The fossil fuel subsidy myth

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Executive Summary

Over the last six years, the phrase ‘fossil fuel subsidy’ has been used by environmental campaigners to demonise the mining industry and call in to question the economic viability of Australia’s coal, oil and gas companies.

The claimed cost of these ‘fossil fuel subsidies’ in Australia depends on the source, but typically ranges from $3 billion to $12 billion per year, or even up to $39 billion per year in one estimate of the ‘social cost of carbon.’

However a critical examination of each claim reveals that these are not fossil fuel subsidies at all.

An energy subsidy is a payment, or other measure, that reduces prices below the true market price.

Energy subsidies, like all subsidies, distort the natural flow of investment, demand and supply in markets, and should not be supported.

However, while there are many governments around the world that set fuel prices, and do so well beneath the supply or true market costs, Australia’s is not one of them.

The refund of overpaid taxes is not a subsidy.

A tax deduction for the cost of a business input claimed by a company that happens to be in a fossil fuel business is not a fossil fuel subsidy.

The abolition of a tax is not a subsidy.

The campaign by environmentalists against mining and fossil fuel companies is politically motivated and pays no regard to the contribution these companies make to taxation, export income, employment or to basic human needs such as electricity and food.

One of the most important organising principles in any society is that the law, including taxation law, applies equally to individuals and to individual companies.

If the product is legal and the company is legal then that company has the right to trade, employ people, pay its bills and claim legitimate business expenses.

The tax system exists to raise enough revenue to pay the government’s bills – it should not be used to pursue political vendettas.
The claims

The current fossil fuel subsidy debate began following the G20 Pittsburgh Summit in September 2009, where the assembled government leaders resolved to “rationalise and phase out over the medium term inefficient fossil fuel subsidies that encourage wasteful consumption”\(^1\) with countries asked to report back to the G20 with lists of domestic subsidies and strategies to remove them.

In response, the Rudd/Gillard Government and the Treasury Department examined domestic taxation laws and programs and concluded that Australia had no measures that fell within the scope of the G20 commitment given that fossil fuels in Australia were not subsidised and that taxation benefits available to fossil fuel companies were also available to other companies.\(^2\)

Unsurprisingly, the environmental lobby did not agree with this conclusion and began to compile hit lists of so-called ‘fossil fuel subsidies’ that it wanted to abolish.

Four of the main proponents of the fossil fuel subsidies in Australia are the Australian Conservation Foundation, Australian Greens, the Market Forces lobby group and the Australia Institute.

Since 2010, each of these bodies has produced a study that seeks to put a dollar amount on the level of fossil fuel subsidies in Australia.

Australian Conservation Foundation

The Australian Conservation Foundation (ACF) released *Giving with Both Hands*\(^3\) on 18 December 2014, an analysis which claimed that federal “handouts for the production and use of fossil fuels” would cost $47 billion over the next four years.

The ACF claimed that the four major components of these handouts were the:

- Fuel Tax Credit Scheme ($27.9b over four years);
- Concessional Rate of Excise on Aviation Fuel ($5.5b);
- Accelerated Depreciation Rules ($1.4b); and
- Removal of the Carbon Price ($12.5b).

This document also criticised the Abbott Government’s Emissions Reduction Fund (i.e. ‘Direct Action’) complaining that it “offers a cash incentive to undertake projects that will reduce pollution.”

*Giving with Both Hands* built on the ACF’s earlier work:

- The 2012 Pre-Budget Submission which claimed that accelerated depreciation for the oil and gas industries alone was worth $3.2 billion over five years together with removing fuel tax credit subsidies for transport and mining companies, phasing out aviation fuel tax breaks,

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removing aircraft tariff exemptions and repealing the petroleum exploration deduction was said to save an additional $18.098 billion (total $21.298 billion over five years)\(^4\)

- The 2011 *Drill Now, Pay Later* paper, which claimed that accelerated depreciation for the oil and gas industries alone represented a $6 billion subsidy over the six years from 2012 to 2018\(^5\); and
- The June 2010 *G20 and Fossil Fuel Subsidies* media brief which set out a total of twelve “producer and consumer support subsidies” worth a total of $7.7 billion per year. \(^6\)

On 29 April 2015 the ACF also released *Subsidising Big Coal: Handouts to Australia’s coal mining companies through the Fuel Tax Credits Scheme*. This pamphlet estimated that coal mining companies received $767 million in Fuel Tax Credits in 2012/13 and proposed a cap on the value of credits any company could claim.\(^7\)

**Australian Greens**

The Australian Greens released a proposal in 2013, *Ending Fossil Fuel Subsidies to the Mining Industry*\(^8\) to cut almost $14 billion in ‘fossil fuel subsidies’ over four years from 2013-14 by abolishing:

- Diesel fuel rebates (worth $8 billion over four years);
- Accelerated depreciation on exploration (worth $4 billion over four years); and
- Accelerated depreciation on assets (worth $1.85 billion over four years).

In 2014 the Greens released updated figures from the Parliamentary Budget Office, maintaining that the abolition of fuel tax credits, accelerated depreciation and exploration and prospecting deductions for the mining industry would save the Budget $13.05 billion over the next four years.

On 6 July 2015 Greens Senator Larissa Waters announced via a media release that the Greens wanted to impose a $2 per tonne levy on coal exports and that exempting mining companies from fuel taxes now cost taxpayers $3.3 billion per year. \(^9\)

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Market Forces

Online environmental lobby group Market Forces (affiliated with Friends of the Earth) also claims that fossil fuel subsidies are worth $10 billion per year and listed a total of twenty one separate items in its 2014 Pre-Budget Submission.10

These items include the Fuel Tax Credit Scheme, accelerated depreciation and concessional taxation on aviation excise as per above, as well as a number of others including employee fringe benefits tax exemptions for car parking, taxi travel, and car expenses.11

Australia Institute

In June 2013, the Australia Institute released Pouring More Fuel on the Fire, an update of earlier work on fossil fuel subsidies, claiming that the mining industry received $4.5 billion per year in subsidies and tax concessions from the Federal Government, up from $4 billion the previous year.12

The Australia Institute claimed that the major subsidies included:

- Fuel Tax Credits (for mining) $2.349 billion;
- Deductions for capital works expenditure $495 million;
- Exploration and prospecting deduction $550 million;
- Statutory effective life caps $400.5 million;
- Coal sector jobs package $218.8 million;
- R&D Tax Concessions $370.8 million;
- ‘Various Budget Outlays to Mining’ $110.8 million;

In June 2014 the Australia Institute also released Mining the Age of Entitlement13 which claimed that aggregate state government assistance to the mining industry represented $17.6 billion over a six year period.

Other group claims

The Climate Institute took a different approach in its September 2014 Counting All the Costs – Recognising the Carbon Subsidy to Polluting Energy paper which sought to put a price on the “social cost of carbon.”14

Its calculations found that:

Australia’s polluting energy sector benefits from an annual subsidy of $14-39 billion from the unpriced cost of climate damages on economic growth, environmental systems, health and security.15

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11 Ibid.
13 Australia Institute, “Mining the Age of Entitlement” June 2014, http://www.tai.org.au/content/mining-age-entitlement
15 Ibid
In May 2015 the International Monetary Fund (IMF) released a working paper How Large are Global Energy Subsidies which asserted, with much publicity at the time, that global energy subsidies were projected to be worth $5.3 trillion in 2015.\footnote{International Monetary Fund Working Paper, “How Large are Global Energy Subsidies?”, May 2015 https://www.imf.org/external/pubs/ft/wp/2015/wp15105.pdf}

To get to this figure, the IMF put a price on what is commonly regarded as energy subsidies (payments that ensure that consumers pay less than the market price) as well as so-called environmental costs, ranging from air pollution to traffic accidents, and the imposition of a consumption tax on energy.
Fossil fuel subsidy definitions

The International Energy Agency (IEA) describes an energy subsidy as:

Any government action directed primarily at the energy sector that lowers the cost of energy production, raises the price received by energy producers or lowers the price paid by energy consumers.  

This is also the definition of an energy subsidy that the IEA, together with the OECD and the World Bank, used as the backbone of their joint report prepared for the follow-up G20 Summit in Seoul in November 2010.

This report also used the IEA’s ‘price-gap approach’ to measure energy consumption subsidies, which seeks to compare:

“Final consumer prices with reference prices, which correspond to the full cost of supply or, where appropriate, the international market price, adjusted for the costs of transport and distribution.”

In other words, an energy subsidy is a payment, or other measure, that reduces prices below the true market price.

The IEA estimates that “the global value of subsidies that artificially lower end-user prices for all forms of fossil energy” was $548 billion in 2013, and has identified a list of 40 countries that subsidise fossil fuel use, with Iran, Saudi Arabia, India, Russia, Venezuela, Indonesia and the UAE the major culprits. Australia is not even mentioned.

Specific examples cited by the IEA include the Egyptian Government directly setting fuel prices below the cost of supply, the Indonesian Government setting the price for gasoline and diesel products below market prices, and the Nigerian Government setting the domestic prices of gasoline, kerosene, natural gas and electricity below the cost of supply.

In Venezuela government subsidies are said to have made petrol ‘cheaper than water and candy,’ and in Iran, while the government increased petrol prices by 40% in May, this only took them to around USD$0.36 per litre.

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19 Ibid.
20 Ibid.
21 Ibid.
The OECD’s *Taxing Energy Use 2015* publication has a useful summary of producer price subsidies in a selection of countries including Argentina, India and Russia.  

In a speech in May 2015 the head of the IEA noted that global fossil fuel subsidies had been gradually declining since 2012, listing a range of countries that had made progress, in particular Indonesia and Mexico.

However it is clear that there is no universally agreed definition as to what constitutes an energy subsidy.

In responding to the 2009 G20 Summit resolution, member countries were unable to agree on what constituted an energy subsidy and adopted their own definitions.

The IEA notes that the OECD “defines a subsidy in general terms as any measure that keeps prices for consumers below market levels, or for producers above market levels or that reduces costs for consumers and producers...” while also acknowledging that the OECD includes budgetary support and tax expenditures when measuring fossil fuel subsidy levels.

In a May 2012 paper for the Minerals Council of Australia, Sinclair Davidson gave a detailed explanation of the variety of definitions of a subsidy and of tax expenditure and examined some of the claims interest groups had made at that time.

While acknowledging that there is a difference of views on this issue, a common theme is to assert that a subsidy is something that artificially reduces the prices of a good below its true market price through price fixing or direct support for a company or industry.

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Assessment of alleged Australian fossil fuel subsidies

While there is no universally agreed definition of fossil fuel or energy subsidies, the examples of subsidies in Australia that are most commonly cited are the fuel tax credits scheme, accelerated depreciation, the excise on aviation fuel, and the tax deductibility of business car expenses.

For the purposes of this paper we will put to one side the assertions of the Climate Institute and the IMF which attempt to put a price on the ‘social cost of carbon’ and on every imaginable cost that could possibly arise from the use of energy or transport.

Fuel Tax Credits scheme

The primary target of the environmental lobby is the Fuel Tax Credits scheme, which allows part or all of the fuel tax component of the price of diesel or petrol paid by businesses, to be claimed back from the Australian Taxation Office.

Fuel tax in Australia exists primarily as a means to help fund roads by taxing the use of fuel in on-road vehicles.  

However, given that fuel is also used for off-road purposes (e.g. for machinery and heating), and is a business input, a tax credit for fuel use is available to Australian companies, along similar lines to the refund that businesses receive for the GST paid at each stage of their production process.

The diversity of business fuel use was illustrated by the Fuel Tax Credits Coalition in its March 2015 publication *Powering Regional Australia – the Case for Fuel Tax Credits*  which gave eighteen case studies of the use of diesel to power agricultural pumps and vehicles, maritime craft, mining operations and in some cases whole households, businesses and towns not connected to the electricity grid.

Australian Taxation Office (ATO) taxation statistics show that while the mining industry is indeed the largest individual industry sector claimant, it is in fact responsible for less than 37 per cent of the value of claims across all industries.  

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<table>
<thead>
<tr>
<th>Industry</th>
<th>Value of Fuel Tax Credit Scheme Claims Paid in 2013-14 ($m)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture, Forestry and Fishing</td>
<td>689.9</td>
</tr>
<tr>
<td>Mining</td>
<td>2,157.5</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>176.5</td>
</tr>
<tr>
<td>Electricity, Gas, Water and Waste Services</td>
<td>109.5</td>
</tr>
<tr>
<td>Construction</td>
<td>418.3</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>142.9</td>
</tr>
<tr>
<td>Retail Trade</td>
<td>22.8</td>
</tr>
<tr>
<td>Accommodation and Food Services</td>
<td>9.5</td>
</tr>
<tr>
<td>Transport, Postal and Warehousing</td>
<td>1,154.6</td>
</tr>
<tr>
<td>Information, Media and Telecommunications</td>
<td>647.7</td>
</tr>
<tr>
<td>Financial and Insurance Services</td>
<td>99.1</td>
</tr>
<tr>
<td>Rental, Hiring and Real Estate Services</td>
<td>45.7</td>
</tr>
<tr>
<td>Professional, Scientific and Technical Services</td>
<td>412.8</td>
</tr>
<tr>
<td>Administrative and Support Services</td>
<td>29.0</td>
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<tr>
<td>Public Administration and Safety</td>
<td>99.4</td>
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<tr>
<td>Education and Training</td>
<td>5.8</td>
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<tr>
<td>Health Care and Social Assistance</td>
<td>2.1</td>
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<tr>
<td>Arts and Recreation Services</td>
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<tr>
<td>Other Services</td>
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</tr>
<tr>
<td>Other</td>
<td>92.4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>5,706.1</strong></td>
</tr>
</tbody>
</table>

Fuel is a business input, just like labour, materials or finance, and requiring businesses to pay fuel tax at each stage of the production process would represent double taxation, and therefore higher prices for the final consumer.

The undesirability of paying taxes on top of taxes is well understood – the GST operates the same way - and it is for this reason, that the ATO refunds the applicable fuel tax credit to Australian businesses.

Fuel tax credits are merely a refund for businesses that have paid too much tax.

Given that this is a refund for taxes paid on the cost of doing business, fuel tax credits are not a subsidy. That they apply to all businesses, and not just those involved in mining or fossil fuels, also clearly demonstrates that this can’t reasonably be described as a fossil fuel subsidy.

**Accelerated depreciation**

Depreciation is a commonly accepted taxation principle in Australia where the value of an item with a limited shelf life that is purchased to assist an individual or business to earn an income is able to be written off against taxable income.

Accelerated depreciation, also known as statutory effective life caps, allows businesses to write off certain investments faster.

An article from the April 1954 edition of the *IPA Review* illustrates how accelerated depreciation had long been a feature of the USA’s tax system noting that “American industrialists were constantly
engaged in installing the latest mechanical devices and in replacing existing equipment with better equipment” and that “they did not hesitate to scrap machinery which had been outmoded by new developments.”

In other words, accelerated depreciation is an important driver of national productivity and innovation by encouraging businesses to continually invest in newer equipment.

Similar to the environmental lobby’s claims about fuel tax credits, accelerated depreciation is not something that is only available to the mining industry – it is also available to other industries including aircraft, agriculture and transport, a point even acknowledged by the Australian Conservation Foundation.

Interestingly, the Greens do not appear to have a problem with the changes to accelerated depreciation for small business announced in the 2015 Federal Budget, which tends to expose their reasons for opposing accelerated depreciation for the mining industry as politically motivated.

Accelerated depreciation is a taxation benefit that allows eligible businesses to claim back the cost of certain business inputs, in other words on the cost of doing business.

It does not apply solely to the mining or fossil fuels industry and is therefore not a fossil fuel subsidy.

**Concessional rate of excise on aviation fuel**

As of 1 September 2015, the standard fuel excise rate in Australia is 39.2 cents per litre, but the excise on aviation fuel is only 3.556 cents per litre.

That aviation fuel is not taxed as highly as other fuels reflects the significant costs of operating aircraft over a decentralised island continent located far away from tourism and business markets.

It does not solely apply to aircraft operated by the mining industry, and is not a subsidy as it merely reflects the fact that the government chooses not to tax aviation fuel as highly as other fuels given the significant distances flown by aircraft over Australia.

This practice is also in line with the multilateral International Convention on Civil Aviation (the 1944 Chicago Convention) which exempts fuel used for international flights from tax given the potential for airlines to source their fuel from other jurisdictions.

Describing a decision not to tax something at a higher rate as a subsidy is an argument that is regrettably finding its way into other policy areas as well, such as superannuation and income tax. Following this logic to its extreme, the only way that all individuals and businesses could avoid being accused of being subsidised by government is to pay 100 percent of their income in tax.

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The concessional tax rate on aviation fuel would likely still apply if it were made from biodiesel. It does not solely apply to the mining or fossil fuels industry and is therefore not a fossil fuel subsidy.

Abolition of the carbon tax and introduction of the Emissions Reduction Fund

The Australian Conservation Foundation’s 2014 paper, 37 which claimed the existence of $47 billion of fossil fuel subsidies over 4 years, counted the abolition of the carbon tax as representing an “implicit subsidy” of $12.5 billion over four years to fossil fuel companies.

Similarly, the ACF implies that the Abbott Government’s Emissions Reduction Fund, which the ACF claims will cost $1.1 billion over four years (though it didn’t include this in its $47 billion calculation), undermines the principle of ‘polluter pays.’

It is ironic that the green movement claims that an initiative that actually pays companies to permanently end their carbon dioxide emissions is a cost, preferring a complicated tax transfer system where consumers pay higher prices for their goods.

The abolition of a tax is not a subsidy – it is the abolition of a tax, even if it is needed by the ACF for over 25% of its fossil fuel subsidy calculations.

Fringe benefits tax, GST and other subsidies

To their credit, the Australian Greens and Australian Conservation Foundation have not added items such as the fringe benefits tax exemption for employees travelling to work in a taxi or GST exemptions for domestic air travel as part of a wider international arrangements to their own tally of ‘fossil fuel subsidies,’ but they have been cited by Market Forces in its 2014 Pre-Budget Submission. 38

While it is not clear whether Market Forces is referring only to the employees of fossil fuel companies, or to employees of all companies whose work appears to incorporate the use of fossil fuel, examination of the most recent Treasury Tax Expenditures Statement suggests the latter. 39

Expenses incurred by businesses or their employees in the course of ordinary business are not fossil fuel subsidies, they are legitimate business deductions for expenses incurred complying with employment obligations.

The same argument applies to the Australia Institute’s claims of a $495 million mining industry subsidy in 2012-13 for capital works expenditure and $370 million in 2011-12 for Research and

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Development Tax Concessions. Development Tax Concessions. Both apply to eligible companies in all industry sectors, and are not fossil fuel or mining industry subsidies.

In fact, there is a recurring theme in many of these analyses, where groups add up all of the potential costs (including highlighting the mining industry’s share of tax concessions available to all, and the additional capital investments that precede increased production) but ignore the ongoing increases in tax or other revenue that result from this research and capital investment.

The Australia Institute’s 2014 publication Mining the Age of Entitlement, which claimed $17.6 billion of state government fossil fuel subsidies, was comprehensively debunked by both Henry Ergas and Castalia Strategic Advisors, who pointed out how the Australia Institute incorrectly labelled commercial investments in infrastructure as ‘subsidies’ while largely ignoring asset user charges, increased asset revenue and proceeds from asset sales.

For example, Henry Ergas cited $3.7 billion spent on Queensland’s road rail network which was later sold for $4.6 billion. Castalia noted that the Public Trading Enterprises that operate these assets are expected to achieve commercial rate of return and actually pay dividends to government.

Economic value of mining and fossil fuel companies

Environmental campaigners also choose to ignore the significant level of company tax and resources taxes paid by mining companies.

The Australian Taxation Office has released data showing that mining companies paid $13.6 billion in net income (i.e. company) tax in 2012-13, second only to financial and insurance services companies ($20.2 billion), which is significantly more than all other industry sectors.

Mining companies also paid $16.6 billion in franked dividends in 2012-13 and $25.8 billion in wages and salaries expenses.

In July 2014 Deloitte Access Economics estimated that the minerals sector would pay $21.96 billion worth of company tax and royalties in 2013-14. While this figure includes taxes paid by non-fossil fuel mining companies including iron ore and gold, it gives a good sense of the contribution of mining to the Australian economy.

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44 Ibid
The value of export earnings from resources and energy commodities was recently estimated at $174 billion in 2014-15, and Australian mining sector employment in the June quarter 2015 some 229,156 people. 46

Even if one were to accept some fossil fuel subsidy claims, they would be dwarfed by the contribution of mining and fossil fuel industries to taxation income, employment and Australia’s balance of trade, as well as to electricity, gas and petrol supplies for heating, cooling and food.

Conclusion

When each claim is looked at critically, it is clear that there is no such thing as ‘fossil fuel subsidies’ in Australia.

An energy subsidy is a payment, or other measure, that reduces prices below the true market price.

Energy subsidies, like all subsidies, distort the natural flow of investment, demand and supply in markets, and should not be supported.

While there are many governments around the world that do set fuel prices, and do so well beneath the supply or true market costs, Australia’s is not one of them.

Environmental organisations are highly selective with what they term a ‘fossil fuel subsidy’ – sometimes referring to a taxation benefit available to many industries (like accelerated depreciation or research and development tax incentives) and at other times a tax concession for the use of a particular fossil fuel (like the aviation fuel rebate).

Sometimes the abolition of a tax is described as a fossil fuel subsidy (i.e. the carbon tax) while at other times a lower taxation rate (aviation fuel excise vs gasoline excise) is claimed as a subsidy.

Fuel prices in Australia are not set by the government, and tax deductions or credits that are available to mining or fossil fuel companies are typically available to other businesses or producers.

The Productivity Commission, which has an established track record of opposition to industry assistance, in its *Trade and Assistance Review 2013-14* found that “the estimated effective rate of assistance from tariff and budgetary assistance for mining is negligible.” 47

It is clear that the campaign by environmentalists against mining and fossil fuel companies is at its heart political.

In its 2013 *Ending Fossil Fuel Subsidies to the Mining Industry* statement the Australian Greens proposed removing the diesel fuel rebate for the mining industry but said that “other industries such as agriculture will continue to receive the rebate.” 48

It is also interesting that the Greens claim to support the changes to accelerated depreciation for small business announced in the 2015 Federal Budget but oppose its use by mining companies.

The Australian Conservation Foundation wasn’t content to run with its December 2014 estimation of the total $27.9 billion cost of the fuel tax credit scheme, and subsequently released an additional pamphlet in April 2015 highlighting the scheme’s use by coal mining companies. This document

48 Australian Greens, “Ending Fossil Fuel Subsidies to the Mining Industry”, 2013 pamphlet,
claimed that “the largest coal mining companies operating in Australia have their fuel subsidised by the taxpayer while they mine a highly polluting substance.”

There is a consistent theme to the rhetoric of these organisations that opposes all mining activity.

This campaign tallies up every imaginable cost to the budget that can be attributed to the mining industry, however loosely, but pays no regard to the contribution mining makes to taxation, export income, employment or to basic human needs such electricity and food.

It also includes the cost of assets or any generally applicable taxation benefits to the construction of assets as a subsidy – which is itself wrong – while conveniently ignoring any income later derived from these assets, even if an income stream runs for decades.

Describing business inputs claimed by the mining industry as a fossil fuel subsidy would be like describing taxation benefits claimed by companies headquartered in Queensland for example as ‘Queensland subsidies’ or personal income tax deductions for self-education expenses for people living in Victoria as ‘Victoria subsidies.’

If the Greens and other environmental campaigners were consistent about subsidies, then they would argue to impose a GST on fresh food, given that it could be argued that under current laws people who buy fresh food are being subsidised by those who buy takeaway.

One of the most important organising principles in any society is that the law, including taxation law, applies equally to individuals and to individual companies.

If the product is legal and the company is legal then that company has the right to trade, employ people, pay its bills and claim legitimate business expenses.

The tax system exists to raise enough revenue to pay the government’s bills – it should not be used to pursue political vendettas.

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