/L.

Item 3 provides for the repeal of the existing rate of excise duty payable on other aviation gasoline, and the substitution of a new rate of \$0.02710/L.