



CPRS Fuel Tax Adjustment Arrangements: Exclusion of Forestry from Fuel Credit Scheme

Recommendations

In order to prevent the perverse policy outcome of rendering many small, Australian forestry businesses unviable and seriously damaging the broader Australian forest industry, NAFI recommends:

- That sections 6-5, 6-15 and 6-20 of the *Carbon Pollution Reduction Scheme (CPRS Fuel Credits) Bill 2009* be reviewed to incorporate forestry and forestry activities as eligible businesses under the CPRS Fuel Credit Scheme.
- That sections 6-5, 6-15 and 6-20 of the *Carbon Pollution Reduction Scheme (CPRS Fuel Credits) Bill 2009* be reviewed to incorporate carbon sequestration activities as eligible businesses under the CPRS Fuel Credit Scheme.

Introduction

The National Association of Forest Industries (NAFI) welcomes the opportunity to provide comment on the *Carbon Pollution Reduction Scheme (CPRS) Fuel Tax Adjustment Arrangements* exposure draft legislation and commentary.

Fuel taxes have major impacts on the viability of businesses and industries that use large amounts of fuel as part of general business activities. These industries include forestry, agriculture and fisheries. Many such industries are based in rural and regional Australia, providing jobs and economic growth in these areas. It is estimated that Australia's forest industry uses nearly 190,000,000 litres of fuel per year.¹

These industries are also exposed to international market pressures – domestic fuel taxes can impede Australian industries' ability to compete in domestic and international markets. In order to maintain the viability of Australian industries, these domestic fuel taxes must be balanced by targeted fuel credits for businesses with significant financial exposure.

¹ NAFI industry estimates, *Harvest and Haulage Fuel Uses and Costs*.

Fuel Taxes and Credits

In order to reduce the impact of fuel taxes on the forestry, agriculture and fisheries sectors, these industries currently have access to fuel tax credits in the form of a diesel rebate scheme. This credit accounts for current fuel taxes but does not make an allowance for future additional taxes or policies that create a cost impost on inputs, such as the proposed Carbon Pollution Reduction Scheme (CPRS).

The Government's proposed CPRS recognises the inflationary effect that carbon trading will have on fuel prices, and the inability of existing fuel tax credits to address this issue. It also recognises that agriculture and fisheries businesses, "pay no effective fuel tax, and so will not benefit from fuel tax cuts. Instead, they will receive a new 'CPRS fuel credit' ... This will ensure that these businesses receive assistance equivalent to the full benefit of the fuel tax cut."²

However, for reasons unexplained, forestry activities are specifically excluded from the CPRS fuel credit entitlements: "The industries benefiting will be 'agriculture' [which excludes forestry activities]...; 'fishing'...; and 'heavy on-road transport'..."³ These provisions discriminate against key forestry activities such as:

- Off-road transport of harvesting and haulage equipment;
- Harvesting activities (including transport of logs and other products within the forest);
- Forest management activities (including forest thinning);
- Carbon sequestration activities⁴;
- Fire management and fuel hazard reduction activities;
- Primary processing activities (such as in-field chipping);
- Off-road haulage of logs and other products; and
- Forest regeneration activities (including site preparation and planting).

Reasons for Exclusion of Forestry

The CPRS commentary does not provide any explanation as to why forestry is specifically excluded from the CPRS Fuel Credit Scheme. NAFI has engaged both Minister Penny Wong's and Minister Tony Burke's offices, as well as the Australian Government Department of Climate Change and Treasury officials regarding this exclusion however none of these sources have been able to provide a suitable rationale.

NAFI considers it likely that forestry has been excluded from the CPRS Fuel Credit Scheme for political reasons – there is no logical public or economic policy argument otherwise. The severe risk to the forestry industry that this political decision poses must require a review of the exclusion. A review of the CPRS Fuel Credit Scheme policy framework should be undertaken in accordance with accepted public policy

² *CPRS Fuel Tax Adjustment Bills – Exposure Draft*

³ *Carbon Pollution Reduction Scheme (CPRS Fuel Credits) Bill 2009 – Exposure Draft*

⁴ *Carbon Pollution Reduction Scheme (CPRS Fuel Credits) Bill 2009 – Exposure Draft*

development principles. NAFI contends that under such transparent public policy circumstances, forestry would be included in the Scheme.

Effects of Exclusion of Forestry from the Fuel Credit Scheme

As identified above, the Government proposes to cut fuel taxes (excise) on a cent for cent basis to offset CPRS impacts on fuel prices. The fuel tax reduction will apply from 1 July 2010 to all liquid fuels currently subject to the general 38.143 cents per litre excise rate. Fuel tax rebates are currently set at the excise rate of 38.143 cents a litre.

Agriculture, fishing and forestry businesses pay no effective fuel tax on their ‘off road’ activities, so will not benefit from fuel tax cuts. To offset this effect, the Government will allow agricultural and fisheries businesses to receive a new ‘CPRS fuel credit’. The amount of credit will equal the amount of fuel tax cut. This will ensure eligible businesses receive assistance equivalent to the full benefit of the fuel tax cut. The proposed exclusion of certain businesses – in this case forestry - that currently receive fuel tax credits, will effectively reduce the benefit of the fuel tax credits by the *full impact of the fuel price rise*.

To demonstrate the magnitude of such fuel price impacts, the industry and individual operator effects of the inequitable treatment of forestry under the proposed CPRS fuel credit scheme are outlined below (refer Box 1). The analysis is based on the Treasury estimate that at a carbon price of \$25 per tonne, the CPRS would result in fuel prices increasing by 7 cents per litre. In this case, the effective rate of fuel tax credit decreases from 38.143 cents per litre to 31.143 cents per litre, and results in an additional cost to the industry of at least \$9 million per annum. More significantly, this would equate to an additional cost of around \$14,000 per harvesting contractor.

Furthermore, while there are a range of estimates for fuel price increases from the introduction of emissions trading, any fuel price increase would place a direct cost on forestry harvesting and off-road activities. These increased costs would not be fully absorbed through the production chain as timber mills will understandably resist efforts by small contractors to pass them on. If the mills were to absorb the costs, it would be at the expense of the competitiveness of their products in the international market place, consequently rendering Australia’s sustainable forestry industry less competitive against overseas imports and in export markets.

As a result, contractors (generally small, family operated businesses) will be forced to absorb the increased fuel cost into their operating margins. Many contractors are already under considerable financial pressure and any increases in fuel costs, delivered without access to the CPRS Fuel Credit Scheme, may push many of these businesses beyond financial viability.

The potential failure of many small, regional businesses would lead to declines in rural and regional economic activity, personal and family breakdowns, social dislocations, unemployment and associated welfare support. As the contractors make up a key part of the forestry industry, such business failures would also have severe negative impacts on the broader forest industry and the Australian economy.

Box 1 – Adverse industry impacts from inequitable treatment of forestry under the CPRS Fuel Credit Scheme⁵

Example 1: Industry wide effects

Currently the forest harvesting sector receives around \$51 million in fuel tax credits (based on fuel usage of 131.8 million litres a year). Should the CPRS lead to a fuel price increase of 7 cents per litre, the industry would receive \$41 million in fuel tax credits, a reduction of 18%. This \$9 million additional cost would have to be absorbed by the industry. This equates to \$3000 per full time equivalent job for the direct operators/contractors engaged in harvesting activity.

Example 2: Individual harvesting business effects

A typical harvesting contractor harvests around 57,000 cubic metres of wood a year and uses 204,000 litres of fuel. Currently the business would receive \$77,811 in fuel tax credits. Should the CPRS lead to a fuel price increase of 7 cents per litre, the business would receive only \$63,531 in fuel tax credits. This business would have to absorb a cost increase of over \$14,000 per annum. As many of these businesses operate on slim profit margins, an 18% reduction in fuel credits would make many harvesting businesses unprofitable.

Typical Contractor Profile

As noted above, the exclusion of the forestry sector from the CPRS Fuel Credit Scheme will have the greatest impact on forestry contractors. These small businesses are generally family-managed, employing local people in rural areas. With the additional financial pressure of rising fuel costs (as will be likely under the CPRS without access to the CPRS Fuel Credit Scheme) many of these businesses will be put under severe financial pressure to remain viable.

These businesses are not in control of major assets; the trees are owned by state forest growers or large private owners and processing capacity is controlled by large sawmilling companies. Contractors usually own just their machines (harvester, forwarder, log truck, etc.) and associated contracts, and many operate under significant debt pressure. Their power to negotiate with either the grower or the processor is limited. Most of these businesses have narrow financial margins and work hard to maintain a successful business.

⁵ NAFI estimates based on information supplied by the Australian Forest Contractors Association.

Conclusion

The current arrangements for the CPRS Fuel Credit Scheme discriminate unfairly against the forestry sector. The negative impacts of the Scheme will fall largely upon small rural businesses with broader regional and social consequences, including business demise, social stress, increased unemployment and reduced rural economic activity.

The arrangements for the Scheme must be changed in order to recognise and address the forestry sector's inequitable exposure to anticipated changes in fuel prices – exposure equivalent to other sectors already identified as being eligible for the Scheme – and financial and social hardship this would otherwise place on an important part of the Australian forest industry.

NAFI welcomes the opportunity to provide comment with respect to the CPRS Fuel Credit Scheme and is committed to working with the Australian Government to ensure the best possible outcomes for the Australian economy and environment.

If there are any questions or queries in relation to this submission, please contact NAFI directly on (02) 6285 3833.