



**TRANSCRIPT
OF PROCEEDINGS**

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PRODUCTIVITY COMMISSION

INQUIRY INTO GENERAL TARIFF ARRANGEMENTS

**MR J.H. COSGROVE, Commissioner
MR M.C. WOODS, Commissioner**

TRANSCRIPT OF PROCEEDINGS

AT CANBERRA ON FRIDAY, 21 JANUARY 2000, AT 9 AM

Continued from 19/1/00 in Melbourne

MR COSGROVE: Good morning, everybody. We're now resuming the Productivity Commission's public hearings into its review of Australia's general tariff arrangements. Just by way of background for anyone wishing to obtain copies of either submissions or the transcripts of these hearings, they can do so from our Internet Web site. If they wish to obtain them in other ways, I suggest they have a chat to a member of our staff here this morning and they will tell you how you can either view them or obtain physical copies yourselves.

As we do always at these hearings, I will be inviting each participant to come to the table to our right and identify themselves and the capacities in which they are appearing at this inquiry. So let me begin by inviting ISONET, our first participant, to come to the microphones please.

MR NEIL: Thanks, commissioner. I'm Chris Neil. I'm the executive director of ISONET. I'd also like to introduce David McLachlan, the chairman of the board of ISONET. We do appreciate the opportunity this morning to make a submission to the Productivity Commission on this very, very important issue for Australian industry and particularly the manufacturing industry. I also appreciate the fact that we are late with our submissions; the submission has been emailed to you and I do have hard copies that I will give to Bill Henderson this morning.

MR COSGROVE: Yes, we now have a copy, but we would like you to take us through it.

MR NEIL: Thank you. The approach I will take this morning - and I understand that we have a few minutes, but I won't take more than a few - is that first I will provide a little bit of background on ISONET and the ISO network for those who are unfamiliar with the organisation. I will provide a bit of rationale as to why we are making a submission and what the objective of our submission is, and then talk about four of the areas of your terms of reference that we believe we have useful and meaningful comment to make and just wrap up with a small conclusion.

ISONET is a public company. It's funded by the Commonwealth government but it is a public, independent company with its own independent board. It was set up in 1995 by the Department of Industry, Science and Resources to act as the national coordination body for the Industrial Supplies Office or ISO network. The ISO network is a body of organisations individually sponsored, managed and funded by the state and territory governments throughout Australia, and there is an office in New Zealand as well, although that's not pertinent to this discussion.

The purpose of the ISO, the objective of that organisation, is to try and solve a market problem that Australian industry has in knowing about itself. There is a suspicion that has been proven in many cases that importers of products and services into Australia are unaware that there may be a completely suitable and competitive product or service from an Australian source that would suit their needs, but they don't have the tools or the resources to perform the research to find that source. The ISO was set up to fulfil that function. The ISO has been extremely successful

throughout its life of 15 years with some \$2.5 billion worth of goods and services that have been redirected to local industry as a result of their research activities.

The way the ISO works, it takes inquiries from people who are suspecting that they would have to import or potentially have to. The ISO then seeks out as much specification detail as it can on the goods and services required. It does some research to see whether or not there is a capability in Australia to meet the needs and, if they find suitable sources, advise the inquirer of those sources and then allow the inquirer to negotiate a suitable deal with the company. If the inquirer then redirects its contracting activity to an Australian industry, the ISO claims that as a successful activity on their behalf.

Through that research activity, the ISO has become accepted as the authority on Australian industry by both government bodies and by industry associations and some industry itself. The fact that it's recognised that way led to activities by the ISO in tariff concession activities, tariff concession applications. So in 1996 with the changes to the Customs Act, when they brought in the concept of prescribed organisations for tariff concession applications, the ISO was promulgated as a prescribed organisation and to date it is the only organisation, as a prescribed organisation, for TCS activities.

The flow-on effect from our involvement with tariff concession activities led to a much increased involvement with policy by-law and, later, project by-law activities. The project by-law ACN firmly writes the ISO into the process of seeking involvement of Australian industry as part of the precursor to receiving a project by-law. So the ISO is firmly written into both tariff concession and project by-law activities at the earliest possible stage to undertake research on behalf of the importers.

We also had a small part to play in the recent nuisance tariff review that was announced by Minister Moore back in July 1998 and concluded in September last year. We played a small research part in that. So the ISO and ISONET together have had reasonably significant activities related to the importation of goods and the imposts on those importations and the benefits that could be gained from redirecting work to Australian industry, so we believe we have some justification in making a submission to you.

Your terms of reference are extremely broad and I don't envy you your task, but we believe we can usefully comment on probably four aspects of your terms of reference. Those four are the protection issue versus the lowering of import costs to manufacture; the second is a discussion of general versus concessional tariff rates; the third is ad hoc removal of tariffs and the fourth is non-tariff factors influencing investment. Those are briefly discussed in our submission and I'll also briefly discuss them now.

Protection: protection is a very emotive issue. The whole issue of protection depends on where you are viewing it. There are manufacturers in Australia who manufacture components. There are also people who manufacture and assemble the

final product. The assemblers of final product are competing against imported final product; the component manufacturers are competing against the importers of their product. Assemblers of course want their input costs reduced, therefore they want the duty on componentry reduced. The issue is also compounded then by where the market is. If the market is offshore - and some research we did indicated that manufacturers who are exporting to Asian countries don't care what tariffs are in Australia, they don't care what the duty rates are - they would prefer pressure to be placed by the government on the recipients of their products so that their tariff rates were reduced, whereas manufacturers of similar products whose market is Australia want to see duty retained so that their production is protected.

Despite deliberating and examining this issue ourselves for quite some time, we discovered there is no simple solution. You can't come up with an equation that makes it easy to decide whether or not the tariff on this item should be removed or retained or reduced or increased. The only sensible and logical conclusion you can come to is that it has to be viewed in the whole strategic picture of the future of Australian industry. I know that is a very bland statement but it is I think the key that has to be remembered with any discussion of what is done to affect industry. It has to have the strategic future of industry as its focus.

On the issue of general and concessional tariff rates, of course the 3 and 5 per cent duty rates have received a great deal of, once again, emotional comment. These duty rates can in fact be swamped by changes in exchange rates, so you have got to ask yourself why there is so much discussion about why a 3 per cent or a zero per cent or a 5 per cent duty rate matters. The reason it matters is that project developers, particularly large infrastructure project developers, have to reduce all costs to zero - not to zero, but to the least possible, so they are going to find every avenue they can to reduce their costs. Even though exchange rates may affect them more, they are going to take whatever avenue is available to them, and if there is an avenue there to reduce their duty costs from 5 to 3 or from 5 to zero, they will take whichever one suits them best. The issue of 3 and 5 per cent gets clouded by the fact that developers are trying to remove as much of their costs as they can.

There are other issues related to the 3 and 5 per cent concessional rates that we believe are capable of reducing the costs for developers and achieve a better outcome for Australian industry. We have a program that we manage on behalf of the Commonwealth government called the Supplier Access to Major Projects program. This gives us the benefit of getting involved strategically with project developers very early in the project's life and attempting to show that there are better cost reductions that can be achieved by using competitive Australian industry than worrying too much about the duty rate. We have had some success with the SAMP or Supplier Access to Major Projects program and our involvement with Invest Australia with that.

I would like to talk very briefly about the ad hoc removal of tariffs and our experience with the nuisance tariff review. It is discussed very briefly in the submission. Once again, the nuisance tariff review and the flow-on effects that have been discovered from that review showed that nuisance tariffs or tariffs themselves are

an extremely complex issue and, while there has been a rigorous program through the tariff concession system of getting tariff relief where there are no manufacturers in Australia, that tariff concession scheme has public consultation, gazettal of information etcetera, on individual items.

When you begin to arbitrarily remove tariffs from ranges of items, a lot of the flow-on effects are not identified until after the event, and those flow-on effects can then cause - "embarrassment" is probably not the right word, but it's close - to those who initiated the review because there are people who are adversely affected and disadvantaged. What we recommend is that with actions to remove blocks of tariffs or ranges of tariffs, that an analysis has to be extremely rigorous, with consultation of all particular parties before the action is taken, not trying to recover it after the action is taken.

Our involvement with tariffs and the tariff issue has largely been related to major investors, to major project developers and investors. I believe that tariffs need to be viewed in relation to whether or not it affects the attraction or causes a disincentive to investment. Once again, we believe there are other more significant things that the government is able to do in the provision of services in relation to investment decisions that overshadow the tariff issue and those are the areas we should be concentrating on, not getting down into a number-crunching exercise of tariffs.

We fall fairly into this area of providing a facilitation mechanism for the benefits that can be given to investors and infrastructure developers to, with good management, redirect their thoughts towards considering Australian industry and showing that Australian industry can be competitive without worrying too much about the detail of the tariff.

However, having said that, what we need to recognise is that right now, for right or wrong, ISONET and the ISO network are able to get access to major project developers because they are seeking to reduce their costs and because they are seeking to get concessional rates of duty because they see that as a tangible reduction. The access we get at the earlier stages of a development can allow us to bring to them more competitive Australian industry solutions, and in the SAMP program - it's only about two and a half years old - we've already been able to do that to the tune of some 260, 270 million dollars worth of contracts.

If the influencing mechanism that we currently have through duty rates and tariffs is removed completely, then the ability we have to strategically engage these investors and these infrastructure developers will be removed as well. So, while we don't see retention or continued support for tariff as a major issue, we see that tariffs pale into insignificance when other issues are taken into account. We believe that the manufacturing industry plays a major part in Australia's future, particularly advanced manufacturing industry, and we believe that the tariff effect on industry is extremely complex and needs rigorous analysis. But the fact that the tariffs are there, whether for right or wrong reasons, causes industry to come to ISONET and the ISO network to see whether there are Australian manufacturers of their goods and services, and

that is a benefit to us and to the Australian industry as a whole. That's the message we'd like to leave with you.

MR COSGROVE: Thanks, Chris. Could you tell us a little about how you actually undertake this research to establish whether or not an Australian supply capability exists.

MR NEIL: The ISO is staffed by about 75 technical specialists throughout Australia and New Zealand. Those technical specialists bring with them a wealth of experience and knowledge about Australian industry capability because they have mostly worked in that industry. We also have at our disposal industry association handbooks, registers and references, and we have developed in the last 15 years a very significant databank of information about Australian industry capability. That information resides on an electronic database which is available to every desk in the ISO.

The research is undertaken using that recorded information as the first point of call. You come to me. You want to buy autoclaves but you believe the only place you can get them from is Canada. We ask you a little bit more about your specification, because we deal with capability, not with product. We find that you want to be able to roll a 32-millimetre steel plate into a five-metre diameter, heat treated to a certain specification. We then go out to our information sources and see whether or not there is anybody in Australia who can do that. They don't necessarily need to be doing it right now - people who have the facilities and the equipment and the trained staff to be able to do it - we go and seek those people out.

MR COSGROVE: Could that mean there could be some delay in the actual availability of product? If someone is capable of making it but is not presently doing so, it might take them some months to gear up to produce?

MR NEIL: It could, but normally when we receive an inquiry we don't just take information about the product; we take information about all of the specifications they have: what's their lead time, what's their delivery rate, do they have a batching issue. We also need to know largely what their budget is. We don't want to know their business, but if you're going to buy \$3 widgets from overseas and they can't make them in Australia for less than 12, then we're not going to offer up Australian industry as a potential supplier because they can't compete.

MR COSGROVE: But if you had a situation in which the cost angle was, let's say, neutral as between domestic and foreign supply, but the foreign supplier could get it onto a wharf in Australia a couple of months before the Australian producer could make it available, would that have a bearing, in particular in terms of your role under the tariff concession scheme and some of these other by-law arrangements, in determining whether or not a concessional rate of duty applied?

MR NEIL: It wouldn't have a bearing on our decision about concessional rates of duty because we don't make determinations in that area.

MR COSGROVE: No, but your advice.

MR NEIL: Our advice? It probably wouldn't have a bearing. We probably would still give the information because there may be other deciding factors that the buyer might use to decide where he gets his source of supply from. We would probably feel a little frustrated if the overseas supplier could land it two months earlier because we'd have to ask what gave them that advantage. I mean, was the order placed before Australian industry was even considered? Given all factors being normal, if this is not an off-the-shelf item - it has to be specified, it has to be manufactured, it then has to be delivered - Australian industry can compete and it can compete better because it doesn't have that long sea journey. So we would have to ask what gave the overseas supplier the advantage.

MR McLACHLAN: Of course, in the more complex equipment you get the whole-of-life costing, where you've got the period of time that it's in service in Australia and you can do that maintenance from Australian bases as opposed to the overseas supplier doing that, and that gives it a sort of tuned-up advantage also.

MR WOODS: You charge for the research and advisory role that you play - is that right - to the potential importer of product?

MR NEIL: No, the ISO services are free. They're funded by state and federal governments. That relates to general ad hoc core business inquiry. Where we are asked by infrastructure developers and project managers to dedicate an ISO staff member to their team for a period - three, six, 12 months - that's a drain on the ISO resources that we can't sustain without some subsidisation from the company, and that's largely the purpose of the SAMP program that the Commonwealth funded, to ensure a national focus is given to major project work where a dedicated research consultant is put in there.

MR WOODS: There's a very limited role for major projects over an extended period where you do your charging.

MR NEIL: Yes. The chairman has just reminded me that for tariff concession work where we are in fact going against what we normally do, which is try to get import replacement, we may be doing research on behalf of an importer who is going to import. That work we charge for.

MR COSGROVE: Could you give us any feeling for the amount involved in providing that advice.

MR NEIL: The costs?

MR COSGROVE: Yes, the costs to the - - -

MR NEIL: They're normally 400 to a thousand dollars, depending on the amount of time taken. It's a small fee, depending on the number of hours the research takes, and

it is a very small percentage of the ISO budget. In the work we're doing, if the importer decides that there is an Australian source of supply there and they don't need to import, then that fee is refunded.

MR WOODS: Where an applicant is looking to get a tariff concession order and use ISONET to in effect verify that there isn't an Australian comparable producer, then you charge on that basis, and that's an unavoidable fee, but if you then identify a relevant Australian producer, that fee is refunded. Is that correct?

MR NEIL: If they use the Australian producer. If they don't, they're not.

MR WOODS: Yes. Thank you.

MR COSGROVE: You mentioned, too, that tariffs are less important than what you call government services as a factor inducing investment. I'm not quite sure what you actually meant by "government services". Do you mean your role or broader factors like exchange rate movements or infrastructure provision?

MR NEIL: The services provided by Invest Australian, major project facilitation activities that can attract investors to invest in Australia, those can have a quite significant effect on the bottom line, the provision of services, infrastructure services.

MR COSGROVE: You may have mentioned, Chris, ISONET's overall budget. If you did, I've forgotten.

MR NEIL: We didn't. ISONET is funded by the Commonwealth, and our operating budget is just under \$400,000 a year for the ISONET office.

MR McLACHLAN: That excludes the ISOs which are funded by their respective state.

MR COSGROVE: Right.

MR McLACHLAN: So if you were to look at the totality of it, it's probably somewhere collectively about \$5 million nationally.

MR COSGROVE: Okay.

MR WOODS: In your overview of submission you made reference to the nuisance tariff process that's recently been concluded, and various witnesses have put to us examples where, even following that process, they are importing product where there is no equivalent manufacturer, whether it be stainless steel or various chemical compounds or the like. You made a cautionary comment about downstream consequences of taking action on any of these issues. Could you elaborate on that a little and offer some views on how to ensure that there is a clean-out that is appropriate but that downstream consequences are properly identified?

MR NEIL: I can give you two examples that we are aware of. One that came to light during the nuisance tariff review is in the submission. It relates to two definitions within the harmonised tariff code relating to frozen potatoes. One was subject to the nuisance tariff review and was to be removed; the other one, duty was to be retained. What probably would happen as a result of that is that people who are importing under the line item that was to be retained would attempt to shift their definition of their imported product to the other one to have their duty removed. Where you have items that are similar, there has to be care taken to make sure that we don't see a shift of approach.

Another one that came to light through a complaint to one of the ISOs related to the removal of duty on the IT componentry. Because it was bulk items or a range of lines that were removed, embedded in there were items that weren't really IT components, they were power components. There was a company that was affected, and didn't discover it was affected until people started importing the goods they had previously bought from this company. They were a power supplier rather than an IT component manufacturer and therefore they weren't considered during the analysis.

MR COSGROVE: This general system of concessions and their use in terms of highly detailed tariff lines does seem to involve a good deal of effort on the part of various people: the importers who might be seeking to make use of them, the Customs Service and, indeed, I guess people such as yourselves who are involved in applying those concessions or advising on their use. Do you think all that's worth the candle, given that we're talking here about - at present - a 2 per cent differential in most cases between the 5 per cent general rate and 3 per cent concession rate? Even if that were pulled back to zero it's a 5 per cent differential. When one gets to low orders of tariff such as those, the question does arise whether the administrative and compliance costs associated with using deviations from the tariff rates comes to mind.

MR NEIL: What I'd like to offer is an opinion on that. We don't have exhaustive analysis to prove it with figures, but when the 3 per cent concession rate for tariff concessions was introduced, we saw a marked reduction in the number of applicants coming to the ISO looking for substitutable suppliers for a tariff concession process. We saw a reasonable increase in the policy by-law, project by-law activity. So our view was that there would be other influences. Downturns in the economy and all sorts of other things affect people applying for tariff concessions, but you could conclude with some reasonable certainty that the introduction of a 3 per cent concessional rate for tariff concessions caused some people - who would otherwise have applied for a tariff concession - not to apply, because the cost of doing so wasn't worth the effort. But some of the other activity in tariff concessions then shifted to project by-laws, because instead of getting only a 2 per cent reduction in their duty they got a 5 per cent reduction through project by-law.

We suspect that some of that activity occurred. The numbers we know, in general, are quite small, except when you get into major projects, and then you're talking about millions of dollars. Those millions of dollars do affect their bottom line and they will attempt whatever process they can to reduce their costs.

MR McLACHLAN: But from the ISO's point of view, it provides an influencing factor for them to come and seek assistance, which gives us an exposure to what they're trying to do or what they intend to do, so we can get Australian industry involved at the earliest stage. Without that mechanism, or some other mechanism or influence to do it, we would see that that would diminish - with the removal of this completely.

MR WOODS: You see the tariff being an important leverage for getting in there to - - -

MR NEIL: It's a leverage mechanism that we would not like to see removed without something replacing it.

MR WOODS: Do you have a view on what would replace it?

MR McLACHLAN: There's the facilitation process.

MR NEIL: Yes, we have excellent examples through the SAMP program, that programs like that are able to cause project developers and importers to change their mind. So if things like the tariff system went away, then we need more educational programs and more awareness-raising programs like SAMP to achieve the same objective.

MR McLACHLAN: The major project facilitation activity that's presently taken by the Department of Industry, Science and Resources is an example where, as part of the recognition of the government's involvement, and recognition of that project, the ISO gets involved in it again there. That's where we've been able to utilise the SAMP program to be able to be very much involved at the earliest stages of major projects. We see that as being an excellent way of doing it. It's an information process.

MR WOODS: That's a different tack to currently under the major project by-laws where you have a role which you are strongly advocating at the front end of getting in to understand the project, working with the project proponent to identify relevant Australian suppliers. But you also have a role at the back end of major project by-laws, as I understand it, of advising customers ultimately on whether there is or is not an appropriate - - -

MR NEIL: If they ask, yes.

MR WOODS: So you have this duality of trying to encourage awareness of Australian manufacturers to the project proponent, at the front end, but in some sense you also have a role, when asked, at the back end of, in effect, giving a yea or nay to whether it's appropriate to give a project by-law concession.

MR NEIL: We do.

MR WOODS: Do you feel that there's a conflict in those two roles?

MR NEIL: No, because we're the authority on industry capability and if we're asked by anybody, public or private sector, we should be able to stand up and be counted where we're giving advice about the Australian industry capability. My opinion is that while we get the benefits out of the project by-law scheme, and we get the benefits out of the tariff concession scheme, those schemes cause potential importers to come to us for the wrong reasons. We would prefer them to come to us for the right reason; that is, to see whether or not Australian industry has got a capability, not coming to us seeking duty relief and then be convinced by us that there is a better way to get their source of supply.

MR COSGROVE: Yet your roles do seem to involve, on the one hand - I may be putting this incorrectly, but it seems to involve, in the first instance, trying to encourage the use of local supply capability.

MR NEIL: Yes.

MR COSGROVE: But this back-end role that Mike was referring to also seems to be the role of a more impartial adjudicator with no particular wish to favour either local supplies or importers. That's I think the notional difficulty.

MR McLACHLAN: But you find that the front end, in many cases, averts the requirement for the back end, because you've been working with the proponents. Because you've been working with the proponents in the earlier stages of the program, you've clearly identified those areas where there is not the capability. They go to customs and customs might come to us purely as a matter of process and it says, "Have you contacted the ISO?" and the requirement is to tick the box. In many cases customs is just validating that tick in the box, because we have been working with this project proponent to show that the opportunity for Australian industry has been presented and he has maximised the use of Australian industry. But there will be some things that we can't do and we just validate that information back to customs.

MR NEIL: I can understand, Mike, what you're concerned about - the conflict. There are two possible scenarios at the back end, if you like, to use your phrase. One is that we have been able to find Australian manufacturers that could do the goods or services, and the person is going to continue to import, therefore he should pay duty because there should be remaining that protection for the Australian industry that we've been able to find. He shouldn't get carte blanche entry. The other scenario is that there isn't anybody in Australia who manufactures the goods, therefore why should we stop him importing duty free, or at a concessional rate, because his goods may be the cost of an input to somebody else's manufacture.

MR WOODS: Given that that involves judgment, and given your self-professed and appropriate bias of trying to find a relevant Australian manufacturer, does that affect, therefore, the judgment that you bring to bear on that decision?

MR NEIL: I hope not. It shouldn't, no. I should also say that ISO is not the only mechanism, it's one that is recommended. It's not the only mechanism. They don't have to use ISO. So if they don't like the answer we give them they can go elsewhere and do their research other ways.

MR COSGROVE: They, the customers?

MR NEIL: The customers, and also the importer. The importer does not have to use the ISO, it's just one of the suggested means.

MR COSGROVE: On a different issue, Chris, I seem to gather from some remarks you made a few moments ago, that people wishing to make use of duty concessions have a choice - in a sense, two bites of the cherry. They can seek to use the tariff concession order scheme, or they can go into a by-law option. Is that choice very widespread? If so, one wonders why there are these two avenues available.

MR NEIL: In fact I don't think they're parallel avenues, I think they're sequential avenues. To get a project by-law they have to have at least shown - one of the processes in the project by-law scheme is to have applied for a tariff concession, as I understand it. You would have to take that from the authorities.

MR COSGROVE: I see. We can check it with customs, I guess.

MR WOODS: One of the matters raised with us, with the major project by-law scheme, is that more recently, as manufacturers are moving into global scale, the equipment can't all be brought in in one shipment from one location, but that it involves progressive manufacture and progressive installation. You know, they'll bring in the main framework and then they'll bring in components. It has been put to us that under that scheme, therefore, each shipment gets tested separately which then requires that instead of being able to contract for a complete unit which would involve particular components, some of which - there may be an equivalent Australian manufacture, but in the scheme of the totality of the piece of equipment it wouldn't fit the specification or might void part of the warranty of the major manufacturer from overseas. Do you see that there's some valid concern in that, from your experience with this scheme, or is that not a matter that you see of concern?

MR NEIL: The arguments have some substance. Whether or not they're valid concerns for the policy, we can't really comment on. We're not in the business of making or commenting on policy. I'll go back to my previous comment, that project developers will do whatever they can to reduce their costs. Those costs may in fact include an element of supply chain analysis. They already have a global supply chain. They buy their autoclaves from one place; they buy their erection equipment, their gas plants from another place, etcetera. They are comfortable with those suppliers.

They don't necessarily want to do the analysis work to see whether or not an Australian equivalent manufacturer is as good or better. They may in fact be better or cheaper, but they don't want to undertake the costs of the analysis, or the risk

associated with that. They're comfortable with their supply chain. So they just want to bring the stuff from where they always bring it. Whether or not they should be allowed to do that is not our business to say.

MR WOODS: No, that wasn't the circumstance I was particularly thinking of. It was more whether there is a complete piece of machinery but that has a number of components to it which are brought in in various shipments, and therefore there is a testing process at each point of shipment, as distinct from a testing process at the front end to validate that the totality of that single piece of equipment - - -

MR NEIL: Are you talking about item 43 issues, where it's split shipments?

MR WOODS: Yes.

MR NEIL: I mean, there is already the avenue for them to bring things in under item 43 where there are split shipments, and they get their duty relief, because they can't fit it all on the one ship. The real issue is the warranty issue that you're talking about, where the item did not get assembled and tested at the one place, put on a number of ships and sent here and then reassembled back here.

MR WOODS: No, it's sourced from various suppliers at various times.

MR NEIL: It has never been put together in one place.

MR WOODS: No.

MR NEIL: It has never been tested, and it doesn't get assembled until it's here.

MR WOODS: Yes.

MR NEIL: From an engineering point of view, you would have to ask why, if the item can be made in one place and tested to that spec and then sent to another place and assembled, why can't it be made in another place and tested for that spec, and that other place could be Australia. I know it's a vexed issue and we really can't comment on the policy related to that, but from an engineering point of view if you are buying components from around the world, then they should be considering Australian industry's ability to build those components to the same spec.

MR WOODS: Thank you.

MR COSGROVE: Chris, some of these matters that we've just been discussing have come to light, for us, via a couple of other submissions which we have received. Would you mind if we drew relevant sections of those to your attention after today and see if you had any further comments to make on the specific points that are raised in these submission?

MR NEIL: Not at all. Certainly.

MR COSGROVE: We'll send them to you and if you wouldn't mind responding.

MR NEIL: We're only too pleased to help.

MR COSGROVE: Thank you. Finally, I just want to come back on that question I raised about the seeming alternative options of using the tariff concession order and the by-laws. I'm probably being a bit dense here, but you seem to say that when the rate of duty applicable to tariff concession orders was lifted from zero to three that there was some diminution of use of tariff concession orders.

MR NEIL: Yes.

MR COSGROVE: Because, you know, the marginal gain was perhaps not enough to outweigh the compliance, investigatory - - -

MR NEIL: We suspect there may have been one - - -

MR COSGROVE: May have been, yes. But then you went on to say that there was a pick-up in use of policy or project by-laws where the duty was still zero.

MR NEIL: Yes.

MR COSGROVE: So it seems to suggest that people wishing to use these schemes do have the choice of retaining a zero rate of concessional duty without having to use the - - -

MR NEIL: Where the project by-law scheme is applicable.

MR COSGROVE: Where it is applicable, yes.

MR NEIL: Of course it has far narrower applicability than a TCS scheme.

MR COSGROVE: I see, yes.

MR NEIL: So where it's applicable they will attempt to reduce their costs wherever they can.

MR COSGROVE: Okay, thank you. That's all I think we have to raise. We will, as I say, send a few extracts from these other submissions to you. If you wouldn't mind reacting to them we would be grateful.

MR NEIL: Yes, thank you.

MR COSGROVE: Thanks for coming.

MR COSGROVE: Our next participant is DHL International. Would you identify yourself and the reason you're here today, please.

MR MULDOON: It's Ken Muldoon from DHL Australia. My position is customs affairs manager for the Oceania region for DHL. We made a submission to the inquiry.

MR COSGROVE: Yes.

MR MULDOON: The predominant focus of that relates to a scheme called Manufacturing-in-Bond, a concessional scheme, and whether that scheme would still have operations potentially with the removal of tariffs.

MR COSGROVE: Are there any points you'd like to make, Ken, or should we begin a discussion?

MR MULDOON: I suppose I'd like to open just with a bit of background and why DHL, as a service provider solely - not an importer, not a manufacturer - is involved in this. DHL, if people aren't aware, has a very large global freight network, started predominantly in documents but has transferred very quickly into the supply of goods, and is certainly a critical party in supply chain management for many international companies. On a global scale, when large multinational manufacturers are looking to establish manufacture and distribution centres around the world, there's an increasing incidence where they approach companies like DHL to find out where they are best located for distribution of their goods to get into the market.

So particularly large IT companies - someone like Dell or Montell who were out in Australia recently - looking to set up manufacturing and distribution centres for Asia will come to DHL as a group and say, "Okay, if we set it up in Australia can you still get our goods to market very quickly and at a low cost?" and those sort of factors we become aware of. I suppose it's like ISONET but in a totally different way - of potential investors in Australia.

Australia has, despite its tyranny of distance that everyone sees - in fact it's quite easy for us to ship goods out of Australia to the rest of Asia overnight. We can pick up goods in Australia finish of business and have them at the start of business through most of Asia. Freight rates out of Australia into Asia are quite cheap because we're a net importer and a lot of planes coming out of the US, going up to Asia virtually empty - we can in fact ship goods, get freight rates out of Australia into Asia cheaper than Asia to Asia.

There are a lot of other benefits here in Australia, you know. There are lower costs compared to places like Singapore for warehousing centres. You have a well-skilled population like the others. But one thing that always seemed to be missing was a competitive customs regime. You've talked about policy by-laws before and the companies that can apply for that. There are some quite strict limits

and they have to be very large. I'll let someone from customs elaborate on what the exact requirements are.

We found that the schemes here in Australia, particularly when you have these large companies that can say, "Well, we can go set up in a free trade zone in China, Malaysia, Singapore or Hong Kong, manufacture these goods, not get caught up in the customs administration and not get caught up in customs tariff issues", whereas that isn't available to us in Australia - so it's sort of like the check list that was discussed before. You could say, "Australia? Can we get them to market?" Well, whereas a lot of people believed they couldn't, we've now overcome that barrier. And they'd go down a check list and then they'd say, "Are there customs concerns, customs costs related to Australia?" and the answer to that is quite definitely yes.

So DHL started looking at what concessional arrangements might be suitable for these type of operations and it was probably about two or three years ago that we started a push, along with a few others at the time, to reconsider the idea of free trade zones or foreign trade zones here in Australia. Those suggestions were greeted with a bit of scepticism and some problems with trade zones, particularly where zones are very site specific. If you set up a zone at an airport you could pull "manufacturer" out of "country regional Australia" to zone - so, yes, there were some problems and I believe just some general perceptions - free trade zones, cheap labour, etcetera - that had problems with that.

At the time an alternative scheme that was already in place some 12 years ago, called Manufacturing-in-Bond, when the old IAC, your predecessor, recommended the removal of Manufacturing-in-Bond schemes, I suppose in a session not dissimilar to what you'd be going through now. While MiB was virtually stopped, the legislation wasn't removed, so it provided an avenue, without having to set up a whole new legislative framework, to get a concessional-type scheme back in place of that nature. It's just over two years ago now that the government announced its agreement to reinstitute Manufacturing-in-Bond and at the same time to develop the TRADEX scheme to replace the TEXCO and duty drawbacks and we still don't see MiB working, but we have a belief that if it was set up properly it could, and that tariff issues aren't the only reason that those schemes were set up.

MR WOODS: Could I just pick up on that? I understand you opened a Manufacturing-in-Bond arrangement back in April 98.

MR MULDOON: We licensed a site - - -

MR WOODS: You licensed a site.

MR MULDOON: - - - that could allow for a Manufacturing-in-Bond operation.

MR WOODS: But it's not as such operational?

MR MULDOON: No. When the government announced that it would agree to

MiB it was seen that TRADEX would be the scheme of the future, if believed - I have some doubts about that - and MiB was seen as a stopgap measure potentially because it could be instituted immediately. At the time, when it was announced, we immediately said to the government, "Unless you remove cost recovery charges and address some tariff treatment issues it wouldn't be commercially viable" and those cost recovery charges still haven't been removed.

The tariff treatment issue, which is very pertinent to all this - if you could imagine a manufacturer producing computers, and even through the IT agreement there are still components for computers which have a duty rate, and Blue Gum producing here in Australia is a prime example. It still pays about \$40,000 customs duty every month. In a free trade zone overseas you could manufacture a computer and then bring it into Australia duty-free because computers are duty-free. If you manufacture that same computer here in Australia you are charged and assessed on each individual component when the goods come in. If you export the goods well and good, but you've still paid out your duty rate.

There are some real disincentives associated with manufacturing certain items in Australia and the computer is an example. If I was a manufacturer I'd prefer to set up in a free trade zone overseas, not have any customs issues, import them into Australia duty-free rather than setting up in Australia, producing them here, having to go through the customs issue. So until I think some of these issues are addressed I don't think you will see the scheme taken up.

MR WOODS: Okay. So you've got a licence covering a site and to your knowledge that's the only action on MiB.

MR MULDOON: I'm sure that is the only one licensed at the moment.

MR WOODS: Yes. You made reference that even should the 5 per cent general tariff be abolished you can see some relevance for MiB or relate type activity.

MR MULDOON: Yes.

MR WOODS: Could you expand on that for me?

MR MULDOON: I see that there is the potential use for concessional schemes and refer there more to cost recovery items again. If you import components into Australia you can remove the tariff, but if there's a cost recovery on every shipment of \$40 per shipment and you can in an MiB site remove that cost recovery charge, as we've lobbied for, that would be worthwhile. If, instead of having to enter the goods fully into the Australian market and the full customs paperwork and process and administration that goes with that, that can be removed or at least minimised through schemes like this I think there are benefits.

The TRADEX scheme and the old TEXCO scheme - or the current TEXCO scheme still - rely on an entry for home consumption of the goods under customs

terminology, so you have to lodge a customs entry as if you were entering the goods into Australia. You then just have a reduction or removal of the tariff. Our proposal under MiB is that you don't go through that process. There is, sure, a cargo report but it's not to the full extent of a customs administration. So I think any scheme that can reduce customs administration and reduce customs cost recovery charges would be an attractive scheme still.

MR COSGROVE: Could you tell a little bit about the nature and extent of these customs charges that apply at present.

MR MULDOON: As I put in my submission, there's some work going on at the moment where they're reviewing how these charges will operate in about 12 months' time when customs restructures itself. The budget that they're looking for in terms of recovering customs running costs through cost recovery charges is about 75.5 million. If we are bringing goods for a company into Australia - and again a computer is a good example - if you source all your components from 50 different sites around the world, you would then have to bring in 50 different shipments. You could be 50 times let's say cost recovery charges plus administration charges, so clearance is going to be about \$50 per shipment, so you're already adding a cost burden on to any manufacturer in Australia.

MR COSGROVE: What would happen to those charges in a tariff-free environment?

MR MULDOON: Those charges would still apply.

MR COSGROVE: Why is that?

MR MULDOON: Unless the goods are valued under \$250 - and even then there's a minimal charge, but if anything is over \$250 at the moment you have to lodge a customs entry and with that lodge a - - -

MR COSGROVE: But that presumably is a practice related to the fact that we do have tariffs higher than zero.

MR MULDOON: No, I think if you could assume that customs and the whole requirement for border processing was removed, if you removed tariffs and the customs cost recovery regime was removed - I think those two would flow together very well - - -

MR COSGROVE: Yes.

MR MULDOON: - - - if that was the line you were going down. I don't think it's always going to be the case. I'm sure for statistics purposes everyone is going to want to know about the trade into and out of the country. Unless they come up with a system that doesn't rely on that being measured at the border you will have a customs presence at the border, and the government has instituted a practice where all work

done by customs on commercial entries shall be charged back to the community.

MR COSGROVE: What is the case, say in Singapore where tariffs are zero? Do you know?

MR MULDOON: Customs cost recovery charges - it's a rare beast but Australia has it, and my personal view is it's not desirable. I cringe each time I see John Howard or anyone saying, "Free down, break down tariff barriers" and yet here we are one of the few countries with a cost recovery regime.

MR WOODS: You used the phrase "customs charges and related administrative burden" several times in your submission. Is there more than what you're describing now?

MR MULDOON: I suppose if you value the work - you know, you can imagine if you're an importer or if you're the importing community - going in charges direct to government, the amount of time and effort in the processing of paperwork and complying with customs to come out and see the goods - - -

MR WOODS: Okay.

MR MULDOON: It's not just customs; there are quarantine charges. The other one I'll probably just mention is the anomalies there. Customs have introduced a cost recovery regime which is totally based on commercial operations. They're not supposed to recover their costs for community protection issues, even drug intervention, but we now have a cost recovery charge introduced by AQIS on every shipment into the country, which is clearly a community protection issue. But the whole cost recovery regime I think could do with a major review.

MR COSGROVE: So the other countries are recovering those costs, which I assume they're incurring, from general revenue sources.

MR MULDOON: As Australia did before it introduced that cost recovery regime, certainly within the last two years.

MR COSGROVE: But there's some sense, is there not, in user charging?

MR MULDOON: There is.

MR COSGROVE: In other words, the whole community may not have an interest in imports of certain items.

MR MULDOON: I would see that under these concessional schemes, though, if a concessional scheme can remove some of those charges and therefore attract new investment into Australia and the Australian community as a whole benefited from that, I think that's a desirable element, and that is why I'm still supportive of these schemes even if tariff concessions were removed but cost recovery was not removed.

MR COSGROVE: And you think they are a significant deterrent to investment?

MR MULDOON: That level - 75 million - you can make sound large or you can make sound small in the whole scheme of things.

MR COSGROVE: It seems pretty small to me.

MR MULDOON: Exactly. I think what it is is, again, that checklist mentality for a lot of companies. See, if I'm looking to invest and I've been given three options of Malaysia, Singapore, or China - sorry, let's make it four and put in Australia. If you're going down the list, "Do you have a free trade zone type set-up in Australia?" "No." "So you have to go through customs?" "Yes." "Are there cost recovery charges?" "Yes." I think it is just a disincentive to investment in Australia.

MR COSGROVE: Yes.

MR MULDOON: I don't think it's the only one, and certainly when we embarked on this project we were also looking at getting state governments and federal governments together to get a better package that we could market to these sorts of companies. You know, if Singapore is trying to attract some of this new investment it's all laid out very neatly for them - all the benefits of the schemes, all the tax concessions. There is a whole package being set up, and we are trying to develop a similar package here in Australia. I think that this is just one element. I'm sure every company, as we've said, looks to reduce costs anywhere it can.

MR WOODS: Presumably at the bottom line, though, it would look at what it's paying through general taxes and what it's paying by way of specific user charges, and there'd be some balancing process. I mean, I can understand the psychological point of there being yet another line entry, but there's the separate point of what the actual bottom line is.

MR MULDOON: I can assure you that every major user or major manufacturer that we've tried to approach has been very interested when they've found out about MiB and said that that would remove one of their negative thoughts on Australia.

MR WOODS: In that context you've referred to the customs thresholds. Do you want to elaborate on that for us.

MR MULDOON: There are a range of customs thresholds. The predominant one I suppose most people would be aware of is, if you import or if you mail-order - I suppose that's one of the type of things - if you do that and it's below a \$250 value and the duty and tax is below \$50 then customs don't collect the duty and tax. It's referred to as a screen-free threshold. Above that you virtually need - there is a thing for an informal entry. It's not computerised and, to be honest, from our industry's point of view, it's not used. So you either have a screen-free entry or a formal entry. If you go into a formal entry, duty and tax will become payable and a higher cost

recovery charge will become payable.

We have been lobbying for increases in those thresholds, or even harmonisation of the thresholds, because there are differing thresholds between Australia Post and anyone else. We have been lobbying long and hard to try and get those thresholds aligned. The other one is the removal of the duty and tax calculation. So the concept that if it's below 250 and the duty and tax is below 50 as a threshold - we would much prefer to see a threshold that said, well, is it below 250? Because as soon as you put the duty and tax on, you have to go through virtually the full customs process of identifying down to eight digits what the goods are classified as, and then working out the tax. It's a scheme that we find administratively cumbersome.

MR COSGROVE: So you're not so concerned about the larger thresholds that apply in cases of imports of capital equipment, the five or 10 million dollar threshold?

MR MULDOON: Yes, for those sorts of schemes. But where we were looking, we were looking to develop a scheme under MiB that didn't have to go to that larger scale, it could apply to smaller-scale operations, and that's where we went with Manufacturing-in-Bond as a potential, where you're in a customs bonded warehouse, you haven't gone into the entry for home consumption, you haven't gone through that customs barrier, and you don't have to be too large. At the moment, if I bring goods into this country, unless I hold them in a bonded warehouse and I then export them, I still have to pay customs costs recovery charges and virtually have to go through the whole customs process - administration from the customs point of view with cost recovery, and my own administration.

MR COSGROVE: Yes.

MR MULDOON: I would think that in developing Australia as a regional distribution centre for Asia that is nonsensical, and it was MiB that we were using. Under all the other schemes you have to go through customs to then manufacture. We were looking at something that, even if you were exporting, you could manufacture without going through that customs barrier here in Australia.

MR COSGROVE: Yes.

MR MULDOON: TEXCO - none of those allow that. It's as if you're bringing the goods into the country, manufacturing and then exporting, with the associated administration and cost overheads. We're looking to develop a scheme that could make Australia a bit more attractive for trade. It was then argued that it should be solely export-focused, but that ignores the reality that Australia is one of the biggest markets in Asia and there will be a desire, if you manufacture something here, to bring a percentage of it into the Australian market. Under the current arrangements the only way you could really do that is to virtually run two separate companies, which we see as undesirable.

MR COSGROVE: But apart from your concern about the present cost recovery

arrangement, what is it that the MiB scheme would offer over a situation in which there were no tariffs? Would it be of any value then?

MR MULDOON: No, and I'd agree, if you could remove cost recovery and you thought of a better way to collect your data than having to go through the administration the way it is, yes, I would see that as quite - the Australian manufacturers - the broader tariff debate that you will be involved in is something I wouldn't like to get heavily into.

MR COSGROVE: Okay. I seem to recall you expressing a little doubt about the value of the proposed TRADEX scheme. Let's assume, though, that that comes into place. Does MiB continue to have some additional value in that situation?

MR MULDOON: Under MiB we've got the government's agreement to remove cost recovery charges for goods going into an MiB site.

MR COSGROVE: I see.

MR MULDOON: That was announced in April last year. Legislation was introduced last year. It got a long way and then has stalled because of the tariff treatment issue. At the same time as the legislation, or in the same bill, the government introduced specific tariff treatment for goods coming out of an MiB which said that they would still be assessed as their component parts. So if you made a computer in an MiB site, when you entered that into the Australian market you wouldn't enter a computer, you would enter each of the individual components and the tariff rates that apply to any of those components would come into play.

MR COSGROVE: Yes.

MR MULDOON: We essentially objected to that and the opposition has put forward an amendment that has proposed that the tariff treatment of goods coming out of an MiB should be as defined by regulation and then some discussion had throughout industry as to how those regulations are framed. Every indication I've got is that while that amendment is still within the parliament the cost recovery regime or the removal of it for MiB won't be being passed.

I mentioned TRADEX. I think TRADEX will be a successful scheme in that the people who are using TEXCO now will change over to TRADEX. So if that's how you measure the success of a scheme, it will be successful. My view is, in attracting new investment to Australia, if it's a scheme that starts to point us in a new direction rather than just replacing the old with a potentially administratively less cumbersome scheme it will succeed, but it still relies on your entry for home consumption, it still has cost recovery charges, it still has all the inherent barriers that we are trying to remove through MiB.

MR COSGROVE: Yes. Thanks very much.

MR COSGROVE: The Australian Chamber of Commerce and Industry is our next participant. Would each of you please identify yourself for our transcript and the capacity in which you're with us today.

MR PATERSON: Mark Paterson, chief executive, Australian Chamber of Commerce and Industry, and appearing with me is Mr Tim Reardon.

MR COSGROVE: Thank you. Mark, would you like to make any points about the submission.

MR PATERSON: Just a brief overview. You have received a submission and no doubt had an opportunity to go through it?

MR COSGROVE: Yes, we have.

MR PATERSON: I think the three major themes that I would assert come through in our submission. One is that the general level of tariffs is no longer the major issue in industry policy that it once was, so it's given I think less attention and is of less importance in terms of the shape of the Australian economy than it once was, but it still remains an important issue and there are a number of factors associated with our existing regime where we'd like to see change.

The most significant area of change sought by us is in the tariff concession scheme area where, as a result of budgetary pressures and some political factors, changes were made to the scheme in 1996. That was argued at the time as being solely for the purposes of revenue. It wasn't in the traditional approaches of any form of protection or barrier. It was a revenue measure introduced and justified at the time by the government as being the business community's contribution to reducing the budget deficit at the time. If the budget is back in surplus there is no justification for continuing the regime. That was amended in 1996 and we'd like to see that decision reversed, and reversed at the earliest opportunity.

Clearly it was a cost impost imposed on business but not on consumer goods, so those businesses operating in Australia that import inputs to the manufacturing process pay a tariff on their business inputs but fully manufactured product coming into the Australian marketplace competing with those firms come in tariff free. So it is a significant impost on a whole range of manufactured goods and is one that I've got to say creates probably more heat for those who are affected by it than many of the other areas of tariffs as they remain.

The second area in terms of our submission is the issue of nuisance tariffs. Nuisance tariffs by and large provide little other than a revenue stream and a pretty ad hoc revenue stream for a government. We believe that there is a strong case for the removal of the nuisance tariffs. They should, where possible, be used as a bargaining chip in terms of removal of tariffs - internationally - but we shouldn't not remove them as a matter of course in any event. So we would argue for their

removal. If it's possible to use them as a bargaining chip and to provide some additional leverage then we should do so, but that doesn't mean to say that we should shirk our responsibilities of removing them in any event.

There have been some moves in recent times to approach it piecemeal, industry sector by industry sector, and in relation to changes to tariffs in the information technology area we don't support a continuation of that piecemeal approach and believe that there ought to be considered whole of government approach on the removal of tariffs. We don't say that the removal of tariffs ought to be contingent upon other areas of micro-economic reform, but believe that more will be gained if we're pursuing tariff reform at the same time as pursuing other areas of micro-economic reform. I think they're the themes that would come through the submission, but I'm happy to elaborate on any of those points or respond to any questions, commissioner.

MR COSGROVE: Yes, thanks, Mark. You do make the point in your submission as regards the 5 per cent general tariff that it would be missing an important opportunity to leverage lower protection levels amongst our trading partners if we went ahead with unilateral reductions. So at that 5 per cent level you want to see, in a sense, a pause subject to responses elsewhere in the world, but at the 3 per cent TCS rate of duty you'd like to see that taken off immediately, as you said, for the budgetary reason now passed. But isn't there some sort of inconsistency between suggesting that a 5 per cent tariff can be used as negotiating coin, but a 3 per cent tariff shouldn't be?

MR PATERSON: The 3 per cent was imposed on business inputs and then competing against fully imported non-tariff protected goods and having those tariffs on business inputs embedded in the cost structure then for those who export from Australia. It's a different position in relation to the 5 per cent general tariff which will apply to manufactured goods coming in wholly made up competing with goods that are manufactured in Australia.

MR COSGROVE: Does it not apply also to some business inputs, even if they may be wholly made goods - - -

MR PATERSON: It can, I think.

MR COSGROVE: They might still be being used by others in their production processes.

MR PATERSON: Our submission does recognise that there are benefits for the Australian economy in the unilateral action in relation to the 5 per cent and recognises that Australia would be better off by unilateral action, but recognises that the current state of play internationally in terms of negotiations may be assisted by using the removal of the 5 per cent tariff in part of that negotiation.

MR COSGROVE: Why is that the case? Why would we want to delay those

benefits rather than take them immediately?

MR PATERSON: I think it's a desire to use the pressure of that removal to assist in opening up overseas markets. It's not saying it's contingent. Our position is quite clear up-front that we would benefit from unilateral action. Our submission clearly indicates that, but we believe recognising the dynamics of international negotiations as they're presently in play - that there would be some benefit in using that as a bargaining chip.

MR COSGROVE: Do you think we have real bargaining coin with a 5 per cent tariff?

MR PATERSON: We've got better than we would have with none.

MR COSGROVE: One can debate that, I think.

MR PATERSON: But there is argument - yes.

MR COSGROVE: Yes, that you would establish credibility as a lower tariff country in international negotiations, and I think we have gained some benefit of that kind in GATT negotiations of late.

MR PATERSON: Yes.

MR COSGROVE: I am asking the question in part because some other participants have argued that there is very little negotiating coin associated with the 5 per cent tariff and that to the extent that a relatively small country such as Australia has any, it would rest more in the areas where tariffs are higher - ie passenger motor vehicles and textiles, clothing and footwear. Are you aware of any evidence of us being able to exercise negotiating coin, whether the tariff level was 5 per cent or 10 or 20?

MR PATERSON: It's a difficult judgment call, I think. Having acknowledged that we would benefit from unilateral action it does recognise that there is a strong stance that could be taken to say that we go to the negotiating table pure if it's removed. I think it is a question of judgment and on balance - given the competing considerations - we came down in favour of seeking to use it as a negotiating tool. But I firmly acknowledge that it was a consideration on balance.

MR WOODS: Pursing that just a little further, if in fact the 5 per cent level may give us some but not a great level of negotiating leverage, then how long would we want to await the unilateral benefits of reduction through the negotiating process before we decided that we're incurring costs greater than the benefits that the economy enjoy by unilateral reduction? Are we saying if we can't achieve it in three years or five years, or do we have to wait for the 2010 period before the costs are outweighing the benefits?

MR PATERSON: Our thought process was - and much of this was developed prior

to the failure of Seattle to agree on the agenda for the next round of negotiations - our time frame was that that round ought to be three years and that we would envisage a period of time no greater than our anticipation of that round. So we don't believe that it's something that needs to be dragged on for ever. If it is available for negotiation it's going to be available within that time frame. If there is any leverage that can be brought to bear that's the time frame in which we would be able to bring it to bear.

MR WOODS: If the judgment becomes, over the course of the next year or two, that three years, or even four years, is not a period in which we're likely to achieve significant breakthrough in reciprocity, then we should enjoy the benefits of the removal of the tariff.

MR PATERSON: Yes.

MR COSGROVE: On this same question, Mark, on page 5 of your submission there's a statement that:

Even while there are large benefits from unilateral reductions in tariffs, such benefits would be vastly increased if there were simultaneous reductions in protection levels by our trading partners.

The word "vastly" is the one I wanted to ask you about. Does it have real substance, do you feel? I am asking that question in the knowledge that most of the serious research undertaken to try to assess the benefits of unilateral, as distinct from multilateral trade liberalisation suggests that a very large component of the benefits in fact comes from unilateral reductions. Some people estimate maybe 80 per cent of the total. Do you have some different perspective on that in using this word "vastly"?

MR PATERSON: I think, seen in the context that it's presented there, it is that we've gained substantially by the general level of tariff reductions that have already been taken in Australia and Australian industry has demonstrated those benefits. The challenge that many in Australian industry face now is access to other markets in being able to further benefit. So in the context of unilateral action, much of that unilateral action has already been taken and those benefits are already in evidence here. The incremental additional gains by the reductions in tariffs here in our view would be outweighed by gaining market access in other markets where there are much higher levels of protective barrier - both tariff and non-tariff barriers.

MR COSGROVE: I see.

MR WOODS: Although by retaining our 5 per cent general tariff brings up questions such as the nuisance tariffs and that debate which would disappear by the removal of the general tariff. Do you have a view on whether the nuisance tariff process recently completed, went far enough or do you see there still being residual items that need to be dealt with?

MR PATERSON: I can't say that I can bring to immediate recall each of the

elements of the nuisance tariff review which would highlight to me any particular areas. To the extent that they remain, our submission argues their removal. They are not there in any significant way providing protection to the domestic economy and that they are as the label has described them. But it's unfortunate there are nuisance tariffs because they're seen not to raise significant amounts of revenue. The TCS is much more of a nuisance tariff than some of the nuisance tariffs.

MR COSGROVE: You make the point that the cost of nuisance tariffs is borne directly by Australia's exporting industries. That, I think, is the case with all tariffs so if you're suggesting to us that a nuisance tariff should be dispensed with, why not all tariffs on that ground?

MR PATERSON: The nuisance tariffs I don't think carry any significant weight in a negotiating sense; the general tariff does. It's that balance of consideration. We say get rid of the nuisance tariffs. We say on balance there would be a benefit in unilateral action in removing the general tariff as well; try and use the removal of the general tariff to provide some opportunities for greater market access.

MR COSGROVE: So it's this bargaining coin point again.

MR PATERSON: Yes.

MR WOODS: You make reference on page 3 of your submission, towards the top, of the cost to business of complying with the various concession schemes. You refer to TRADEX, TEXCO, but it would also be duty drawback and MiB and tariff concession orders, etcetera. Is there any way in which your organisation would be able to assist in estimating the actual costs of business? We're pursuing separately with customers and the like the administrative costs at their end, but to the extent that you are able to draw on hard information, that would greatly assist our inquiry.

MR PATERSON: I will take that on notice.

MR WOODS: Yes, thank you.

MR PATERSON: The anecdotal feedback that I'm conscious of is that the administrative complexity and the process of going through it means that people don't bother. So being able to accurately estimate the cost of the drawback, given the administrative arrangements that are in place - - -

MR COSGROVE: It's a deterrent.

MR PATERSON: It's a deterrent and if it's too hard bureaucratically to claim it back they don't bother. So whether we'll be able to get the hard evidence to demonstrate that - - -

MR WOODS: We have some of that flavour as well. The more it can be catalogued the clearer we can be on that point.

MR PATERSON: Yes, we'll take that on notice.

MR COSGROVE: Thank you. Mark, there was another point on page 4 just up above the nuisance tariff section of your submission in the second complete paragraph there. It ends with a sentence saying:

The TCS 3 per cent duty may at some time in the future be judged as contrary to international rules under the WTO.

Do you know what you had in mind there?

MR REARDON: Yes, the point there is that at some stage in the future the bound rates under the WTO may be reduced to an extent where the 3 per cent is contrary to WTO rules.

MR COSGROVE: Meaning that the bound rate would be below the 3 per cent?

MR REARDON: At some stage.

MR COSGROVE: I see. Yes, right. I think that's about it. Mike, do you have anything?

MR WOODS: Only whether you wish to expand on what you consider might be less distortionary revenue measures that would replace the revenue currently garnered from tariffs. You spend several paragraphs in your conclusion saying that there may be some, but whether you want to proffer a view on the particulars.

MR PATERSON: We would always prefer to find a way of doing it without further revenue raising. So less distortionary revenue raising measures may well be on reduction on the expenditure side rather than proffering alternative new taxes.

MR WOODS: Thank you.

MR COSGROVE: Very well. That's an option. Thank you very much to both of you for coming along and helping us.

MR COSGROVE: Our next participant is the Winemakers Federation of Australia. Will each of you please identify yourselves for our transcript recording and indicate the capacity in which you are with us today.

MR BATTAGLENE: My name is Tony Battaglene. I am the general manager of the Canberra Wine Bureau, which is the Canberra office of the Winemakers Federation of Australia.

MR STRACHAN: I'm Stephen Strachan and I'm the senior analyst at the Winemakers Federation in Adelaide.

MR COSGROVE: Thank you. You've come a long way. Thanks for the submission which you have provided to us already. Are there aspects of that that you want to draw to our attention this morning, or some other matters?

MR BATTAGLENE: Yes, there are a few aspects. When we prepared this submission we still had some feelers out in the industry, certainly to get some more information on products of concern, and I've got some more of that to present to you.

MR COSGROVE: Good.

MR BATTAGLENE: But I'd like to at this particular time give you a bit of background into the wine industry, very briefly, and explain why we consider the removal of a lot of these tariffs on our inputs are particularly important at this stage, if I may.

MR COSGROVE: Yes.

MR BATTAGLENE: We're going into a period where there are record supplies of grapes coming onto the market, both in Australia and internationally. This looks like happening for the next few years and it's the first time that we'll actually be able to meet demand for a lot of our final product. We're a very export focused industry, but what we're going to see with the increased supply of grape product and the resultant wine produced is that there are increased competitive pressures that are coming on in the international market, as everyone is competing for increased market share at this stage.

We're seeing increased technology transfer, particularly through joint ventures in countries such as Argentina and Chile. These countries have massive production potential and they're now being able to produce quality wine in quantities that they haven't been able to do in the past, and that will only improve. We don't have any fears that we can't compete with these countries on the quality of our wine. In fact the major fear that we see is market access issues for our industry, apart from taxation, which is a domestic issue which I won't go into. But domestically we're seeing that we're having significant imposts on the industry through increased taxes, because we actually suffer an increased tax after the GST introduction because we've

got the wine equalisation tax, which unfortunately hasn't proved as equal as we would like.

What it means is that with the increased competitiveness internationally, we are looking to make efficiencies in our production. That's the area where we particularly welcome this inquiry, because we've got a number of significant inputs which are subject to tariffs - not high tariffs but they do make a particular impost. In our submission we mention oak in particular, and a number of other things, including machinery. There's a couple of other very important ones that I'd like to mention now. One of these is stainless steel, and I understand from looking at the submissions on your Web site, that a number of the stainless steel producers have also raised this.

MR COSGROVE: A few supporters, yes.

MR WOODS: Yes, we were going to draw that out in debate and I'm pleased that you've done that for us.

MR BATTAGLENE: It's particularly important. It probably costs our industry 6 or 7 hundred thousand dollars a year and that, we forecast, will increase to probably \$1 million next year, because with the increased supply of grapes we're seeing that we need the processing capacity to meet that supply, and stainless steel tanks is where that happens. Now, there's no domestic producer of stainless steel that I know of, particularly of the tank material, so it seems an ideal tariff that could be a significant help to our industry if we could remove it. Just a single company, one of our big four companies, estimated costs. They spend about \$2.6 million per year solely on stainless steel and they're looking for that to increase. Southcorp are looking for a fairly significant increase in usage of stainless steel over the next few years, right through till 2003, 2004, 2005.

The other issue apart from stainless steel is cork. Now, cork stoppers don't have a tariff I understand but agglomerated cork, which also goes into corks, currently faces a 3 per cent tariff. The code for that I believe is 4504, and talking to some of our cork manufacturers, it's a significant impost on their costs, and that's passed on to us.

MR COSGROVE: Could you tell me, Tony, is agglomerated put together here or does that also come - well, it comes from abroad because there's a duty on it, but is it produced in Australia as well?

MR BATTAGLENE: I've tried to find this out, but I don't think there's any cork produced in Australia. It comes together in blanks. It usually comes in and they produce the cork from that, though it can come forward in the form of corks itself. So that's another significant one because, particularly in the lower price ranges, the corks you get in many of the bottles is the agglomerated cork, whereas if you're drinking a Grange, which no doubt productivity commissioners do - - -

MR COSGROVE: No, we are not in that league I'm afraid.

MR BATTAGLENE: We don't either, unfortunately. The other issue - we mentioned closures and sealants. That's the champagne-type closures and crown seals. There's also raw PVC which is used for the closures over bottles. That's imported by our manufacturers as well and that faces a 3 per cent duty. So they're the main issues and the main tariff codes of concern. There's obviously machinery. There's the machinery used to make cork, which faces a tariff, and there's some bottling machinery and items such as those. They're of some importance too, but not as important as the cork, the PVC, the oak and the stainless steel. They're the big ones that have a significant effect on our industry. Stephen, would you like to - - -

MR STRACHAN: Just to put in perspective the magnitude of the stainless steel requirements over the next few years, a couple of years ago a typical vintage in the industry was about 700,000 tonnes. There's been quite a rapid rate of plantings - we're up to about 1 million tonnes per year - but just based on what's in the ground, we're pretty sure we'll be at about 1 and a half million tonnes by about the year 2004-2005, so we're talking about pretty much a doubling of where we were two years ago. We do know that we're pretty much as close as we possibly can be to about 100 per cent capacity use at the moment.

What that means of course is there is no excess capacity in the industry. If this fruit is going to be processed and stored then obviously we will need to put in that infrastructure to do that. The expectation is that wineries will do it, and in all probability they will, but of course they're only going to do it if they can see a profitable market for that wine. So at the end of the day it means that we're looking at some pretty hefty increases in stainless steel demand.

MR COSGROVE: How much would you say? I mean, is a doubling likely?

MR STRACHAN: That's the sort of magnitude that we're talking about, yes. Probably not quite doubling from where we are today - maybe about a 50 per cent increase. What wineries will probably have to do is - what you will see is, for instance, the proportion of wine going into oak may dip. We'll still see more of it but it may dip in a proportional sense for a couple of years, for cash flow reasons as much as anything. Nevertheless, the oak requirements will still be quite significant over the next few years. That's to some extent exacerbated by the fact that oak is mainly used for red wine and most of what's coming on is red wine at the moment.

MR COSGROVE: Could you provide us with information on the proportion of total costs of wine production, whether by case or bottle or per ton, which is constituted by oak and stainless steel storage - perhaps not day, but if you - - -

MR STRACHAN: Yes. What we could do is get some information confidentially from some of our companies. It's guarded pretty closely as you can imagine.

MR COSGROVE: Yes.

MR STRACHAN: And unfortunately the industry doesn't have an industry-wide benchmarking study.

MR COSGROVE: I see, yes.

MR STRACHAN: We are actually doing one and we'll have that probably in about February.

MR COSGROVE: Well, that would be more useful to us, to be honest, than confidential company-by-company data.

MR STRACHAN: Okay. Well, as soon as we get that we can certainly pass it on, yes.

MR COSGROVE: Okay, if you wouldn't mind.

MR STRACHAN: Southcorp have actually given us their figures for oak, have they?

MR BATTAGLENE: Not yet. They're supposed to be coming.

MR WOODS: But a more comprehensive run-down of the contribution of each of those to the total costs on an industry basis rather than a particular manufacturer would be helpful.

MR BATTAGLENE: Certainly.

MR COSGROVE: Did you want to say anything more, Stephen?

MR STRACHAN: No.

MR COSGROVE: Your submission also has something to say about oak and we weren't quite clear as to what you were trying to convey. This is section 4.0, Issues. You talk there about:

Of most concern to the industry are tariffs on oak barrels and coopers' products -

and then a little further down there's a sentence that reads:

There is no wine stored in oak barrels produced from oak grown in Australia -

and again, a little further down once more:

There is no competitive reason for the tariff on oak imports as there is no Australian oak industry.

The first of those sentences that I read out might be construed as meaning that there is a domestic oak industry, but the second suggests not. There's none?

MR STRACHAN: Are you after a clarification?

MR COSGROVE: Yes. There is none, or - - -

MR STRACHAN: There's certainly no oak manufactured in Australia, or grown in Australia for that matter. There is a cooperage industry in Australia that's quite small. What happens with those coopers is they import the oak and then value add, so I guess we're talking about imported oak and imported barrels as well.

MR WOODS: And there's no movement on the part of the forest industry to start meeting some of this demand?

MR STRACHAN: Not that we're aware of.

MR WOODS: Or is there no desire on the part of the manufacturers to have things labelled as being "in Australian oak" as distinct from French oak or from American oak?

MR STRACHAN: No.

MR BATTAGLENE: I think because of the prestige of French and American oak, which are well-recognised in the international community as providing specific flavours to the wine and imparting specific characteristics, it wouldn't be a good marketing ploy to have Australian oak.

MR WOODS: We don't know what the flavour is.

MR COSGROVE: Eucalyptus.

MR WOODS: It may be good.

MR BATTAGLENE: It might be, but not on the export market. If it's an issue for us, it will be 20 years away I'd say.

MR WOODS: Okay. So there's no prospect by the forest industry to pick up into that market?

MR BATTAGLENE: No, I wouldn't think so.

MR COSGROVE: In that same section of your submission - and you referred to it a moment ago yourself - you've raised the question of concerns about tariffs on machinery for making various closures. What type of - well, I can imagine the type of machinery it is, but is that tariff protecting Australian producers who can make

machinery broadly of that kind?

MR BATTAGLENE: I don't think we're an expert on the Australian producers. We're looking purely at the end point, that there is an impact on our - - -

MR COSGROVE: So you would just favour a lower cost of that particular input.

MR BATTAGLENE: That's our perspective of it, yes.

MR COSGROVE: Yes, I see.

MR BATTAGLENE: Very parochial on that sort of issue.

MR WOODS: We notice you, as the Winemakers Federation, encompass also brandy producers as part of your electoral college system. Would the elimination of 5 per cent tariff on imported brandies and whiskies, etcetera, be seen as detrimental to the Australian brandy industry?

MR STRACHAN: It would, much more so than - - -

MR WOODS: I mean, is there substitutability across spirits or within spirits or - - -

MR STRACHAN: Certainly within the brandy market there is. If you look at Australian brandy sales in Australia, they have come down quite considerably since the mid-70s, and most of that reduction has been taken up by imported brandy, particularly French brandy. At the end of the day we're not as cost competitive with imported brandy as we are in relation to wine. The wine price is pretty much an export parity price whereas the brandy price in Australia is pretty much an import parity price.

To add to that, it is a bit of a contentious issue in the brandy industry in that we currently have countervailing measures on imported bulk French brandy and we're looking to apply countervailing measures on imported bottled French brandy, because we're fairly sure that what came in under subsidised bulk brandy has now been switched into subsidised bottled brandy. We're actually making that case at the moment, so in that sense if the tariff comes down I suspect you'd see a reduction for most of the brandy that's sold in Australia of an equivalent amount.

MR WOODS: And what about substitutability across spirits? If the tariff on Scotch whisky for instance was abolished, is that going to have any impact on local spirit producers in a more generic sense in Australia?

MR STRACHAN: I think there is reasonably strong substitution on brown spirits and less so on the white spirits, so I think it would have an effect.

MR WOODS: So you're arguing for removal of the tariffs on your inputs but not on competing imports.

MR STRACHAN: Can we actually address wine and we'll certainly get to brandy in a minute.

MR WOODS: Yes, fine.

MR STRACHAN: The issue of wine is that we haven't actually taken a policy position on the tariff on wine in Australia.

MR COSGROVE: Is that a 5 per cent tariff?

MR STRACHAN: Yes. But the fact that we haven't taken a policy position was partly because this inquiry was just before Christmas and we didn't have an opportunity to, but also it reflects the fact that it's not a big issue in the industry.

MR WOODS: In the wine segment?

MR STRACHAN: In the wine industry. Our prices in the domestic market are driven by our prices on export markets. That's where the focus of the industry is, that's where the growth is. So you tend to find that the price on the domestic market reaches some sort of equilibrium with the price on export markets. We are seeing an increase in imports of branded product into Australia but we don't see that as an issue in terms of competitiveness. It's more an issue to do with shortage of supply. So we can't say categorically that the Winemakers Federation would support a reduction to zero in the tariff on wine but I honestly don't think it's an issue, and we will take a policy position on it and get back to you on that.

MR BATTAGLENE: If I can just put it in the international negotiating context, we've had discussions certainly in some of our international fora on the tariffs on wine, and the position being taken by the United States in particular, who have a tariff much the same as ours, is that they don't want to see a zero tariff in the WTO round until some of the European countries and Asian countries bring their tariffs down to parity, and we've been supporting that position in the short term. We're not looking at zero for zero though, as Stephen says, we'll be taking a policy position on this in the near future and I suspect that we may actually go for zero for zero.

MR COSGROVE: How high are the tariffs in Europe, do you know?

MR STRACHAN: I don't actually know.

MR BATTAGLENE: I haven't got the actual figures. Higher than ours.

MR COSGROVE: We could find out, I'm sure.

MR STRACHAN: The major impost is the non-tariff barriers in some of those markets as well.

MR BATTAGLENE: Non-tariffs and subsidies. Asia are the biggest tariffs around, they're the biggest problem, but it's a smaller market for us, but certainly that's one of the areas we're looking at in the WTO round, to really impact on the removal of those tariffs.

MR COSGROVE: So is your main worry in Europe is problems associated with the common agricultural policy, that type of stuff?

MR BATTAGLENE: Yes. There are very heavy subsidies in Europe and certainly there's a big subsidy program coming down under the new agricultural policy which is to get a higher quality product and to increase market share. They're actively targeting increased market share and pulling out inferior vines and replanting better quality vines. There are also subsidies on marginal areas, and they do have import restrictions which are almost WTO inconsistent which just haven't been challenged yet, which cause problems in market access for us.

MR WOODS: On quarantine grounds?

MR BATTAGLENE: It's a bit confused with Australia because we actually have a treaty with them, a wine treaty, in which we've agreed to making our wine to their practices that we export to their market. We don't have a lot of flexibility in that agreement at the moment, though we're renegotiating it. So we're restricted to using their technologies, in essence, for the wine we put onto their market, whereas, being a fairly innovative culture, we're getting a lot of new technologies which make probably better quality wine and it takes a long time before they will accept those.

MR COSGROVE: Yet you're planning, as you said, to double production over the next - I've forgotten - 10, 15 years, which I assume means that your members are fairly confident of being able to sell that additional production. So how severe are these market access problems for you?

MR STRACHAN: Just to clarify the comment that we're planning to double production, actually it will be a lot less time frame than that. It will be in about five years - not quite doubling; probably about a 50 per cent increase from where we are now. But what we have is a situation where we represent wineries. Wineries produce about 30 per cent of the grapes in Australia. There's obviously also a group of independent grape producers as well. What we've seen in the last few years is that wineries have recognised I guess the increased competition offshore and the fact that they need to shift their investment focus from vineyards into processing and storage capacity.

However, the forward price signals haven't necessarily been adequately picked up by the grapegrowers, so what we've seen is a lot of grapes have gone in pretty much under speculation, not under contract or whatever, so they're not planted by the wineries, they're not done, I wouldn't say, in a proper planning environment and there's no knowledge when they are being planted that there's a high likelihood that they'll be sold offshore. So I guess that's the background, and so in that respect a lot

of the downside risk in terms of us not being able to access some of these markets will be with the grapegrowers, not with the winemakers.

MR BATTAGLENE: But if I could add, strategically there will come a time when our increased exports will provide a threat to the United States and to Europe and there will be some reaction from those countries, and that could be in the form of - you know, a similar thing to the lamb type issue or it could be tariffs, you name it. There could be something happening. So we're trying to set strategic moves into action which are basically sign agreements with these countries that will prevent non-tariff barriers being brought in and give us some protection for that type of behaviour. So we're looking at a multilateral treaty within the New World at the moment, which we're hoping to have significant progress in by February.

MR COSGROVE: Was that intended to be on the agenda at the so-called millennium round of WTO negotiations?

MR BATTAGLENE: No, that's being done outside that. There's no real need to bring that in there. There's more danger for us to open up too many wine issues in the WTO because it's, as you know, a problematic forum, and the Europeans have a number of issues to do with wine that they wish to raise, notably on intellectual property issues, that we don't want to see reopened. They want to reopen the SBS agreement, TVT agreements and intellectual property, and for us the dangers of that are quite high. So the main areas that we're putting forward for the WTO round when it happens are the reduction of tariffs, and certainly of subsidies within Europe - they're the key two areas - and then maintain the status quo for the other ones.

MR COSGROVE: Would your alternative proposal outside the WTO have legally binding effect?

MR BATTAGLENE: We're looking at treaty status. There already are bilateral treaties between a number of countries. Australia has one with the European Union. We're just signing one with Switzerland so a multilateral treaty is just an extension of that, and that would essentially create a bloc of the non-European countries, the major producers.

MR COSGROVE: Does that involve most favoured nation treatment of markets?

MR BATTAGLENE: There are some indications there, possibly. You'd have to talk to my colleagues in DFAT about that.

MR COSGROVE: If not, it would be challengeable under the WTO.

MR BATTAGLENE: Yes. We're not looking at tariff reduction at this stage. What we're looking at is non-tariff measures - oenological practices in particular - so we can't restrict imports and labelling issues and technical issues. There is a desire eventually to look at some of those other issues.

MR WOODS: You were going to then move on to the brandy side.

MR STRACHAN: Right. The issue with brandy would be more contentious in terms of the tariffs on brandy than it would be on wine. As I said earlier, we haven't taken it to our members so we'd have to discuss it. The Winemakers Federation would have to take a consistent position between brandy and wine, for obvious reasons, and I think we've made it fairly clear what we think the position on wine would be, so without pre-empting that decision I suspect that's the sort of line we would come back with.

MR WOODS: I think I understand that.

MR COSGROVE: Anything else? I don't think I have any further questions. If there's nothing else you wanted to put to us we'll finish our session.

MR BATTAGLENE: That's fine with me.

MR COSGROVE: Okay. Thank you very much for coming along.

MR BATTAGLENE: We'll provide you with that information.

MR COSGROVE: Yes, when you have it. In the next month would be good.

MR COSGROVE: Our next participant is the Pulp and Paper Manufacturers Federation of Australia. I'd be grateful, Bridson, if for the purpose of our tape-recording, you could just identify yourself and the capacity in which you're with us today.

MR CRIBB: I'm Bridson Cribb. I'm the executive director of the Pulp and Paper Manufacturers Federation of Australia.

MR COSGROVE: Thank you, and thank you for the submission you've already provided to us, which we've had a chance to read. You may want to make some remarks.

MR CRIBB: I think the submission is pretty straightforward. There are probably three main areas. In terms of general tariffs, we see no reason, for the reasons set out in the submission, why there should be any early reduction in the existing level of tariff protection which is at maximum level of 5 per cent, average level of 3 per cent. In terms of the 3 per cent impost under the tariff concession system that was applied in the 1996 budget, we think that that definitely should be removed, and in terms of policy and project by-law arrangements, we have some changes that we'd like to propose to those, in order to facilitate the importation of pulp and paper-making equipment in Australia. I don't want to go through in detail all of the submission; you've read it, but that's really the guts of it.

MR COSGROVE: That's fine. Okay, thank you. We might just take up some aspects of it with you. On page 2, you indicate that some parts of the industry are operating without any tariff protection at all but generally, I guess, it's benefiting from a 5 per cent duty. Why is it, do you think, that some parts of the industry are able to be competitive without a tariff and not others?

MR CRIBB: I wouldn't put it in those terms. I think the reason why some parts of some sectors haven't had any tariff protection are for historical reasons - newsprint, for example. Traditionally, newsprint has had no duty and that's not just in Australia but in other countries as well, because of the desire to facilitate freedom of speech and those kind of motivations. I'm not so sure why pulp has had a duty-free history, but that's certainly the case. But if you leave those two areas aside, the rest of the industry has traditionally had quite high levels of protection in the past and this fits in with the whole pattern of Australia's post-war manufacturing development, where it was common for many industries to have that level of protection. That's all been wound back very significantly over the last 15, 20 years. But particularly with newsprint, there are just straight historical reasons why it's never had tariff protection.

MR COSGROVE: I can understand the historical aspect, but the fact of the matter is it still is competitive without a tariff. There is no obvious reason why that should be the case vis-a-vis the protected sectors, except perhaps that it is efficient because it has had no tariff.

MR CRIBB: The newsprint sector in Australia certainly is efficient. I would say that the other sectors of paper manufacturing are also efficient or they have been forced to become efficient over many years. The level of protection we're talking about is not a significant level of protection, but it does provide some buffer against import competition and in many other grades of paper, such as fine papers, there has been significant competition from Asian countries, many of which have benefited over recent years from the currency collapse as a result of the Asian crisis. There have been significant anti-dumping actions that have been taken against some of those suppliers because they have been dumping product in the market. That hasn't been the case so much with newsprint, although there have been some problems in that area as well over the last little while.

I guess what we're saying is that when you have tariffs on your other inputs such as things like motor vehicles and textiles, clothing and footwear, where you have the 3 per cent impost under the tariff concession system - which was put in for purely revenue-raising reasons - to have the minimal level of protection that is left provides some offset for those additional costs. One of the arguments we've made in here is that if you're going to look at getting rid of tariff protection, it should be across the board. There should not be a situation where some sectors receive preferential treatment over others, because that adds to the input cost of the sectors who aren't benefiting from that level of protection.

MR COSGROVE: Are the PMV and TCF sectors significant input costs for your members?

MR CRIBB: All paper companies run car fleets and that kind of thing. I couldn't give you a figure on the exact percentage, but I have a number of heads of my companies either have come from North America or are North Americans and they always comment on the high cost of vehicle fleets in Australia compared to North American, for example.

MR COSGROVE: And the TCF area?

MR CRIBB: The TCF would be less significant, but there are the felts and whatever that are used for running through paper machines that the paper is formed on. I don't know exactly, but I would expect that that would add to the cost of those.

MR COSGROVE: Yes. Well, you're right to point to those input cost problems, but if we leave that to one side for the moment, what is it about the last 5 per cent on your output tariffs that is so important to be retained? I know, as you said, the industry has adapted reasonably well, it seems, to a change from much higher levels of tariff to five. Why is five to a lower figure such a difficult hurdle?

MR CRIBB: There are a number reasons that are set out in the submission, but partly it's a question of maintaining our competitive position. A lot of competitors that we're dealing with often benefit from high levels of government assistance in the first place. They often have domestic markets that are protected by their own

domestic tariff barriers and they also have very significant non-tariff barriers. By contrast, our situation is quite different from that and people say, "Well, 3 or 5 per cent is not much, just get rid of it." I think it's important to look at these costs in context because if you take each individual element of government policy and say, "Well, it's 2 or 3 per cent here and a few per cent over there," it may not appear very much, but when you put it all together, the cumulative effect is quite significant.

For example, if we are faced with the prospect of having our residual tariff protection removed, that would be 3 to 5 per cent that comes off. The industry is now having to wear additional costs as a result of greenhouse measures. For example, the 2 per cent mandated renewables target that the government is in the process of implementing will add to the industry's energy costs. You're talking about, again, a 2 or 3 per cent addition to costs there. There are a range of government policies. Just taking them one by one may not seem like a lot, but when you put it all together, it continually comes off the company's bottom line.

The other thing that's important to recognise, I think, is that the pulp and paper sector - in Australia, but also worldwide - is a highly competitive industry and the financial performance of companies in that sector has been abysmal over the last 15 years. Worldwide, if you look at the index for pulp and paper share prices compared to movements in the stock exchange index as a whole, the pulp and paper sector has been one of the worst-performing sectors - that includes in Australia - and the impacts of all these government policies makes these companies less profitable and you get into a whole cycle which is going to affect the investment attractiveness, etcetera.

I think it's important to look at these things in the context of the whole of government policy, whereas I think what we've been subject to is various parts of government imposing additional costs or removing protection without much regard to what is happening in other areas of government policy.

MR COSGROVE: Is there excess capacity globally in this industry? Is that the reason why it's performing - - -

MR CRIBB: It suffers from that, yes. It's a commodity-based industry still to a large extent, so it suffers from boom and bust-type cycles. At the moment, the price of pulp and paper is starting to improve a little. It's been in the doldrums for quite some time, but I think the pulp and paper sector has had some particular problems and part of it has been that there has been overcapacity that has been developed and has been most recently occurring in Asian markets, which as I said before are mostly protected by domestic tariff barriers, and that contributes to the problem of overcapacity and it makes our situation more difficult.

MR WOODS: Can I just pick that point up a little further? In your submission, you say there is absolutely no benefit to be gained by Australia considering or making any unilateral tariff reductions. One of our terms of reference is a request that the commission report on the costs and benefits to Australian consumers, industries and

their employees and the general community of a reduction in all general tariff rates. Is it a reasonable conclusion that there would be no benefit to Australia? I'm thinking of consumers; I'm thinking of users of your product in business who would benefit from a reduction in the tariff.

MR CRIBB: I think the rest of what the statement said was in advance of the conclusion of the next round of multilateral trade negotiations and that that's really what that comment is aimed at; that when you have a new round of trade negotiations - it was meant to get off the ground in Seattle and didn't. One presumes that it will get off the ground at some stage. From our perspective, there is no benefit in throwing away negotiating coinage in advance of some multilateral settlement. If the government's intention is to get rid of our tariff protection, which as I've said we oppose for a number of reasons, there would seem to be absolutely no point in doing that and not get something in return in the multilateral negotiations. It's a case of unilateral disarmament. I mean, why would you unilaterally make a concession when you can make the same concession in a trade negotiation and get something in return for it?

MR WOODS: Doesn't that presuppose two things, though? One is that giving away 5 per cent by Australia is actually significant in the multilateral negotiation process and also that there would be no gains to our domestic economy in us unilaterally making a reduction in our tariffs. I think it's worth exploring both of those points and I'm happy for you to take them in whichever order you wish.

MR CRIBB: In terms of the negotiating process, any concession is important. Most of these negotiations are done as some kind of a package deal and particularly if you're looking at other sectors beyond pulp and paper, if you give away all of your negotiating currency in advance of the negotiations, when you finally sit down to talk turkey with other countries to finalise a package deal, you've got nothing left to give because you've already given it away. So I think from a strictly negotiating point of view, there is absolutely nothing to be gained. In terms of benefits to consumers - - -

MR WOODS: Can we just sit on that one for a minute? We've had put to us by other witnesses that the 5 per cent by Australia, which is generally regarded as a fairly open market now anyway, carries little weight and, in fact, you could suggest that Australia's negotiating position as an open market, ie having no tariffs, might have as much moral value as a giveaway of 5 per cent residual on the tariff side, so we're having counter arguments put to us by other industries.

MR CRIBB: Others may put that view, but from our experience in multilateral trade negotiations, anything you have to give as a concession is important and it doesn't matter how small it is. Other industries are entitled to their opinions, but we certainly don't share that opinion. I think the experience of multilateral trade negotiations suggests that that's not correct, the view that you've put that others have said.

MR COSGROVE: That's a point I was going to mention, that it has been

Australia's experience in recent negotiations that we have been given credit for unilateral reductions which we've made in the bargaining process. In other words, leadership can have some effect, just as you claim following might.

MR CRIBB: I would say we have already. If you look at our position, particularly compared with some regional competitors, we are a long way ahead of the game. It would be nice to see some other countries exercise some leadership for a change and voluntarily give most of their tariff protection. Why should Australia always be the first one to take the lead in these matters?

MR COSGROVE: I don't think we've been the first.

MR CRIBB: Certainly in the pulp and paper sector, we have one of the most open markets in the world, particularly when you take into account non-tariff barriers, and as we've said in our submission, from our point of view, the onus should certainly be on other countries to catch up, to make the opening gambit. If they're seeking to get the kind of credibility that flows from that, well, I think they're welcome to it.

MR COSGROVE: Have you thought about how such an approach might actually be put into practice? At what point would your association be satisfied that enough had been done by the rest of the world to enable us to do more?

MR CRIBB: During the APEC negotiations on early voluntary sectoral liberalisation - the EVSL negotiations - quite significant progress was made towards that. For example, there were going to be commitments, particularly on the non-tariff barrier side; there was going to be a review of non-tariff barriers by all economies in the APEC region. It was envisaged that these would be incorporated into annual action plans on which economies would have to report, all of those kind of things. I mean, we still had reservations to quite an extent about some parts of it, but overall, particularly in terms of non-tariff measures, we were quite encouraged by the direction in which those negotiations were going.

They, I guess, ran into the sand, or they have been now passed on to the WTO effectively, is my understanding of them. I haven't been following it that closely over the last little while. But we were actively engaged in that process and we were talking with government, and, as I said, we were quite encouraged by the progress that was being made, particularly in the non-tariff barrier area. Unfortunately, perhaps what was being proposed was too much for some of those economies to agree to.

MR COSGROVE: That may be, although there remain the APEC free trade and investment commitments for the developed members by 2010, and the developing countries by 2020. But I'm trying to think more in conceptual terms. I mean, would you see as a requirement that, let's say, every paper-producing country had a tariff on every individual line of production of no more than 5 per cent before Australia should move?

MR CRIBB: That would be an ideal situation, certainly. We can talk in conceptual

terms but unfortunately the reality of negotiations rarely meets the theories. If our major competitors were prepared to have a similar level of, or similar lack of, protection that we have - and, again, particularly in the non-tariff area which is particularly troublesome in the paper industry - if other countries were prepared to do that then the arguments that we would have for retaining our protection would be greatly diminished, if not eliminated. But the reality of the situation is that it is not like that.

MR WOODS: Could you elaborate on the non-tariff protection? Are we talking subsidy to industry, or are we talking about subsidy of raw material inputs?

MR CRIBB: There's a whole range of things. I'll just give you one example: Malaysia has recently completed its first newsprint mill, and our primary feedstock for that newsprint mill is wastepaper generated in Malaysia. So to ensure that that mill has a supply of wastepaper, and that the wastepaper can't be exported, the Malaysian government has banned the export of wastepaper in order to guarantee that mill a low-cost supply.

MR COSGROVE: That's not too good for the Malaysian wastepaper producers, is it?

MR CRIBB: No, it's not. It's very good for the mill.

MR COSGROVE: Yes, but you see, as Mike was pointing out a little while ago, in our terms of reference we're required to look at a broad range of effects including those on the community in general.

MR CRIBB: Sure.

MR COSGROVE: The sort of subsidy, in effect, that you were just identifying does come at a cost to another part of the Malaysian economy.

MR CRIBB: That's right.

MR COSGROVE: So it's not an unequivocal gain. In fact it may well be a loss, for all I know.

MR CRIBB: To come back to the second part of your question earlier on about the similar impacts in Australia from the level of our protection, my industry doesn't accept the purist, free-market theory that there is a level playing field and that you should get rid of all protection because it's good to do so in itself. I think it's good to look at some of the longer-term impacts that removing residual levels of protection may have on an industry such as pulp and paper. For example, if that contributed to the industry's decline in Australia, that would have impacts on the balance of payments. We already have a large trade deficit in pulp and paper.

However, as we point out in the submission, if we had no industry at all in

Australia we would have a much larger trade deficit, about three or four times as high. The industry is located in many regional areas of Australia, such as the Latrobe Valley, Mount Gambier, Albury, Tasmania, areas like that. The industry has very long-lived capital equipment. When plants get built, they stay there pretty well forever, and those plants underpin and generate high value, long-lasting jobs for the community. There are a whole lot of spin-off economic benefits. So there may be some temporary, short-term gain for consumers if the price of paper was a little bit lower because you removed our - - -

MR COSGROVE: Why would it be temporary?

MR CRIBB: It may not be temporary, but there may be some short-term gains.

MR COSGROVE: I'm not even sure why it should be short-term.

MR CRIBB: It would depend on how - - -

MR COSGROVE: If the tariff is having the effect of assisting existing producers then presumably its removal will permanently result in lower prices, if there's adequate competition, and there seems to be from what you're saying.

MR CRIBB: Sure.

MR COSGROVE: It's the nature of the industry.

MR CRIBB: Yes, but we're talking about 3, maximum 5 per cent, level of tariff.

MR COSGROVE: Yes.

MR CRIBB: I'm not talking about a huge gain for consumers here, as compared to some other sectors. It's one of these things that governments and societies have to make a decision about. That's their role.

MR COSGROVE: It's a judgment.

MR CRIBB: But our judgment is that some of the other longer-term economic impacts would be quite significant, and whether they are compensated for by the small gain in price that you may achieve is another question, I think.

MR COSGROVE: I was struck in this context, Bridson, by the early statement in the submission that the industry directly employs 8000 people but has a further impact on the employment of an additional 100,000.

MR CRIBB: Yes.

MR COSGROVE: That seems to be very high leverage from the industry

employment.

MR CRIBB: That's the best estimate we have. Those aren't recent figures, they're about two or three years old.

MR COSGROVE: Even so, how do you get such a pronounced amplification?

MR CRIBB: For a start there's a lot of, for example, contract maintenance jobs - sorry, there are a lot of maintenance positions and those kinds of things which - effectively people who are directly employed in mills - that are being contracted out. So there's a whole pool of people like that. Then there is a very wide range of supply companies. I don't know if you've ever been to a pulp and paper plant but, in terms of physical size and capital cost they are literally huge undertakings and they consume a whole range of goods and services, from computer equipment to lubricants, to fabrics that go through the machines - there is a very wide range. Then there's the whole transport sector that runs off that. You have plants scattered all around Australia. You are shipping product all around the country. You have wastepaper which is being shipped around the country. There's a whole collection network for collecting wastepaper. You know, that figure is casting the net very broadly, but if you didn't have a paper industry there are a lot of jobs that would be affected.

MR COSGROVE: Some of those functions would continue in a situation where the domestic market was supplied entirely by imports, I guess - the transportation of the product - - -

MR CRIBB: The transportation ones, transportation and marketing perhaps.

MR WOODS: And the wastepaper collection. There would still be some form of industry in those areas presumably?

MR CRIBB: Probably not. I mean my industry is the main consumer by far of wastepaper. I mean, if we weren't there, why would you bother to collect it?

MR WOODS: Is there no external market for it?

MR CRIBB: There are very small exports of wastepaper. You know, wastepaper is not exactly a high-value commodity. So in terms of environmental perspective on that aspect, if there was no pulp and paper industry in Australia I doubt there would be a paper-recycling industry.

MR COSGROVE: You mentioned, in the section of your submission which addresses project by-law arrangements, that the way the policy is interpreted and implemented makes it impossible for you to get pulp and paper-making machinery into Australia duty free. Could you explain a little what it is about the interpretation and application of the policy that is the problem?

MR CRIBB: Sure. First of all, under the tariff schedule the pulp and paper-making

equipment is certainly meant to come in as zero tariff. There are no local manufacturers. In fact there are very few manufacturers in the world. It is highly specialised, complex engineering equipment. In terms of paper-making equipment, I think there are now only three, possibly four, companies in the world that make it. It's such a specialised business. But the main problem is policy by-law, item 43. In order to gain this duty-free access, this policy by-law requires the machinery to be shipped by a single, overseas supplier as a single shipment and to enter through one shipping port, and that is just completely impossible.

Visy Industries is running into these problems at the moment, or will run into these problems with its new plant at Tumut. But the most recent example that has been completed was Amcor's completion of a new paper machine at Maryvale. They already had four paper machines, this was bringing in a fifth paper machine. The importation of that paper machine, or the parts that make up that paper machine, took place over a period of 14 months. The machinery was shipped in approximately 180 containers and the number of import entries was in excess of 200. So because of that, it's very hard to actually achieve duty-free entry in reality.

MR COSGROVE: Is part of the problem that these machines are so large that they can't be shipped in a completed form?

MR CRIBB: Most definitely. They are huge pieces of equipment. Also, because it's such a specialised business, even if you are buying the equipment from one company bits of the equipment may be coming from that company's operations all around the world. So you could have part of it that comes from Germany, part of it comes from Brazil, part of it comes from Scandinavia. Even the company that makes the machinery doesn't ship it from the one destination.

MR WOODS: As we understand it, that's where the issue in this particular area lies, in that because it's multiply-sourced then the argument goes that therefore Australia may be able to contribute some of those particular elements. Obviously not the mainframe and the specialised parts, but some more of the standard componentry. But it would be helpful if you could give us a case study or something that demonstrates the point you're making, to give some more substance to this particular issue.

MR CRIBB: Would you like me to send that to you in writing?

MR WOODS: That would be helpful.

MR COSGROVE: Yes, fine.

MR CRIBB: Sure, okay, I'm happy to do that.

MR COSGROVE: I think you mentioned that you had some suggestions for improving this situation?

MR CRIBB: Yes, we have a proposal before government at the moment on how we think it could be improved. One of the ways in which we think it could be improved is, for example, the capital cost of Amcor's Maryvale machine was \$330 million. That's for one machine. So obviously any significant importation of this equipment is, by definition, a major project. Basically what we're proposing is that the supplier company should identify up-front what are all the component parts that make up the equipment, so you get an up-front definition from the relevant government authorities as to what actually constitutes a piece of pulp and paper-making equipment, so that's defined in advance.

Then, as the equipment comes across the docks or whatever, it will be suitably identified as being part of this special, major project, and it has already been identified in advance as being part of a pulp and paper-making machine and therefore it automatically qualifies for duty-free entry, and it would come in that way.

MR WOODS: So you have a front end once-only approval?

MR CRIBB: That's right.

MR WOODS: Rather than then being challenged on each of the bits as to whether there's an appropriate - - -

MR CRIBB: That's right, that's the guts of what we're proposing. Obviously you have to preserve the integrity of the customs system and that kind of thing. That could be achieved through audits or a paper trail or whatever. There are various methods of doing that. The requirement for active, physical inspection of every single piece of the thing that comes across the docks when it has already been identified in advance would seem to be unnecessary. The companies could enter into a particular arrangement with the relevant authority as to how this could be done.

MR WOODS: That approach is not dissimilar to in fact how the scheme operated some time ago. Is that true?

MR CRIBB: I'm not fully familiar with how the scheme used to operate, but I understand that there were concerns - I'm not sure whether it was my industry or another industry - that there were abuses of the system. So we're conscious of the fact that that's something that government obviously wants to prevent and it's not something that we want to encourage. But we're trying to find a solution that will ensure that doesn't happen, but will still allow us to import our equipment.

MR COSGROVE: We don't have any further questions, Bridson. Is there anything else you wanted to say to us?

MR CRIBB: No, that's fine, thank you.

MR COSGROVE: If you could provide any material along the lines that Mike was inquiring about, we'd be grateful.

MR CRIBB: Yes, I'm just making a note of that. Thank you very much. I appreciate the opportunity.

MR COSGROVE: Thank you for coming. There are no further participants today, so we'll adjourn and resume the hearings in Sydney on 27 January.

AT 2.36 THE INQUIRY WAS ADJOURNED UNTIL
THURSDAY, 27 JANUARY 2000

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