Australian Government
Australian Customs Service

Customs House
5 Constitution Avenue
CANBERRA ACT 2601
Telephone: (02) 6275 6462
Facsimile: (02) 6275 6377

Mr Paul Gretton
Acting Assistant Commissioner
Productivity Commission
PO 80
BELCONNEN ACT 2616

PRODUCTIVITY COMMISSION INTERIM RESEARCH REPORT
RULES OF ORIGIN UNDER THE AUSTRALIA-NEW ZEALAND CLOSER ECONOMIC RELATIONS TRADE AGREEMENT

The Australian Customs Service (Customs) would like to thank the Productivity Commission (the Commission) for the research it has undertaken in preparing the Interim Report on Rules of Origin under the Australia-New Zealand Closer Economic Relations Trade Agreement (the Interim Report).

Customs would also like to thank the Commission for the opportunity to respond to the Interim Report's findings and recommendations. Customs' response is as follows:

Interim Recommendation 1:

***The following changes be made to address some of the day-today shortcomings of the current CER Rules of Origin (RoO)**:*

- ***The 'last place of manufacture' requirement be replaced with one based on the 'principal firm', defined as the firm that performs, or has performed on its behalf, the last process of manufacture in the CER region;***

The current definition of 'last place of manufacture' does not adequately capture modern outsourcing practices and all genuine local content.

The Joint Ministerial Statement on Rules of Origin issued at the CER 20th Anniversary Ministerial Forum in Sydney in August 2003 (copy attached) mentions that Australian and New Zealand officials will examine RoO and will consider improvements that will benefit business in Australia and New Zealand. Their work is to be guided by a number of principles, including the principle that all genuine local content should count towards meeting the RoO.

The Joint Ministerial Statement also mentions that officials have been tasked to design changes to the RoO which will ensure, among other things, equity of treatment for outsourcing manufacturing processes in both countries.

New Zealand has addressed the issue of outsourcing through the Customs and Excise Amendment Regulations 2003. Those Regulations include the introduction of the concept of 'principal manufacturer'.

Australia intends to introduce similar amendments to its customs legislation.

- ***The valuation and coverage of eligible costs in Australia and New Zealand be aligned to achieve a single set of rules implemented according to uniform practices;***

The Joint Ministerial Statement on Rules of Origin issued at the CER 20th Anniversary Ministerial Forum refers to the establishment of a Joint Customs Committee to "ensure a harmonised approach to the manner in which rules are administered".

The Customs Services of Australia and New Zealand have established a Joint Customs Committee. One of the tasks of the Committee is to ensure consistency in the administration of RoO.

- ***A standard definition of manufacturing be adopted, based on the Australian and New Zealand Standard Industrial Classification.***

Customs agrees that a standard definition of 'manufacturing' may be advantageous in increasing the levels of certainty and transparency and in reducing CER related compliance and administration costs.

The Commission's recommended definition of 'manufacturing', as provided by the Australian and New Zealand Standard Industrial Classification (ANZSIC), is not considered suitable for Customs purposes. The broad scope of the ANZSIC definition does not adequately specify which processes can actually be regarded as manufacture for the purposes of determining origin.

Customs suggests that the Commission considers the adoption of a definition similar to the definition of 'manufacture' in section 153UA of the *Customs Act 1901* (for the purposes of the Singapore-Australia Free Trade Agreement).

Interim Recommendation 2:

A 'waiver' be introduced to provide automatic duty free entry to any goods:

- ***manufactured within Australia or New Zealand (i.e. as defined in interim recommendation 1); and***
- ***for which the difference between the Australian and New Zealand MFN tariff rates is 5 percentage points or less.***

The Interim Report has identified that the current CER RoO no longer adequately fulfil their initial purpose of facilitating and promoting trade between New Zealand and Australia due to ever decreasing tariff rates and the difficulties faced by manufacturers in meeting the RVC threshold.

Customs considers that the implementation of this recommendation will encourage trade between the two countries and will lessen the administrative and compliance burden on manufacturers and Customs.

Change of Classification Method (CTC method)

Customs notes that the Commission has considered a switch to the CTC method but has not recommended it.

Customs has examined the CTC method as part of the Australia-United States Free Trade Agreement and the Thailand-Australia Free Trade Agreement discussions, and provides the following comments on CTC.

The Commission noted that, because the extent of transformation involved in a change in tariff heading varied greatly between headings, the CTC method would provide inconsistent origin determinations.

Customs considers that the present RoO system can also provide inconsistent origin determinations. The complexity and resource requirements of the 'last process of manufacture' criterion vary from product to product.

The Commission has stated "… because of the unsuitability of the classification for determining origin in some areas of the tariff, its implementation typically involves the use of secondary criteria, such as sector-specific regional value content rules and technical tests".

Customs considers that a CTC method demonstrates that substantial transformation has occurred. A regional value content requirement is generally an additional requirement, to a change in tariff classification rule, that is imposed for particular industry sectors. A regional value content is not used because a change in tariff classification rule is considered unsuitable for particular products.

The CTC approach does not necessarily have to be slow to adapt to changes in technology as indicated by the Commission. The RoO could be changed by agreement of the parties at anytime to reflect technology changes; changes to RoO do not need to wait for changes to be made to the Harmonized System.

Customs considers that the use of CTC would not be a financial or administrative burden on manufacturers because they already possess the information required for CTC RoO.

Interim Recommendation 3:

The regional value content threshold under CER be reduced from 50 per cent to 40 per cent immediately, with a further reduction to 30 percent in 2010.

A gradual phasing of the RVC under CER, though allowing manufacturers easier access to preference, could potentially lead to confusion where goods are produced or shipped during each transition period.

Confusion during transition periods would, however, be minimised under the 'waiver' option proposed by the Commission in Interim Recommendation 2, as fewer goods would be required to satisfy an RVC threshold.

Interim Recommendation 4:

In the longer term, consideration be given to further change in order to advance the goals of the CER, in particular:

- ***Elimination of the CER content threshold with only a 'principal firm' manufacturing test being applied;***

This recommendation would further reduce the administration and compliance burden of CER on manufacturers and Customs.

- ***Alignment of remaining non-zero MFN rates in the Australian and New Zealand tariff schedules, so that ultimately merchandise from all sources enters each jurisdiction on a common basis.***

Customs would like to note that the effectiveness of aligning the remaining non-zero MFN rates may be influenced by duty drawback and export concession issues.

The issue of duty drawback was raised during the roundtable meeting on the interim report in Canberra on 24 February 2004. Customs would like to point out that there could be administrative costs for industry and Customs if the Commission recommended, and the Government decided, that duty drawback should not apply to those Australian goods that qualified under CER for duty-free entry into New Zealand. For Customs, administrative costs would arise when duty drawback claims were checked to ensure that the Australian goods did not qualify under CER for duty-free entry into New Zealand.

I would be happy to provide additional information in relation to the above comments.

John Arndell
Acting National Manager
Trade Branch

March 2004

Joint Ministerial Statement on Rules of Origin

The Australian Minister for Trade, the Hon. Mark Vaile, and the New Zealand Minister for Trade Negotiations, the Hon. Jim Sutton, have agreed that officials from Australia and New Zealand should examine CER Rules of Origin (ROO) with a view to considering whether improvements which would benefit businesses on both sides of the Tasman should be made. In their work, officials will be guided by the following principles:

- ROO should continue to facilitate trans-Tasman trade in goods manufactured in the Free Trade Area and recognise the changed economic drivers as both economies seek to become more internationally competitive;

- All genuine local content should be counted towards meeting the ROO;

- The ROO should not act as a constraint on the development of innovative and efficient business practices within Australia and New Zealand;

- There should be equity of treatment for all businesses, whether they are integrated manufacturers or use outsourced manufacture;

- The ROO need to be able to be administered effectively and consistently by the Customs Services of Australia and New Zealand

Officials will henceforth consult regularly for this purpose, and will jointly report to responsible Ministers on progress. The first such report will be made by end December 2003, the second by end March 2004. The third and final joint report due in June 2004 will contain the conclusions of officials' deliberations, and recommendations to Ministers on elements of a possible comprehensive package of reforms.

These deliberations will take place in parallel with the Australian Productivity Commission's review of Rules of Origin and may inform or be informed by that process or any other appropriate example or independent study of ROO regimes.

Consistent with the desire to ensure ROO do not act as a constraint on trans-Tasman trade, Ministers have agreed upon a number of incremental improvements to the current system which should improve the situation for businesses on both sides of the Tasman in the short to medium term. Officials have therefore been tasked to design, without delay, changes to the ROO which, when implemented, will ensure:

- Equity of treatment for outsourcing manufacturing processes in both Australia and New Zealand. While New Zealand will move first to amend its regulations, the intention of both parties is to move to a consistent approach to outsourcing in the context of the comprehensive package of ROO reforms;

- That imported intermediate goods will be appropriately disregarded from the calculation of the total cost of the finished good for the purpose of calculating local content under the CER; and

- The establishment of a Joint Customs Committee to ensure a harmonised approach to the manner in which rules are administered.

Officials are also encouraged to identify other issues for potential early harvest as their broader examination of ROO continues. Such issues might include sensitivity to exchange rates, apportionment of overheads, and issues related to the equity of treatment between integrated and outsourced operations.

Sydney
28 August 2003