Australia's tax policy: How are passenger vehicles taxed?

With cities designed for motor vehicles and a comparatively low usage of public transport [1], exacerbated by the COVID-19 pandemic, Australians continue to purchase and rely on cars for their commutes. As of 31 January 2021, there were 20.1 million registered motor vehicles (which includes cars, trucks, motorbikes, tractors, caravans and trailers) in Australia [2]. Of these, 14.9 million (73.7 per cent) were passenger vehicles. Passenger vehicles include both private and public (e.g. taxis, hire cars) vehicles intended for the carriage of passengers and designed to seat no more than nine persons (including the driver) [3].

Why should passenger vehicles be taxed? What taxes are imposed on consumers when purchasing and maintaining a private vehicle in Australia? How could these tax policies be improved?

Why should passenger vehicles be taxed?

Funding of public roads and other infrastructure, which support passenger vehicles, has proven to be a significant and ongoing expense for governments. Taxation, for the purpose of funding this public infrastructure, should be equitable by ensuring those who use the roads and infrastructure more are taxed accordingly; one approach to achieve this is via a user-pays model.

Taxing passenger vehicles can also offset the negative externalities generated by their use **[see our Tax Fact #4, "Good tax policy – Taxing negative externalities"]**. These negative externalities include air pollution, traffic noise pollution, congestion and traffic accidents [4]. Taxation of passenger vehicles for this purpose is done to a limited extent in Australia.

How are passenger vehicles taxed in Australia?

In general, there are three types of taxes that apply to passenger vehicles: taxes on acquiring the vehicle, owning the vehicle, and using the vehicle.

Taxes on acquiring a passenger vehicle

When transferring ownership of a passenger vehicle or at its initial purchase point, one or more of the following taxes may apply:

1.Goods and Services Tax (GST) – GST, a Commonwealth tax with revenue distributed to the states and territories, is applied on passenger vehicles in the same way it is applied on all applicable goods – at a flat rate of 10 per cent. As is the case with the disposal of privately owned assets, GST is not payable on the private sale of a passenger vehicle [5].

2.Stamp duty – stamp duty (also named motor vehicle duty in some jurisdictions) is a tax levied by state and territory governments paid when transferring ownership. It is applied on all transactions involving passenger vehicles, including private sales. It can be considered the once-off cost of registering a passenger vehicle or transferring the registration of a passenger vehicle. Rates of stamp duty differ across jurisdictions and are generally levied based on the market value of the vehicle.

3.Luxury Car Tax (LCT) – LCT is a Commonwealth tax levied on passenger vehicles over a certain value. It is imposed on all sales of passenger vehicles that are two years old or less, at a rate of 33 per cent on the GST-inclusive value of the vehicle above the LCT threshold. These thresholds are, for 2021-22, $79,569 for fuel-efficient vehicles (fuel consumption that does not exceed 7L/100km) and $69,152 for all other vehicles [6]. LCT is estimated to raise $800 million of revenue in the 2020-21 financial year, and $2.54 billion in the four years to 2024-25 [7].

Taxes on owning a passenger vehicle

The following taxes are also levied at the point of purchase or transfer of ownership and additionally require an annual renewal:

1.Registration - at the initial purchase point or transfer of ownership, an ongoing, annual registration fee is charged by the relevant State or Territory Government in which the vehicle is being registered. Registration identifies a particular vehicle and its owner, including crucial details related to the vehicle (such as engine, weight, number of passengers, and vehicle make and model). Registration allows for the vehicle to be driven legally on public roads.

2.Taxes on compulsory third party (CTP) insurance – CTP insurance is compulsory in all states of Australia, and premiums may include taxes such as stamp duties on insurance and GST. In some jurisdictions, CTP is included in the vehicle's registration fee. If the consumer wishes to take on additional insurance, taxes are also levied on those premiums.

Taxes on using a passenger vehicle

Taxes also exist on the usage of passenger vehicles – namely through the purchase and subsequent consumption of fuel. An ACCC report found that taxes can represent as much as 38 per cent of the retail petrol price [8].

1.Fuel excise – fuel excise is a Commonwealth tax levied on petrol, diesel and excisable fuel products. Excise duty rates differ based on the particular fuel, however most are currently set at a rate of 44.2 cents per litre [9]. Revenue has declined recently due to improvements in vehicle efficiency, including zero- or low-emissions vehicles. Industries that do not use public roads, such as the mining and agriculture sectors, receive rebates on the fuel excise they pay [10]. Excise revenue from petrol, diesel and other fuel products (all vehicles and before refunds and drawbacks) is estimated at $21.07 billion in 2021-22.

2.GST – GST is levied on fuel products at a flat rate of 10 per cent. It is calculated on the price of fuel after including fuel excise.

3.Road-user charge – a road-user charge is a tax that involves charging vehicles per unit of distance travelled. A road-user charge has been introduced in Victoria, with New South Wales and South Australia to begin administering similar schemes from 1 July 2027 or when electric vehicles make up 30 per cent of total passenger vehicle sales in the respective state (whichever comes earlier). A road-user charge is intended to make up for lost revenue from fuel excise as green vehicle use increases. Victoria charges 2.5 cents per kilometer for electric and hydrogen vehicles, and 2.0 cents per kilometer for plug-in hybrid electrical vehicles [11]. Payment is based on an odometer declaration at the start and end of a registration period or transfer of vehicle.

How could the taxation of passenger vehicles be improved?

When considering the taxation of passenger vehicles, Governments must consider many factors such as revenue, resource allocation, income distribution, the environment, administrative simplicity and efficiency [12].

Relative to other countries, Australia could do a better job of aligning passenger vehicle taxes to offset negative externalities from passenger vehicle use. For example, stamp duty and annual registration taxes linked to CO2 emissions or fuel consumption have been put in place across the European Union due to mandatory CO2 emissions reduction targets for new passenger vehicles. This policy idea is strengthened as stamp duties are generally considered an inefficient tax. In Australia, only the ACT has linked one of its motor taxes to emissions under the Vehicle Emission Reduction Scheme.

Such policies can help shift purchasing priorities towards greener vehicles, which offset some negative externalities (such as pollution and noise), but not all. Traffic congestion is one of these unsolved externalities, which could be combatted with congestion charging – a system of surcharging imposed to reduce congestion. The Grattan Institute argues that a congestion charge in Australian capital cities could mean 40 per cent fewer vehicles entering CBDs in the morning peak, and speeds up to 16 per cent faster on roads in the CBD and up to 20 per cent faster on sections of major arterials leading into CBDs [13].

The Commonwealth could also establish a nationally consistent model for road-user charging to account for a fall in fuel excise revenue as green vehicle use increases. This will ensure a particular state is not seen as a 'tax haven' for green vehicles and will ensure that fuel excise, a Commonwealth tax, is adequately replaced. This is of particular importance since renewable energy will become cheaper as technology develops, decreasing the cost of using electric vehicles, increasing their use, further reducing fuel excise receipts, and exacerbating congestion [14].

Finally, the Henry Tax Review argued for abolition of the luxury car tax (LCT) since its narrow tax base renders it inefficient [15]. In addition, it is neither horizontally nor vertically equitable **[see our Tax Fact #21, "Dimensions of tax fairness"]**, as it taxes people with a preference for relatively expensive vehicles regardless of wealth or income.

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