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HOT CLOTHING COMPANY PTY LTD

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SUBMISSION TO THE ENQUIRY ON - 'RULES OF ORIGIN UNDER THE AUSTRALIAN – NEW ZEALAND CLOSER ECONOMIC RELATIONS TRADE AGREEMENT' –

Dear Sir,

We understand that submissions are invited from the 'public' to assist the Productivity Commission with their research study into the rules governing ROO under CER as it presently stands.

Our experience involves our Company's export to NZ of women's clothing, which has been 100% Made in Australia.

We have been and still are as at today, being charged duty at 19% on the invoice value by NZ Customs when the goods enter N.+Z.

We are a typical clothing 'fashion' house. On our premises in Sydney we design the clothes, we make the patterns, we make the salesman sample ranges, we purchase fabric and we cut the fabric 'in-house'. Without all of these activities it would be impossible to make the clothes. This is all essential expenditure. We contract out to specialist 'making' factories the actual sewing up of the final product. In addition to the sewing-up of the garments this includes applying the labels, zippers, buttons and swing tags etc.

Therefore all of the overhead and manufacturing cost of the goods is incurred in Australia. Under overheads we include rent on the premises and insurance etc.

Under the intent and spirit of CER, our goods should qualify for duty free into New Zealand.

Due to a 'flaw' or 'loopholes' in the way the original CER Agreement and legislation was drafted, an absurd interpretation is being applied by NZ Customs in two critical respects.

1. Unless all of the actual costs our goods are incurred on our premises, not withstanding that they are incurred in Australia as explained above (see 'contract out' etc) then it is being determined that these costs do not count towards the 50% local content qualifying criteria. This is absurd.

2. Secondly, only those costs incurred in the factory which is defined as 'the last place in the process of manufacture', can be included as part of the 50% cost of the local qualifying content. This is also patently ridiculous and not in the spirit and intent of CER.

There is a third scenario and that is where the fabric itself is imported. This cost is therefore not a local, Australian cost and is presently excluded. We feel this is wrong and the law should be changed – because we substantially alter or change the nature of a roll of fabric into clothing. Therefore 'imported components' should qualify as local costs.

We are further advised by NZ Customs that if we have a whole roll of plain fabric and we get it printed on, which we often do (in Australia) at substantial cost, that this cost is not an 'allowable' qualifying cost. The reason given is that this process is (merely) a value added process i.e. it merely adds value to the fabric, but is not a 'cost of manufacture'. This is not fair as it is a manufacturing cost. The same also applies to embroidery. We often have expensive embroidery done on our clothing on the fabric panels *after* it is cut, but before it is sewn up into a garment. We are told by NZ Customs that this is not an allowable qualifying cost as it is deemed to be merely adding value to the fabric and is not a manufacturing cost! This is wrong as it *is* a manufacturing *cost* and the process is done in Australia.

A further complication has been added by NZ Customs, towards allowable complying Australian costs in respect of the goods we have manufactured by contract outside our premises, but still in Australia. That is, that we must deduct the 'profit component' that our contractor makes (and charges us) because that item is not an Australian cost of the goods!

We then have to become involved in investigating the profit our contractors make in their own factories. This is a whole new cost accountants exercise, plus we are asking to be privy to someone else's confidential business, which we have no legal right to do. This becomes impossible.

The whole ANZCERTA Agreement must be re-written as a matter of urgency. The CER Agreement is between two countries; Australian and New Zealand. Both countries sign it, yet it is being interpreted and applied completely differently in NZ compared to Australia. The circumstances we have outlined above are being applied by New Zealand yet Australian Customs say this is completely wrong and not how the Act/Agreement is meant to work and of course they are correct.

It is as if a certain 'mind-set' prevails in New Zealand and the attitude is to try and find every loophole and angle in the wording to penalise the Australian Clothing Trade and raise revenue for New Zealand. They cannot or will not see the 'Bigger Picture' and the overall reason for the existence of CER.

We have been advised in several letters from the NZ Minister for Trade, the Hon. Jim Sutton and the Australian Minister for Trade, the Hon. Mark Vaile, (both of whom have been exceptionally helpful and understanding), that the foregoing 'modis-operandi' of NZ Customs is wrong and will be fixed. We have also received a personal letter from Helen Clark, the Prime Minister of NZ, expressing sympathy with our situation.

We have been fighting this injustice since July 2002 and everyone (both governments) agree (except NZ Customs) that the Agreement is being interpreted and applied incorrectly by NZ Customs. Unfortunately the way the system works, no one can issue a directive to another Department i.e. to NZ Customs; to correct the situation. It has been referred to a Committee of Enquiry such as the present one; the subject of this submission.

Specifically, we now refer to New Zealand Customs Service 'FACT SHEET' (20) ANZCERTA – Rules of Origin (R.O.O.) – Rules Governing Entitlement to Preferential Rates of Duty for Trans-Tasman Trade.

Page 3. Item No. 6 **"Last Process of Manufacture"**
"Where manufacture has occurred in Australian and New Zealand it is necessary that the last process in the manufacture of the goods must be performed in Australia or New Zealand, as the case may be".

This is OK. So far, so good; but then …….

Page 3. Item No 7 **"The 50 Percent Rule – Customs"**
"What is the setting for the 50 percent and who must incur it? The scheme of current Australia/New Zealand, legislation is built around 'the factory', which is defined as the place where the last process in the manufacture of the goods, was performed. It is important to understand that the manufacture is defined as the person undertaking the last process in the manufacture of the goods"….. etc.

Also 7.3 "All expenditure forming part of the 50 percent requirements must be incurred by the manufacturer of *the goods*".

- The above item No 7 is the first big problem in the present legislation and must be changed, as it gives the opportunity for the present narrow interpretation (by NZ Customs) to say that only the costs of '*the factory'* i.e. 'the last process of manufacture' applies. THIS IS WRONG AND MUST BE CHANGED, to avoid any ambiguity and be left open to any interpretation.

***THE PLACE* OF MANUFACTURE SHOULD BE DEFINED AS *'THE COUNTRY'*, NOT *'THE FACTORY'*.**

- Next, imported goods/components i.e. raw materials such as fabric should be an allowable local cost under R.O.O. provided they are incorporated into the manufacture of the goods and their 'finished' nature is different than the 'form' in which it was imported. eg. a roll of fabric made into clothing. Where the fabric is very expensive it represents a larger per-centage of the total cost of the garment and despite the fact that garment is 100% made in Australia, when we exclude the 'imported' fabric cost we sometimes do not reach the 50% qualifying cost threshold.

- Overheads, both Direct and Indirect where necessarily incurred to produce the product in Australia must be an allowable cost.

Page 3 Item 7. **<u>"How is the 50 percent calculated?"</u>**
……..…… "It is important to note that the 50 percent calculation excludes the profit of the manufacturer who produces the goods on which preference is claimed….. etc".

- Where we the principal, contract out some of the manufacturing process, we cannot determine the profit of the manufacturer. We have no legal right to these figures and this so called manufacturers 'profit' should be a qualifying cost to us the principal. The full cost of the contract makers invoice to us should qualify as local cost.

Where any doubt ever exists in interpretation of the legislation, the over-riding criteria must always be to revert back to the intent and spirit of the legislation.

Yours Faithfully,

Jonathon D. Ind
Director