## Cabinet: Background information and talking points

**Topic:** ***Temporarily reversing increases to petrol excise duty and road user charges for six months due to heightened fuel prices***

**Portfolio:** *Transport*

**Officials Attending (subject to remote access arrangements):**
- *Marian Willberg, Manager Demand Management and Revenue, Ministry of Transport*

**Background information for the Minister: Reversing increases to petrol excise duty and road user charges is possible but is likely complex and could be ineffective at reducing cost or equity issues relating to the recent increases in fuel prices**

- You have an oral item at Cabinet on reducing the rates of petrol excise duty (PED) and road user charges (RUC) to 2017 levels for six months. Officials are uncertain if decreasing rates would offset the impact of increased fuel prices on businesses and households, especially if the price increases are likely to persist. Officials advise any support should be timely, targeted, temporary, and ideally not undercut the government's transport and wider priorities (including those relating to climate change). s 9(2)(f)(iv) .

- It is important for Ministers to be clear on the purpose of any petrol excise duty cuts or public transport subsidies, and whether such measures are intended to directly support households manage increased fuel costs, broader household living costs, support businesses, or more broadly dampen inflationary pressures. Other tools in the broader tax and welfare system may be more appropriate levers if the objective is to target low-income households struggling with higher living/fuel costs.

- Officials understand that international oil prices are passed through to domestic fuel prices at the pump almost immediately, and that petrol prices are a component of CPI (the consumer price index). This means an increase in fuel prices will have a direct and immediate effect on inflation. The cost of fuel is also an input into the production process (which includes transport costs) of many goods and services. Higher fuel prices will put pressure on the costs faced by businesses, who may pass these costs onto consumers. Officials understand that higher fuel prices can reduce economic activity (household spending and business investment), which tends to reduce inflationary pressure over the longer term. Work is needed to understand whether high fuel prices are likely to be short term and transitory or medium term.

- Early discussions with the Ministry of Business, Innovation and Employment and the Treasury suggest that the proportion of household costs impacted by a 10.5 cent reduction in petrol excise duty could be quite small.[1] Other tools may be more appropriate.

- Officials advise lower-income households have less discretionary income than higher income households. This means high fuel prices likely disproportionately impact lower-income households. There could be better or more targeted ways to mitigate the disproportionate impacts on lower-income households from increased fuel prices than reducing the rates of road user charges and petrol excise duty, if equity (between low and high income households) is the predominant concern.

**Reversing the Government's three increases to petrol excise duty and road user charges**

- To fund the government's transport priorities, petrol excise duty and road user charges rates were increased in 2018, 2019 and 2020. In 2020, the government ruled out further increases for three years (2021, 2022 and 2023).

- If all three rate increases were reversed (2018 to 2020), the rate of petrol excise duty would reduce by around 10.5 cents per litre (with an equivalent decrease for road user charges). The rate of petrol excise duty would be around 59 cents (it is currently around 70 cents) per litre, and road user charges for a light vehicle (e.g. a diesel vehicle) would be about $62 (currently $76) per 1,000 kilometres. There are many rates of road user charges for different vehicle types predominately those over 3.5 tonnes (ranging from $82 to over $1,000 per 1,000 kilometres).

**Cost to the National Land Transport Fund is around $300 million for six months**

- Revenue raised from petrol excise and road user charges is dedicated (or hypothecated) to land transport through the National Land Transport Fund.

- Reversing the increases for six months could reduce revenue by around $300 million. However, this is uncertain due to COVID-caused reduction in personal travel (working from home, home deliveries).

- I understand the Minister of Finance has asked Treasury to look at whether a Crown grant could off-set any reduced revenue from road user charges and petrol excise duty. A Crown top-up would assure no reduction in planned transport expenditure.

[1] The New Zealand Household Travel Survey suggests petrol accounted for about 3.6% of weekly household expenditure in 2016.

**The legislative process for decreasing the rates could be complex**

- Rates of petrol excise duty can be changed by Order in Council under Schedule 3, clause 20 of the Customs and Excise Act 2018,[2] however achieving the 1 April coming into force date would be very challenging.[3] The complication with decreasing petrol excise duty rates is that rates for its refund[4] (predominately relating to off-road uses of petrol) would also need to be amended to prevent those entitled being refunded more than the rate of petrol excise duty when the fuel was purchased.

- Decreasing the RUC rates is more complex. The Road User Charges (Rates) Regulations prescribe rates for over 80 different types of vehicle and vehicle combinations at different weight bands. It would be complex because section 85 of the Road User Charges Act requires that any rate change only comes into force 42 working days (six weeks) after being notified in the *New Zealand Gazette*. It would not be possible, by Order in Council, to reduce rates by 1 April. To achieve 1 April, section 85 would need to be amended so the notice period did not apply when rates were being reduced. Such an amendment would require a Bill in the House and for it to be prioritised in the Government's legislative programme as a matter of urgency.

- Officials advise that we could not simply reinstate the rates in the Road User Charges (Rates) Regulations 2015 as new RUC vehicle types have been created since 2016, and reduced rates would need to be calculated for the new vehicle types.

**Implementation could also be challenging and could be ineffective at offsetting the recent increase in fuel prices**

- It is likely the main issue resulting in high prices is constrained international supply. Even if a 10-cent per litre reduction in petrol excise duty occurred prices would likely remain high until the international supply constraints resolved (retail price of 91 has risen almost 25 cents in the last month).

- Reductions to petrol excise duty rates would likely take a few days to flow through to retail prices at the pump. Officials understand that oil companies price petrol on its replacement value, so officials would expect a fall in retail prices soon after any rate

[2] Clause 20 provides that the Governor-General may, by Order in Council, suspend the rates of duty specified in the Excise and Excise-equivalent Duties Table in whole or in part; and may, by the same or a subsequent Order in Council, provide for a rate of duty that is lower than a suspended rate of duty to apply instead of the suspended rate until the suspension ends.

[3] Indicative timetable to achieve 1 April commencement: A cabinet paper would need to be lodged on 17 March for CBC or CAB on 21 March and EC either on the same day or thereafter. There would be no Ministerial consultation and officials may request you ask for permission to lodge the paper late.

[4] Under the Land Transport Management (Apportionment and Refund of Excise Duty and Excise-Equivalent Duty) Regulations 2004, refunds of petrol excise are available to operators of exempted vehicles, commercial and rescue ships, and users of petrol for commercial purposes (but not petrol used in any motor vehicle, vessel, or aircraft).

reduction. However, it is possible, due to the volatility in the international market, any decrease in the rates would not be directly seen at the pump by the consumer due to an increase an the importer price of fuel (however would likely offset some of the increase). Decreases in the taxes could increase road travel, creating more demand and price pressure.

- Road user charges are pre-purchased in 1,000 kilometre lots in advance of travel, but many road users purchase 2,000, 5,000 or 10,000 kilometres at a time (to minimise the transaction cost). Consideration could be given to putting in place a refund arrangement for pre-purchased kilometres, but this could be very difficult and expensive (and exceeding the refund value). Officials would need to engage with Waka Kotahi about its practicality. There is also the risk that a temporary rate-reduction would encourage the bulk purchase of large amounts of road user charges ahead of rates increasing in 6 months.

- Fuel prices are volatile and difficult to predict. It is not known whether prices would have decreased or increased in six months. Given this, it is not possible to predict the practicalities associated with re-introducing the current rates in six months time – or whether an extension (or further reduction) may be required given the international situation.

s 9(2)(g)(i)

[redacted]

s 9(2)(f)(iv)

[redacted]

**Annex: Additional information requested by the Minister of Transport (if needed)**

**Fuel vouchers could be difficult and may not help reduce households' broader living costs**

- Administratively complex (targeting, delivery mechanism), the potential for a secondary market to develop, increase demand for fuel and therefore increase prices. Even if a delivery mechanism is available, fuel vouchers would not help reduce households' broader living costs (eg food).
- Targeted support arrangements could be explored using the benefit system, including increases to the rate of the Winter Energy Payment, due to commence on 1 May 2022, or the Disability Allowance. There are risks regarding wider inflation and the ability for these transfers to be wound-back if the shock is transitory. Additionally, there is a need to determine whether these would provide an effective way to target those at greatest need.
- s 9(2)(g)(i) [redacted]

**High fuel prices have the potential to induce behaviour change or mode shift**

- Evidence suggests that increases in price of fuel result in a modest reduction in car use or mode shift, but small price increases can induce the uptake of more fuel-efficient vehicles. The price required to achieve a change depends on the trip and the availability of alternatives. Public transport (or walking or cycling) is often not a direct substitute for car travel, this can be due to lack of public transport services or other alternatives like ride share.
- In terms of specifics, New Zealand modelling shows[5] that a 10 percent real rise in petrol price could decrease fuel consumption by 1.5 percent within a year. In terms of traffic demand:
    - urban off-peak traffic could fall by 2.7 percent by a 10 percent price increase
    - urban peak traffic could fall by 0.9 percent by a 10 percent price increase
    - rural traffic could fall by 1.6 percent by a 10 percent price increase
- Work from the United Kingdom shows a 1 percent increase in driving per-mile cost reduces car mileage by less than half of one percent.
- New Zealand and the United Kingdom work suggests a significant price increase may be required to reduce the distance travelled or encourage sustained mode shift.
- In 2008, when the price of petrol reached $2 a litre in Wellington there are reports that there was a shift from motor vehicles to public transport in the capital for a short period. However, it has been suggested the shift was not sustained, people may become accustomed to the increased price and revert to regular travel habits.

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[5] The modelling was done in 2007 and related only to a small change in price. The modelling may not apply the recent and significant increase in price or due to COVID.

**How other countries have acted to the high price of fuel**

- In Australia the Commonwealth so far as "ruled out" reducing federal excise duty.
- The Biden Administration has reportedly considered a federal fuel (or gas) tax holiday. Commentary questioned its effectiveness. It is understood that the Biden Administration may no longer be pursuing the measure and has focused on increasing fuel supply to bring down prices
- In the United Kingdom, pressure has been put on the Johnson Government to temporarily reduce the rate of VAT on fuel (particularly for fuel used for winter heating).
- The Republic of Ireland is reducing tax on petrol (20 cents per litre reduction) and diesel (10 cent per litre reduction), however there is concern the reduction will be "wiped out" by rising international prices.

**Public transport support options to help address equity issues of rising fuel prices**
The Ministry's preferred option is to provide you with advice on how best to achieve your objectives Some of the options below are being considered as part of Budget 22. There is the potential some of these could be brought forward, but that is uncertain and may risk unsuccessful delivery.

| **Options** | **Ministry of Transport advice** |
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| **Budget 2022 bids** | |
| **Equity-orientated vehicle scrappage scheme** - aims to shift low-income people out of fuel powered cars to low emission vehicles, or low emission alternatives, by offering low-income households who scrap their vehicles s 9(2)(f)(iv) [redacted] | An equity-orientated vehicle scrappage scheme has the potential to reduce costs to low-income households by reducing their weekly expenditure on fuel. Officials are working through implementation options for the scrappage scheme. s 9(2)(f)(iv) [redacted]<br><br>[redacted] |

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| **Community connect pilot expansion** - Offering a 50 percent concession on public transport for Community Services Card holders (CSC). | Extending the Community Connect pilot could mitigate the direct costs that some CSC holders face of rising fuel prices if the scheme encourages CSC holders who currently drive to switch to public transport.<br><br>CSC holders who already use public transport or do not rely on a private car will not be directly impacted by rising fuel prices but will indirectly benefit – rising fuel prices will indirectly put upward pressure on living costs (eg food prices), and offering cheaper public transport is a way to offset these rising living costs.<br><br>The Community Connect pilot in Auckland is expected to start from July 2022, with pre-registration and associated community engagement expected to start in May. Efforts to accelerate the launch of the pilot are dependent on additional resourcing to agencies to speed up implementation. Efforts may also be limited by Auckland Transport's ability to process applications and distribute HOP Cards to applicants, if it receives a significant number of applications. MSD's ability to speed up their processes is also likely to be constrained by other work priorities, especially in response to COVID. The proposed July 2023 launch for the budget initiative to roll-out Community connect nationwide is already ambitious and is dependent on MSD working with public transport authorities. There are also limitations with the Regulations governing the CSC which still need to be worked through with the Ministry of Health. |
| **Other options (not currently a budget bid)** | |
| **Public Transport fare reductions to all** (non-targeted) | Reducing public transport fares to all, in a non-targeted way, would be administratively simple and offer many households living cost relief. Those living in rural areas or with living patterns and work schedules not well-aligned to public transport timetables are less likely to benefit. Progressing this option would require Crown funding and would significantly reduce the value proposition of Community Connect and would have immediate implications for the Auckland pilot starting in July.<br><br>The costs of implementing this initiative is roughly the foregone fare revenue. Total national public transport fare revenue per year has been between $200-250 million over the last two financial years. Prior to covid-19, fare revenue was about $315 million in 2018/19. It is possible 'free' fares could increase public transport patronage (which has reduced due to COVID-19) but reduce walking and cycling. Any significant uptake in public transport could require capacity improvements, which would have a cost. If capacity improvements do |

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| | not occur service quality could deteriorate. Evidence suggests the quality of public transport is critical to uptake. |
| Direct form of support to regional councils (credit on HOP or Snapper Cards) | Administratively complex version of Community Connect and public transport fare reductions to all. The Ministry of Transport would advise to prioritise Community Connect and public transport fare reductions over this option. |