“Cash for Clunkers” – Henry to the rescue

The Commonwealth’s cleaner car rebate scheme (better known as “cash for clunkers”) may fall victim to budget cuts. As an environmental initiative it is an extremely expensive way to reduce CO_2 emissions. To keep faith with the electorate the Government would do well to integrate its best elements into an interim reform of motor vehicle taxes, incorporating the principles of the Henry Review, which would use restored real levels of fuel excise to finance elimination of state taxes, particularly stamp duties on new vehicles, which discourage people from upgrading their vehicles.

One of the Government’s election promises was a scheme designed to remove 200 000 older passenger vehicles from the roads to be replaced with new, more fuel-efficient vehicles. This scheme, budgeted to cost $394 million over four years, involves a $2000 rebate for purchase of a new vehicle.

It has been deferred to allow design of proper delivery mechanisms. Few people would be disappointed if the scheme were scrapped altogether. Only 1.3 percent of Australia’s 16 million vehicles would be eligible for the rebate.[1] To qualify a vehicle must be made before 1995 (i.e. 16 years or older by the time the scheme is implemented), and the replacement car must have a Green Vehicle Guide greenhouse rating of six or higher – generally a small to medium-sized passenger car.

Few people would qualify for the program. To benefit, one must be disposing of a car worth less than $2 000, and buying a new car – A Hyundai Getz at $13 000 is around the cheapest vehicle available.

Not many people would fall into that category – so poor as to be owning a car worth less than $2000 but able to buy a new car. The beneficiaries would seem to be young people with their parents’ hand-me-downs, or who are moving from education to employment. (As a university lecturer, however, my observations of campus car parks is that the only clunkers belong to academic staff.)

The scheme would be useless to poorer people living in the country, such as indigenous people owning ancient Holdens or Land Cruisers, for even in the unlikely event that they could afford a new car, there are few vehicles with a high greenhouse rating which are suitable for outback roads.

And the scheme would apply only to passenger cars, not to commercial vehicles. Australia’s fleet of commercial vehicles is old, and old diesel engines contribute not only to CO_2 emissions, but also to deadly local particulate pollution.

The environmental benefits of the scheme would come at high cost; the Government estimates a reduction of CO_2 of a million tonnes. With a budget of $400 million over the program’s lifetime that’s expensive – $400 a tonne! There would also be some road safety benefits, and some equity benefits in terms of lower fuel costs.

---

1. At the end of 2009 there were 16 million registered vehicles in Australia, of which 12 million were passenger vehicles.

It is hard to see many benefits for the domestic automobile industry, which is generally under-represented in the low-price-high-efficiency vehicle mix.

Yet, in light of the political reaction to broken promises in general and to the abandonment of the CPRS in particular, the Government would be reluctant to scrap it.

A face saver, with better outcomes, would be to make a first step towards road user charging as recommended by the Henry Review. The Review was in favour of reducing fixed charges on motor vehicles – stamp duty, registration and third party insurance – and replacing these with charges more in line with the externalities associated with vehicle use, those externalities being pollution, congestion and road use.

Comprehensive road user charging, as recommended by Henry, is still some years off technologically, but as a first step there could be a significant amount of revenue raised through raising the fuel excise, which is presently 38.143 cents a liter, and has been frozen at that level since the Howard Government abolished its indexation in 2001.

If the fuel excise were now to be restored to real 2001 levels, it would be raised by 12 cents, yielding revenue of around $4.0 billion a year – a figure dwarfing the cash-for-clunkers average expenditure of $100 million a year.[2]

To put that figure into perspective, it would be enough to provide almost a $4000 rebate to *every* new vehicle sold in Australia – passenger or freight – based on annual sales of 1.04 million vehicles.[3]

It would be more than enough to pay the states to remove entirely the stamp duty on new vehicles, which is around $1000 for a medium-priced passenger vehicle and considerably more on high-price and commercial vehicles – averaging around $2000 a vehicle, and which currently raises around $2.0 billion in state government revenues.

The additional $2.0 billion of excise duty left over after the abolition of stamp duties could almost halve ongoing registration fees, which presently raise around $4.4 billion in state revenues.[4] In a country where almost every adult owns a motor vehicle, registration fees are virtually a poll tax – one of the most regressive forms of taxation. And they apply regardless of distance travelled.

These are gross figures, and the purpose of this paper is to point in the direction of a practical, revenue-neutral reform. (And to point out that half of the cash for clunkers payments would be absorbed by state stamp duties.) There are ways to shape such a tradeoff which are more elegant than simply abolishing stamp duties and halving registration fees. Registration fees, for example, could be shaped in line with vehicle greenhouse ratings.

Rather than applying all the $2.0 billion to registration fees some of the funds could be used to keep aspects of the cash for clunkers scheme. A general abolition of stamp duty goes half

---

2. The CPI over this period has risen from 132.7 to 173.3, a rise of 31 percent, which would bring the excise rate to just under 50 cents. At 38.143 cents the excise raises $13.2 billion a year. A rise of 30 percent would raise an additional $3.96 billion. This figure ignores the likely price elasticity effect, which would reduce revenue, but it also ignores the offsetting GST effect, which would apply to that proportion of fuel sales destined for final consumption rather than business inputs.

3. Comprising 0.59 million passenger vehicles, 0.23 million sport utility vehicles, and 0.22 million other vehicles over the 12 months to September 2010.

4. In 2008-09 states raised $2.03 billion in stamp duties on registration, and $4.43 billion on registration fees.

way to the cash for clunkers promises – without the restrictions on vehicle type. There could still be a separate scrap payment of $1000 for old vehicles, with protection against rorts such as retrieving wrecks from backyards. (The aesthetic problem of car bodies which decorate our country towns needs to be addressed with specific “clean up” programs, rather than as a by-product of a cash for clunkers scheme.)

Such a proposal could be criticised for pre-empting more general carbon pricing or road user charging policies. But, politically, it would allow the Government to keep the cash for clunkers scheme, while giving effect to two important tax reform principles – charging for vehicle use rather than ownership, and compensating for costs associated with greenhouse abatement while retaining market-based incentives for CO_2 reduction.

In raising the cost of vehicle use, such a change in motor vehicle taxes would help reduce congestion costs (which the cash for clunkers scheme does not do) and, because it need not be restricted to passenger vehicles, it could have wider environmental and safety benefits. Because so many of Australia’s urban roads are used at full capacity, even small reductions in vehicle use can have significant private benefits in travel time and environmental benefits in terms of more efficient fuel use associated with freely flowing traffic. State governments could defer road widening projects, diverting the funds so saved into other road and public transport projects.

Another benefit is that it could be packaged with reforms to fringe benefits tax. Specifically the provisions in FBT concessions that encourage motor vehicle use could be withdrawn. The privileged FBT position of motor vehicles was intended, in part, to support the motor vehicle industry. A reduction in stamp duty is a much more direct means of achieving this end, without the distortion of incentives to clock up 25 000 or 40 000 km of annual vehicle use to qualify for FBT concessions.

A 12 cent rise in excise (translating to a 13 or 14 cent pump price rise once GST and profits are included), in itself, would not be popular, but if it can be linked to benefits of cheaper new vehicles, lower registration fees, less congested roads, and a contribution to reducing greenhouse pollution it should be sellable. A total tax of 55 cents a liter (50 cents excise, 5 cents GST) is still well below the level of fuel taxes in European countries.

There would be a case for relief for people in remote regions; they have few options for transport, and while they contribute to CO_2 pollution, they do not contribute to harmful local pollution or to congestion. (A reading of the Henry Review suggests comprehensive road user charging would separate out the costs of pollution, congestion and road provision.) Such relief could be based on existing zone rebate regions.