

Received  
08 DEC 2017  
Office of Hon Phil Twyford  
**BRIEFING**

**DRAFT CABINET PAPER: INTRODUCTION OF A REGIONAL FUEL TAX**

<b>Reason for this briefing</b>	You asked us to prepare a Cabinet paper on a regional fuel tax.
<b>Action required</b>	Direct officials to make any amendments you require to the attached draft Cabinet paper before lodgement with the Cabinet Office.
<b>Deadline</b>	Tuesday 12 December 2017.
<b>Reason for deadline</b>	To enable officials to make any required amendments to the Cabinet Paper in time for you to lodge it with the Cabinet Office by 10 am, Thursday 14 December 2017.

**Contact for telephone discussion (if required)**

Name	Position	Telephone	First contact
Marian Willberg	Manager, Demand Management	[REDACTED]	X
Andrew de Montalk	Adviser, Demand Management	[REDACTED]	
Bryn Gandy	Deputy Chief Executive, Strategy and Investment	[REDACTED]	

**MINISTER'S COMMENTS:**

s 9(2)(a) of OIA.

<b>Date:</b>	8 December 2017	<b>Briefing number:</b>	OC05415
<b>Attention:</b>	Hon Phil Twyford (Minister of Transport)	<b>Security level:</b>	In-confidence

**Minister of Transport's office actions**

- Noted*
 *Seen*
 *Approved*  
 *Needs change*
 *Referred to*  
 *Withdrawn*
 *Not seen by Minister*
 *Overtaken by events*

## **Purpose**

1. This briefing provides a draft Cabinet paper on a regional fuel tax, for your consideration and discussion with colleagues.

## **Draft Cabinet paper for you to consider**

2. On 4 December 2017 you provided feedback on the design of a regional fuel tax. Based on your feedback we have drafted a Cabinet paper based on the feedback you gave.
3. The purpose of the attached draft Cabinet paper is to seek Cabinet's approval to the fundamental design elements of a regional fuel tax and approval for legislation to be drafted by Parliamentary Counsel Office.
4. This draft Cabinet paper has been prepared quickly. We apologise for any errors and will continue to work on the paper.

## **Using the revenue for Auckland Transport Alignment Project**

5. In our briefing (OC05444 refers) we set out various options for the use of revenue from a regional fuel tax. You indicated you favoured option two. Option two provides funding for specific capital projects, associated debt incurred as a result of the capital projects, and operational expenditure when it is associated with the delivery of a package or programme of projects.
6. Auckland Council (the Council) wants greater flexibility than that allowed by option 2. The Council wishes to fund various "transport activities" including existing operating and capital expenditure specified in its planning documents. We have also set out the Council's view, which was also provided to the Treasury, in the draft Cabinet paper.
7. The Treasury has requested a comment be included in the draft Cabinet paper. The comment states that the revenue should be used to fund capital payments and associated debt repayments for projects proposed by the regional council and approved by joint Ministers.
8. You indicated you preferred the revenue from a regional fuel tax to be used to fund projects identified as part of the update of the Auckland Transport Alignment Project (ATAP). We have drafted the Cabinet paper to reflect your preference for this approach.

## **Effect of trucks fuelling outside Auckland on revenue estimate**

9. In the draft Cabinet paper we have provided an estimate for a 10 cent per litre regional fuel tax in Auckland. Since 4 December 2017 when we discussed briefing OC05444, we have estimated the potential effect of long haul trucks which travel between regions choosing to fuel outside Auckland. Our current estimate is that this could reduce revenue by up to \$20 million per annum.

## **Simplifying refunds for off-road use of diesel**

10. On Monday 4 December 2017 we discussed with you about how off-road diesel should be treated. We thought it would be helpful to clarify the recommendation included in the attached draft Cabinet paper based on that discussion.

11. The draft Cabinet paper provides that refunds for off-road use of diesel be available on the same basis as Fuel Excise Duty Refunds are available for petrol vehicles. We consider this to be the fairest and most logically consistent approach.
12. The attached Appendix provides further information about refunds for off-road use of diesel.

***A maximum rate provision will be required***

13. Based on our earlier advice, you indicated you favoured flexibility about the maximum rate of a regional fuel tax. Since that advice, we have been looking at similar tax provisions that seek to give flexibility to adjust the rate, while providing for direct Parliamentary oversight of rates of taxation.
14. We propose to base the model on the way excise rates for engine fuels are set under the Customs and Excise Act 1996, which is a close analogy. Under this proposal, the maximum rate of the tax would be specified in the primary legislation (potentially in a schedule). This maximum rate would be able to be subsequently amended by Order in Council, with the Orders in Council being subject to confirmation by Parliament through the annual confirmation process.
15. We propose that the initial maximum rate be determined jointly with the Minister of Finance prior to introduction of the Bill.

**Two outstanding matters being worked through**

16. The following matters are still being worked through:
  - a regulatory impact statement has been prepared to accompany the Cabinet paper. The attached draft regulatory impact statement has not been formally assessed by the Treasury.
  - we are continuing to work with the Treasury to get agreement for Crown funding for NZ Transport Agency's initial set-up costs.
17. We will provide your office with an update on these matters when it is available. We will also provide draft speaking notes for the Cabinet meeting.

**Next steps**

18. Once we have received any amendments you require to the draft Cabinet paper, we will provide a revised paper to your office for lodging with the Cabinet Office. If your amendments are substantive, it may be necessary for us to recirculate the Cabinet paper for agency comment.
19. To enable a Cabinet decision before Christmas, you have the option to take the paper to:
  - Cabinet on 18 December 2017 or
  - Cabinet Business Committee (with Power to Act) on 20 December 2017
20. We envisage that Parliamentary Counsel Office may be able to draft legislation more quickly than normal given the new legislation draws on the design of the 2008 regional fuel tax legislation.


**Recommendations**

21. We recommend that you:

- (a) **agree** to seek approval for legislation specifying a maximum rate of regional fuel tax (noting this will replace your agreement to recommendation (e) in our earlier briefing (OC05444)). Yes/~~No~~
- (b) **note** a maximum rate will later be agreed with the Minister of Finance.
- (c) **agree** that refunds for off-road use of diesel should be available in the same circumstances as a refund for Fuel Excise Duty would be available for off-road use of petrol (noting this will replace your agreement to recommendation (h) in our earlier briefing (OC05444)). Yes/~~No~~
- (d) **direct** officials to make any changes to require to the Cabinet paper by Tuesday 12 December 2017. Yes/~~No~~
- (e) **note** that the Cabinet paper will need to be lodged with the Cabinet Office by 10am on Thursday 14 December 2017 for it to be considered by Cabinet on Monday 18 December 2017 or by the Cabinet Business Committee on Wednesday 20 December (with Power to Act)

  
Bryn Gandy  
Deputy Chief Executive, Strategy and Investment

**MINISTER'S SIGNATURE:**

  
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**DATE:** 12.12.17

## Appendix

This Appendix follows up on the discussion at your meeting with Ministry officials on 4 December 2017 on off-road fuel use. It is an elaboration of paragraphs 58-62, and recommendation (h), in our briefing to you of 30 November 2017 (OC05444).

Cabinet agreed on 20 November 2017 that a regional fuel tax (RFT) should apply to "petrol and diesel purchased for use on roads". You have agreed to our recommendation that we base the collection rules on those already in place for the Local Authorities Fuel Tax (LAFT), which is strongly supported by the fuel companies.

Fuel companies are required to pay LAFT on all petrol and diesel, with the exception of fuel they deliver to be used for:

- commercial marine purposes; or
- electricity generation.

This covers some categories of off-road use, but in our view does not go far enough to meet Cabinet's decision of limiting RFT to fuel purchased for use on road. We do not think it would be desirable to address this by adding to the list of exceptions that fuel companies must apply.<sup>1</sup> Doing that would compromise the objective of aligning RFT and LAFT compliance obligations, and in many circumstances the fuel companies will know whether the fuel will be used off-road.

We therefore recommend that fuel purchasers be able to claim refunds of RFT for off-road use in addition to commercial marine and electricity generation.

### Petrol

A mechanism already exists to claim a refund of Fuel Excise Duty (FED) (59.24 cents per litre) for fuel used in dedicated off-road vehicles. This mechanism does not allow a refund where road vehicles are used off-road – or a range of other uses, such as in non-commercial boats or garden tools. These limitations are to reduce opportunities for fraud and the number of small claims that would have disproportionately high transaction costs.

For petrol users, we propose to align the ability to claim a refund for RFT with the existing ability to claim a refund for FED – so a combined refund process will be developed to enable FED and RFT claims to be made through a single process.

### Diesel

35 – 40 per cent of diesel is used off-road, but there is no tax on diesel for road use and therefore no mechanism to claim a refund for it where diesel is used off-road. Road-going diesel vehicles pay for road use by way of kilometre-based Road User Charges (RUC). A refund scheme does exist for RUC, which enables it to be refunded when a RUC vehicle is driven off-road.

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<sup>1</sup> One possible exception is diesel fuel supplied exclusively for use in railway locomotives – if this cannot be achieved, a refund will be available.

We considered two options for determining eligibility to claim a RFT refund for off-road use of diesel:

**Diesel refund option 1 – align with ability to claim FED refund (recommended)**

Under this option, a diesel purchaser will be able to claim a RFT refund where the fuel was used in a dedicated off-road vehicle – such as a tractor or earth-moving machinery. No refund would be able to be claimed where a diesel road-going vehicle was driven off-road – such as a diesel ute driven on a farm.

Advantages	Disadvantages
<i>Equity and fairness – the same approach is taken to petrol and diesel</i>	<i>Not comprehensive – off-road use of diesel road vehicles still subject to RFT.</i>
	<i>Potential volume of claims - off-road use of diesel road vehicles is more prevalent than off-road use of petrol vehicles, so industry may lobby for a wider ability to claim exemption</i>
	<i>Inconsistent with RUC – the ability to claim RUC refunds for off-road use is well-understood – applying RFT to off-road use may be argued to be unfair</i>

**Diesel refund option 2 – add a further ground for claim which aligns with RUC refund**

Operators of RUC vehicles pay RUC in advance. When a RUC vehicle is subsequently driven off-road, a refund of the relevant RUC can be claimed.

Under this option, in addition to allowing a RFT refund to be claimed for dedicated off-road vehicles as described under option 1, there would also be an ability to claim a refund for fuel used in a RUC vehicle off-road, in parallel with the RUC claim.

Advantages	Disadvantages
<i>RFT is refunded for all off-road use</i>	<i>Unfair - off-road use of diesel road vehicles would be eligible for a RFT refund, where off-road use of petrol vehicles would not be.</i>
	<i>Complex – a mechanism is needed to determine the number of litres of fuel associated with a number of off-road kilometres. This is likely to be costly to comply with and administer, and creates a risk of fraud.</i>
	<i>Not coherent - mixing a fuel-based tax with location based rules is not coherent. Generally RFT applies to fuel purchased in Auckland, regardless of where fuel is used. If a refund is allowed for off-road use inside Auckland, this may raise a question as to whether a refund should also be allowed for on-road use outside Auckland. If it was, this would create a situation where RFT is not applied where diesel road vehicles are driven outside Auckland, and RFT is not paid where diesel road vehicles are driven inside Auckland using fuel bought outside it</i>

Our view is that the "not coherent" disadvantage of Diesel option 2 set out above highlights the risk and complexity of mixing refunds based on location of use with a charging mechanism based on location of fuel purchase. We see this as a fundamental issue with this approach. Complexity and cost are also issues, and we think that applying the same rules to petrol and diesel vehicle owners is important. In our view these disadvantages outweigh the arguable benefit that comes from aligning RFT refunds with RUC refunds.

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