



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

ECONOMICS LEGISLATION COMMITTEE

**Reference: Customs Amendment (Warehouses) Bill 1999 and Import
Processing Charges Amendment (Warehouses) Bill 1999**

WEDNESDAY, 4 AUGUST 1999

MELBOURNE

BY AUTHORITY OF THE SENATE

INTERNET

The Proof and Official Hansard transcripts of Senate committee hearings, some House of Representatives committee hearings and some joint committee hearings are available on the Internet. Some House of Representatives committees and some joint committees make available only Official Hansard transcripts.

The Internet address is: **<http://www.aph.gov.au/hansard>**

To search the parliamentary database, go to: **<http://search.aph.gov.au>**

SENATE
ECONOMICS LEGISLATION COMMITTEE

Wednesday, 4 August 1999

Members: Senator Ferguson (*Chair*), Senator Murphy (*Deputy Chair*), Senators George Campbell, Chapman, Gibson, Murray and Watson

Participating members: Senators Abetz, Boswell, Brown, Conroy, Coonan, Faulkner, Harradine, Lundy, Parer, Quirke, Ridgeway, Schacht and Sherry

Senators in attendance: Senators Chapman, Gibson and Murphy

Terms of reference for the inquiry:

Customs Amendment (Warehouses) Bill 1999 and Import Processing Charges Amendment (Warehouses) Bill 1999

WITNESSES

McDONALD, Mr Ross, Manager, Government and Investor Relations, BHP Steel	2
NORTON, Mr Alan Edward, Manager, Property Newcastle, BHP Long Products	2
WOODWARD, Mr Glenn, Manager, Tariff and Trade Services, BHP Steel	2
MULDOON, Mr Kenneth Robert, Customs Affairs Manager, DHL (Australia) Pty Ltd	10
MORRIS, Mr Allan Agapitos, Member for Newcastle, House of Representatives, Parliament of Australia	16
JEFFERY, Mr John Harland, National Director, Commercial Division, Australian Customs Service	20
McCULLOCH, Mr Alan Barton, Assistant Manager, Customs Policy Section, Department of Industry, Science and Resources	20
WEBB, Mr Robert John, Manager, Customs Policy Section, Department of Industry, Science and Resources	20

Committee met at 0.00 p.m.

CHAIR—Today the committee is considering the Customs Amendment (Warehouses) Bill 1999 and the Import Processing Amendment (Warehouses) Bill 1999, which were referred to the committee by the Senate for inquiry and report by 10 August this year. This is a public hearing and, as such, all members of the public are welcome to attend. Today we will be taking evidence from two organisations and a member of parliament who have made submissions concerning certain provisions of the bills. We will also receive a response from government officials on comments made during the hearing. To assist all parties involved with the inquiry, I propose that the committee agree to publicly release all submissions received during the inquiry, except those to which confidentiality applies. There being no objection, it is so ordered.

Before we commence taking evidence, I wish to state for the record that all witnesses appearing before the committee are protected by parliamentary privilege with respect to evidence provided. Parliamentary privilege refers to the special rights and immunities attached to the parliament or its members and others necessary for the discharge of the parliamentary functions without obstruction and fear of prosecution. Any act by any person which operates to the disadvantage of a witness on account of evidence given by him or her before the Senate or any of its committees is treated as a breach of privilege.[1.00 a.m.]

McDONALD, Mr Ross, Manager, Government and Investor Relations, BHP Steel

NORTON, Mr Alan Edward, Manager, Property Newcastle, BHP Long Products

WOODWARD, Mr Glenn, Manager, Tariff and Trade Services, BHP Steel

CHAIR—Welcome. Do you wish to make an opening statement?

Mr Woodward—I do. Thank you for providing us with the opportunity to discuss our submission with you. We feel that any such economic discussion can only be a positive step in building a more user-friendly manufacturing in bond system. As you can see from our submission's executive summary, BHP Steel has expressed its support for the passage of both bills in their current format. This does not mean that we are blinkered to any initiative that leads to an improvement of the proposed system or the bills. We also believe that, in our time before you today and at any time in the future, we will continue to demonstrate our commitment to achieving a commercially viable and economically responsible manufacturing in bond system. A commitment to that has evolved from 1996 onwards, when we first advocated the establishment of a foreign trade zone in the Newcastle area under the BHP banner name of Steel River.

In addressing our submission, I will make one point about the import processing charges amendment. I suspect that it has bipartisan support, and it certainly has industry support. Anything that reduces our cost impediment and makes us more commercially viable we support in any shape or form.

There appears to be a problem at the nub of the issues that we are to discuss, and that is the tariff treatment of goods as they enter the domestic economy if they are diverted from exportation. Remember that the Manufacturing in Bond scheme was initiated to facilitate export orientated industries. We would expect, as those systems came into place, that the majority of the goods produced in the manufacturing in bond environment would be for the export market. We honestly do not know—it is a bit of crystal ball gazing—what percentage would be diverted in domestic consumption.

The tariff treatment is affected by both bills. Our case has already been stated. We support the tariff treatment on the input of the goods as they were introduced into the manufacturing in bond situation. We say this because we are business unit driven and downstream customer driven. We have canvassed our downstream customers and business units. All those businesses and a number of industry associations have supported the input scenario.

We can certainly move on to other points of the submission when we get into our cross-examination, as I will call it. We believe that we have a flexible alternative which can satisfy all parties in this tariff treatment. It is based on documentation submitted to the then Department of Industry, Science and Tourism in 1997, when the Newcastle Beyond 2000 Committee put forward a discussion paper entitled 'Proposal for the introduction of a foreign trade zone in Newcastle—a potential model for Australia'. It encompassed our original proposition of a US-based model not entirely being utilised in Australia but certainly having the eyes picked out of it.

The major issue under consideration today about the tariff treatment of goods entering the domestic economy is fully addressed in that discussion paper. A foreign trade zone board was appointed to administer the foreign trade zone scheme and individual economic assessments could be made of each manufacturing in bond proposal put before that board. They have a variance which allows a tariff treatment on either the finished goods or the input goods.

We suspect that there are opportunities to explore, through the customs regulations that have already been proposed, the application process of manufacturing in bond that could help facilitate that type of treatment and, therefore, be fair and commercially equitable to all parties no matter where they are from, be it the IT sector, the manufacturing sector, pharmaceuticals, chemicals or whatever. We think that flexible approach will deliver a far more competitive advantage to all Australian industries plus promote local manufacturers to be part of a Manufacturing in Bond scheme. That primarily concludes my opening statement.

CHAIR—Do either of your colleagues wish to add to the opening statement?

Mr McDonald—No. I think that is okay.

Mr Norton—No, thank you.

Senator MURPHY—At point five of your submission you refer to case study No. 4. I would be interested in your elaborating on that a little more. If I understand what you have just said about the application of the flexibility arrangement, a board would make a case-by-case assessment of the circumstances confronting the company or industry with an MiB application?

Mr Woodward—Yes.

Senator MURPHY—It is currently proposed that there be a single licensing, single strain approach. It would be useful if you could expand a little more on case study No. 4 and on your view about the MiB being treated as an export destination; I assume that also fits in with what you have just proposed.

Mr Norton—Case study No. 4 is a simple study to try to illustrate our point about the potential impact on a domestic manufacturer if the end product were duty free. We picked it very quickly out of our experience and nominated the harmony codes associated with it. But the impact of this could apply to any domestic manufacturer who potentially could supply a manufacturer who is an MiB licensed manufacturer.

Prima facie as things stand at the moment, a manufacturer in an MiB can take the goods in duty free and manipulate manufacture, assembly or whatever to produce his final product. Still considering case No. 4, if the duty is charged on the finished good, that manufacturer could import to the detriment of an established Australian manufacturer. That could then effectively start to cause that Australian manufacturer to consider relocating offshore to be able to again enjoy those competitive advantages. It could start to work to the detriment of Australian industry.

Senator MURPHY—It would not be overly helpful either to someone proposing to set up, let us say, a barbed wire manufacturing process in this country, would it? You say that imports would come in duty free?

Mr Woodward—The finished goods, in this example.

Senator MURPHY—If the finished barbed wire is manufactured in the country—and we will get to the GST a bit later—if I understand what is in your submission, you would have to pay. Do I understand you correctly? You say:

The wire enjoys a 5% tariff assistance, yet the finished product, barbed wire [Tariff Item 7313.00.00] may be entered duty free. That Australia can compete in its own market to produce the majority of the barbed wire consumed in Australia attests to the efficiency of the Australian rural products producers. However, removal of the duty on the feed wire by production of barbed wire in an MiB would disadvantage the Australian wire industry . . .

Mr Woodward—They currently receive tariff assistance of five per cent. Effectively, if that were removed—

Senator MURPHY—Yes, if it were removed.

Mr Woodward—Yes. They are currently competing in a very viable way against the finished component, which is entering duty free. So we were using that example of the finished goods scenario to say that there are various tariff anomalies for finished goods or inputs right across the tariff. It is very hard to categorise them into sectors as such because there are thousands of tariff items, and I do not think a full economic assessment has been done of the inverted tariff situation. But this was one quick case study that came up in the time frame we had in which to put the submission together.

Senator MURPHY—Where, under the implementation of this legislation, you could—and probably inadvertently—disadvantage the domestic manufacturer.

Mr Woodward—Absolutely, yes, especially if we went to a finished goods situation. In an either situation, if you make the legislation as it stands go through, it will disadvantage certain sectors—it is setting up against MiB—as you would do if you went for finished goods. What we are trying to improve upon with our initial submission, which again is business unit and customer driven, is a flexibility whereby the manufacturing in bond situation would be enhanced. You could—be it through regulation, administrative guideline or some discretionary ability—have an applicant for an MiB facility having to put in an economic statement as to local manufacturing capability and the possible detrimental effect for an MiB licence being created. You could then link it to either way of tariff treatment.

Senator MURPHY—Is this something that your proposed board, when it gets an application, could consider?

Mr Woodward—Yes.

Senator MURPHY—They could consider local industry.

Mr Woodward—We used the foreign trade's own model from the US because that was the best one we found in our search around the world. I would anticipate that board not being set up in Australia's model. I suspect that the Department of Industry, Science and Resources would receive the initial application. What an applicant has to do is very well documented in the regulations at the moment. There is scope within those regulations for a licence to be granted upon certain considerations. So it would not necessarily mean the creation of another bureaucracy. I would like to see it being kept within an industry policy department. It could certainly be done within industry, science and resources.

Senator MURPHY—Where you would provide a process for the domestic industry, when they were aware of an application being made, to say, 'Look, this will have a detrimental effect on us'?

Mr Woodward—Exactly. I suspect that, even in our Steel River situation, where we as BHP are currently promoting the input tariff regime, we would obviously want the finished goods as well when there was not a local manufacturing industry to assist, especially in the IT situation.

Senator MURPHY—Does BHP have a view about MiBs being virtual reality rather than specific or zone specific?

Mr Woodward—We do.

Mr Norton—We do. We proposed that initiative some time ago. We have had a number of discussions with officers from the Department of Industry, Science and Resources and from Customs about this. I think it is fair to say there is a general consensus that this could happen. We need to work through how it should go ahead.

Through this, we are seeking to foster opportunities for small- and medium-sized enterprises to gain the benefits of manufacturing in bond. This will enhance their export potential, development and employment growth whilst not overburdening them with the appropriate administrative cost structures which are necessary to reimburse the various government bodies and so forth. By putting a number of small SMEs together under a single licence, the idea is that a competent organisation, such as a forwarding organisation, would then administer those sub-licences, so to speak, and have one point of contact with Customs. Therefore, economies of scale would be introduced in administering the process and, at the same time, economies of cost structure would encourage small- and medium-sized enterprises to use this government initiative.

Senator MURPHY—Licence costs are not necessarily your problem, I suppose. But there is probably a bit of an inequity between small enterprises versus large industry. What is your view about that?

Mr Woodward—We have not addressed it as such. But certainly the start of any reduction in import processing could flow through to the licensing of warehouses et cetera in making industry more competitive. Take a single-licence operator for a warehouse under the current scheme with a successful manufacturing in bond facility of \$7,000 and a \$4,000 annual renewal fee. If, as my colleague Alan states, that were to be spread over a number of associated organisations under a one-operative licence, that could do it.

As we have gone to an owner-onus situation with industry in dealing with government, I would like to see us get, say, an audit facility. Why should we pay a licence fee when effectively the government is using all our financial business reporting systems? Rather than conducting their own separate audit, they do a systems based audit on our company records. You might be able to reduce or even have a zero licence fee. Effectively, the applicant is doing all the work, and it would be a minor check, perhaps. Perhaps my industry, science and resources colleagues would disagree with me, but I would like to see a reduction or certainly a spreading of that onus.

Senator MURPHY—That is probably a valid point. It might save some of our industry and science colleagues from some bureaucratic effort.

Mr Woodward—Yes.

Senator MURPHY—Do you want to add anything to the issue of the MiB being treated as an export destination?

Mr Norton—We see that as an important benefit for the competitiveness of Australian industry. A manufacturing in bond facility could now theoretically both import goods from overseas and get them domestically. Prima facie suppose the product costs the same both domestically and imported before the imposition of any embedded duties or the GST. Once those duties or GSTs are applied, the domestic product is disadvantaged to the imported product. Designating an MiB as an export destination levels the competitiveness for the domestic manufacturer. Again, it reinforces the underlying policy idea behind this project, which is employment generation and economic development.

Mr Woodward—Obviously we are trying to foster as many local component manufacturers to participate in these Manufacturing in Bond schemes as we can rather than just have an offshore facility located onshore.

Senator MURPHY—It is not inconsistent with what the government has said in respect of the GST.

Mr Woodward—Exactly.

CHAIR—Pardon my ignorance, but does your company run an MiB scheme?

Mr Woodward—No, we do not as yet; we hope to.

Mr Norton—Perhaps I can give you some background. I was involved in setting up the Steel River project. In setting that up, we went out and looked at how we could make this site competitive internationally. There were a number of factors. One of them was MiB, which was then foreign trade zones. We set out to attract them and to seek policy amendment for them.

We will be setting up an MiB operation as we start building and constructing on the site. Our partners, Baulderstone Hornibrook, are already working collaboratively with us in that area. We are also working collaboratively with local businesses and local freight forwarding agencies in determining how that can go ahead. The concept of this single-licence multiple-user application has enormous attraction for small businesses in the Newcastle area. So, yes, we are planning for it.

CHAIR—How large a business are you talking about?

Mr Norton—We think the single-licence multiple-user type facility would attract multiple businesses of up to 15 people. They are small enterprises but, by being able to access this system, they will grow and employ more people. Ultimately, they may become much larger organisations.

CHAIR—But what will be the size of the business you are currently planning to be an MiB? What size turnover are you talking about?

Mr Norton—We would be trying to set up a facility to handle maybe 10 or 15 initially.

CHAIR—How many dollars in annual turnover? Give me a feel for what we are talking about. Will it do a tiny bit of business or be a large business?

Mr Norton—One organisation we are talking to directly will be a unit by itself. They will employ 1,100 people and turn over \$700 million per annum. At the other end of the scale, in the multiple-user single-licence application, they could be \$50,000 to \$100,000 per annum; that is at the extreme end, the bottom end. People we have spoken to in Newcastle who are interested have turnovers of \$2 million to \$3 million a year.

CHAIR—Obviously the concern is about tariffs on the imports into an MiB scheme. The minister has announced that the Productivity Commission is going to look at import tariffs anyway. What is your company going to say to the Productivity Commission?

Mr Woodward—We have already made a submission on nuisance tariffs. I am fairly certain that the charter of the Productivity Commission encompasses follow-up to nuisance tariffs as opposed to Australia's general tariff rate of five per cent. As a BHP entity, we are currently undergoing a massive restructure. My colleague on my right and I will be formulating, along with the rest of the BHP entity, a position for the Productivity Commission's hearing into general tariff because it has also been announced that tariff concessions and policy by-laws will be looked at.

Hopefully, I am saying the right things here; this is probably more in Ross's line. As a general policy stance, BHP as an entity rather than BHP Steel—remember that there is BHP Steel, Petroleum, Minerals, Transport, et cetera—has fully supported the government's initiatives, whichever government has been in power, from 1988 onwards regarding tariff reduction in a structured fashion. I suspect that our policy directive will still be following those lines. Our businesses—I am speaking for BHP Steel here—have certainly followed that tariff policy and the structured reduction thereof in our offshore and onshore business investments in seeking finished goods, components or whatever. So the policy should continue along those lines as to Australia's commitment with APEC or whatever.

Mr Norton—Australia's manufacturing base is under severe pressure at the moment. Any further erosion of competitiveness, we think, will continue to result in sell-offs and closures of many downstream parts of industry. Australian manufacturing is under a lot of pressure from reviews of both reductions in nuisance tariffs and the general reference. In certain items, Australia is the only producing country that does not have any form of tariff assistance. That makes it tough going internationally. I think you could question whether the balance is starting to get out of vogue, because we are finding increasingly that many of our export items into the Asian markets are not experiencing a reduction in tariffs as we are here in Australia.

Mr Woodward—In our recent example of the nuisance tariffs inquiry—I think that is an absolute misnomer, especially for manufacturing in steel—the so-called nuisance tariffs amounted to something like \$1.2 billion of market share. We do not see that as a nuisance tariff.

Senator CHAPMAN—As I understand your evidence, you propose some sort of administrative structure to determine whether items manufactured in bond going to the Australian market should have the tariff applied on the completed product or the components?

Mr Woodward—Since we put in our initial submission, we have been in consultation with various industry associations and other proponents of Manufacturing in Bond schemes. This issue has certainly become what we believe is the crux of the matter. We have not delved into this in entirety at the moment but, certainly under current regulations, there are provisions for an applicant to fulfil his role in providing certain information to Industry, Science and Resources upon application. That could then even have a discretionary function in an economic impact study if those goods were to be diverted into home consumption. An assessment could then be made as to how to treat the goods, either on the finished goods or the input component.

We have not had an absolute brainwave here, but certainly it could be done through regulation or some form of administrative guideline rather than through the initiation of reams and reams of dogmatic legislation. We are using the foreign trade zone US model, which certainly has the flexibility we need. Each applicant is considered for MiB acceptance in the US, and the components and the finished good tariff treatment is assessed on that application. Even though I have mentioned the foreign trade zone board, we do not see the need for more government departments to be created.

Senator CHAPMAN—Another submission we received argued that applying the tariff to the components rather than the finished product could diminish opportunities for manufacturing in bond in Australia.

Mr Woodward—We can certainly see that in an inverted tariff situation, and there would be examples. With the tariff in so many thousand items, you will always get a possible winner-and-loser situation if you have but one judgmental criteria. What we are now promoting—and

we could possibly put in a supplementary submission to our initial submission focusing on this—is that if you had the flexibility to go either way, you would encourage all the sectors, local manufacturing and the offshore investment that you are hoping to attract to Australia. But we are now thinking along the lines that if you just go with the current legislation as it stands and have it on imports, perhaps you are denying some other industrial sectors as well. We would like to see there being flexibility.

Senator CHAPMAN—If you go the other way and have it on the finished product, isn't that going to encourage more manufacturing in bond so that you will have a bigger manufacturing cake to which Australian components will have access? Even though there might be imported components also having that access, you are going to have a bigger cake.

Mr Woodward—It will depend on each business case as an applicant puts up for a manufacturing in bond licence. Remember that they have to go for a warehouse licence first and then follow through to a manufacturing in bond licence with a business case which sets out some three years hence what they intend to do with their sales. Both export and potentially, you could ask whether they are going to be diverted to local manufacture. So that business case could be judged at that time. Without knowing the business case, I would be indulging in a bit of crystal ball gazing.

Senator MURPHY—There would have to be a meeting of trade obligations under GATT et cetera.

Mr Woodward—Absolutely. Australia's commitment to, say, anti-dumping or the WTO and the World Customs Organisation would have to be paramount; we cannot be usurping that as well.

Senator CHAPMAN—You say that there should be some case-by-case consideration of the tariff rather than a consistent determination made that it is on either the finished product or components.

Mr Woodward—That is exactly what we are saying. Our Steel River project could benefit from both. If I do crystal ball gaze—Alan has done more of this than me because he is attracting customers there—some of those people who may use chemicals or resins may want the finished component. Other people, such as those in the automotive industry, may want inputs. It will vary on a business case. That is the problem with having the legislation as it is at the moment. When and if people decide to take up a manufacturing in bond situation, you run the risk of denying them the economic advantage. It could be created with a flexible approach, a discretionary approach.

CHAIR—I think we understand what you are currently proposing. We do not have much time. Perhaps a supplementary submission would be useful. We have to report to the parliament next week, and perhaps you could just put that additional point in writing to us; the committee would find it useful.

Mr Woodward—Certainly.

Senator MURPHY—We would like to get that supplementary submission, I assume, before we actually finalise the report.

CHAIR—Yes. There is no point in doing it unless we can get it before we report. So we really have to have it by the end of this week. Friday is the deadline. You have made the point clear to us. But, just to help other senators belonging to the committee, it would be useful to have that in writing from you. That completes our hearing of your evidence. Thank you for coming along and thank you for your submission.

Mr Woodward—Thank you for this opportunity, Mr Chairman and Senators.

[1.33 p.m.]

MULDOON, Mr Kenneth Robert, Customs Affairs Manager, DHL (Australia) Pty Ltd

CHAIR—Welcome. Do you have an opening statement?

Mr Muldoon—Yes. We have already lodged a submission to this committee hearing. DHL, for those who do not know us, is an express freight company. We are not manufacturers. Our involvement in this is not so much a direct interest as an indirect interest. I would like to put that into a bit of perspective.

Quite often companies that are manufacturing around this world come to logistic suppliers like DHL looking to set up regional distribution centres or regional manufacturing centres. Quite often our Asian operations are approached by companies, for example in the US, that would like to establish a distribution or manufacturing centre in Asia. As one of their considerations, they will look at where they can service an Asian market from. They come to companies like DHL and say, 'If we were to set up in Asia, where should we set up so that we can service these markets in a timely manner?'. This is in a world of just-in-time or on-time supply chain management.

DHL Australia got involved in this because Australia quite often was not making the consideration lists when that was happening. Hong Kong, Singapore, Indonesia, Malaysia and China were obviously getting on these lists and Australia was not. So DHL said, 'If DHL Australia is to prosper, we obviously need to get Australia on these lists.' It is there that we looked at what are the disincentives. In fact, we find that there are not too many disincentives but more positives for Australia. We have an educated work force, low land costs compared with places like Hong Kong, good infrastructure and, most recently, political and financial stability. Something people do not realise is that, while we may be some distance away from our Asian market, in fact it is quite often cheaper to fly goods out of Australia into many Asian centres than it is to fly from Asia to Asia out of Singapore because of the cheaper line haul rates out of Australia.

So we looked at all the positives and then tried to look at the negatives. One was the perception of distance. I think companies like DHL are trying to overcome that by providing overnight services into Asia. Another was some customs compliance issues. Companies would, almost on a checklist, say, 'Customs in Australia? No, it does not do as well as a free trade zone in Indonesia or Malaysia.'

I suppose that background lets you know why DHL got involved in this whole discussion. Our view is that, if we are to succeed as a company, there should be more import-export trade for Australia. Hopefully, that is a good thing for our company and for Australia.

It was there that we got into the talk of foreign or free trade zones. Understandably there were some problems with the concept of free trade zones, particularly socioeconomic concerns. I will later talk about Bluegum in Wangaratta. A big concern is that, if a free trade zone were set up only at the international airports or sea ports, you would have companies moving from regional centres. There is the idea of Australia's advanced customs treatment, which does not rely so much on where you are. I think our customs service has moved a long way from dealing with the physical control of goods to the documentary control of goods; the MiB scheme seems at least to have moved some way towards that. It was also seen by the government as a very quick fix because regulations and legislation were already in place that had allowed for MiB a decade ago. So the government allowed through just the regulatory change for MiB to come in. This was, I suppose, a precursor to something like Tradex, which is before parliament at the moment.

So we ended up with MiB about 18 months ago. Unfortunately, it still suffered from some detriments, one of which was the cost recovery issue. Rather than just sitting back, we have lobbied very strongly for the cost recovery issue to be addressed. Fortunately, it has been addressed, and certainly we welcome that as part of this legislative package.

The second issue that is part of this legislative package is more of a concern to us. We have heard the debate already between you and BHP on the tariff treatment. I think that is a very complex issue. Personally, it is unfortunate that it has been lumped in with the cost recovery issue, because the cost recovery issue has received bipartisan support with everyone agreeing that it should flow through into legislation. We certainly—I want to make this point up front—do not want to see the legislation for cost recovery jeopardised by a longer debate on the tariff treatment of goods.

We have been trying to attract new manufacturing capacity into Australia. One of our prime focuses has always been how we can compete against the free trade zones in Asia. About 10 years ago, the Industries Assistance Commission forecast that free trade zones in Asia would effectively be a failure and that Australia should not follow that model. I like to think that maybe they were wrong and, unfortunately, that we are in a bit of catch up now. With that in mind, I suppose it was always a concern to us when it was mooted that Customs might look at treating goods as the components and not as the finished product. In many ways, we are, you may say, in some ways biased in that the companies we are talking to tend to be in the high-tech IT industry where you may have duty on components. In most instances, however, the finished products are duty free.

In trying to compete, we have to explain to these multinationals looking to invest in Asia that we have something equivalent to a free trade zone but that you do not actually pay duty attached to your finished product because you still treat it as components. We saw that as a fundamental problem in our discussions with them, particularly in the IT industry. That is where our biggest concern is, and it is certainly addressed in our submission. We are particularly concerned about legislating the tariff treatment in the Customs Act. If perchance in six months we say, 'Well, that was a bad decision,' with it having gone into an act rather than into regulation, we are very concerned about our chances of getting it changed. There was previously a regulation that treated MiB goods going into the Australian market. That regulation allowed for the duty rate to be the lower of those on the finished product or the components.

Our initial submission, of course, has always favoured that lower approach. However, having spoken to companies like BHP and other companies in other sectors, we can see that there could be some fundamental problems if you look at it sector by sector. Accordingly, we obviously support the concept of flexibility in a scheme allowing for a beneficial treatment for sectors like IT and a component based one for other sectors.

We are not manufacturers but, from the philosophical base, it is clear to us that the IT sector is a very important sector. We have certainly been approached by some very large companies—the Intels of this world—that are looking at establishing bases in Australia or the region. In terms of turnover, we are talking about very large companies that would have a large impact on our economy. I stress that there would be some clear detriments to the treatment that is proposed.

While we can talk about it on a theoretical basis, I also wanted to get some facts and figures associated with it, so I went to the company Bluegum, the IBM company in Wangaratta. While everyone talks about the removal of tariffs and duty rates on imports, Bluegum still pays about

\$14,000 a month in customs duties for components. A company producing a PC overseas brings that into Australia duty free. Because Bluegum acts as an agent for someone else, the paperwork involved, I suggest, is a detriment. Not only is it a detriment going into the Australian market but, because of the paperwork and corporate structures involved, Bluegum also has some difficulty in terms of the drawback regulations. So that \$14,000 is a direct impediment to a computer manufacturer sitting in Australia supplying the Australian market or the export market. That is something we certainly do not want to see.

They are the essential elements of where we are coming from. In the IT sector, the component manufacturers have supported the removal of tariffs so there can be a broader manufacturing base they can supply into. As such, we would like to see a scheme that allowed for that beneficial treatment.

Another area of importance is that of licensing fees. As Senator Murphy rightly said, there is an inequity with the whole cost recovery structure and licence fee type structure. It certainly hits our smaller companies. Even with the cost recovery regime, if you have to bring in 100 different entries because you cannot afford a large stockpile, you are up for 100 times the cost recovery. On the other hand, a large manufacturer can bring it in in one hit. I think there are some inequities in the whole cost recovery regime, but I suppose we should not get into that in too much detail here.

We certainly support BHP. Alan Norton commented on the idea of MiB as an export zone for local manufacturers. If they have paid duties and there is a duty component built into their costs, and if they can then supply what they have produced into an MiB production process, the opportunity to get a drawback of duties then and there rather than waiting for the goods to be manufactured and exported is a good idea and would enhance the attractiveness of the scheme.

My only other comment is that we are working with state and federal government in working out ways of promoting this scheme overseas and attracting these big companies. I think that will work. Since the announcement, DHL has seen a renewed interest in MiB. We are holding workshops in each of the states at the moment. We will soon be holding some seminars in at least the major states in conjunction with the state governments. I think it is now an attractive package. Equally, we do not want to see that attractiveness lost in certain sectors like the IT sector. We would like to work with the government as some of the benefits being shown in MiB transfer into the Texco scheme that is before parliament now.

I notice that you have asked for supplementary submissions. In an hour I had spare in the airport lounge, I drew up a very short supplementary submission, if you would like it tabled today. Like BHP, we support a more flexible scheme where someone like the Department of Industry, Science and Resources could say that the tariff treatment should be such and such for the IT sector and such and such for the automotive sector et cetera. The example is Bluegum.

CHAIR—Please give us that submission. We would be pleased to receive it. I assume the committee agrees to the publication of it. There being no objections, it is so ordered.

Mr Muldoon—There is nothing in it that I have not really covered or that has not been covered by BHP. It essentially backs the removal of cost recovery. It identifies problems with the Bluegum-type example. It identifies another folly: if Bluegum manufactured in an MiB site and brought it into Australia, they would pay a duty. If they manufactured in an MiB site in Australia, shipped it over to New Zealand and then reimported it into Australia, it would enter duty free. I recognise that there will be anomalies with this whichever way you go and,

as was rightly said, some winners and losers. That is why we would like a flexible scheme that does not apply one or the other.

CHAIR—You are now basically supporting the flexible scheme that BHP outlined. Is that correct?

Mr Muldoon—With the companies we are dealing with and the success we have seen in free or foreign trade zones in Asia, we support primarily and predominantly the concept of an area outside the customs border. We do not particularly like the idea of a scheme that sort of straddles that idea. But, equally, we can see benefits in the other.

CHAIR—That is plain from your submission, yes.

Mr Muldoon—We would not like to see it come down to one or the other. We obviously prefer the finished products. But if there were some imperatives for certain industries in Australia in that that would cause dramatic problems, rather than it going to just the components, we would much prefer some flexibility, particularly in the IT industry. We believe that industry is quite critical to the future of Australia's development.

CHAIR—BHP has given us some numbers regarding the potential turnover from their project. To give us a bit of perspective on the economic potential of some of the possibilities that have been floated past your company, can you give us some numbers? We will take them on board as possibilities only.

Mr Muldoon—When this whole scheme was being mooted, the Department of Industry, Science and Resources said, 'How much will this generate in Australia?' We said that it depends on how attractive the scheme is made. Certainly the companies we are talking to on a regular basis are the multinationals—the Eriksens, Nokias, IBMs and Intels. With this scheme or any scheme that overtakes it, you are looking at billions of dollars of turnover on an annual basis, potentially.

CHAIR—If the current problem you highlight in here is addressed one way or the other, are you confident that there will be investment in MiB schemes by such companies in Australia in the next few years?

Mr Muldoon—Yes. At the moment we suffer from the fact that MiB was announced 18 months ago, and the cost recovery issue was one detraction from it. I do not think it will ever be a quick turnaround for a manufacturing sector to change the way it operates. I do not think it will happen quickly. People say, 'Well, if MiB was such a good idea, why aren't we seeing so many?' The removal of cost recovery is one reason why we will see an interest generated.

We had a meeting in Melbourne just late last week where we invited two companies, Eriksen and Bluegum, to discuss it. We restricted it to that number because we wanted to get an industry perspective of how attractive it was. I suppose in some ways I even questioned whether we were sitting in a theoretical world. I wanted to get some real industry perspective on it. We restricted the number of companies because they would not have opened up to us if their opposition was there.

Along with Eriksen and Bluegum, we have about six companies on a list to whom we will be talking in Sydney within the coming weeks and there are about six to 10 companies in Brisbane to whom we will be talking thereafter. All those companies have indicated a support for the scheme. I can certainly give you a letter of support from at least one company that has said it is now looking at moving its manufacturing base to Australia solely on the basis of the MiB scheme.

CHAIR—It would be useful to the committee if you could.

Mr Muldoon—It is an IT based company. Until I clear their support, I will not mention their name.

CHAIR—I understand. I have mentioned the announcement by the industry minister of the Productivity Commission inquiry into the input tariffs. Would you care to comment on that process as it relates to this problem.

Mr Muldoon—In our tariff structure at the moment, there are areas where inputs have a duty rate yet finished products are duty free, and the reverse occurs. Until there are no duty rates or a set duty rate, that will always be the case. In an MiB scheme the discussion we have had will continue. Look at our fundamental tariff structure. While ever there are variations, there will be a problem with it. It may not be an insurmountable problem, but there will be a debate about how it should occur. Where that will go I am not really sure. As BHP has said, what is important in this debate is that there be some flexibility to ensure the best outcome for individual sectors. Legislating in the Customs Act for a specific treatment cuts down any chance to address that flexibility.

Senator MURPHY—You have an example relating to cost recovery on page 3 of your submission. Will you just explain a couple of things to me so that, when the department comes before us, I can at least try to ask a question of them on the basis that I might know something. With the example you give, you state:

Thus if a computer manufacturer processed 50 entries for imported components to produce 100 computers in an MiB facility, that manufacturer may incur charges in order of—

and they are set out there in the dot points. You then state:

In contrast, an overseas manufacturer bringing in a single shipment of 50 computers would only incur charges in the order of \$26.45.

In the case of the 50 entries for components, you say that the charge would be \$1,140. That is \$22.80 times 50. Why wouldn't the person bringing in the components bring them in as a single entry?

Mr Muldoon—It would depend on whether they are sourced from the same country, the same supplier. I agree. It is a theoretical example. But if I were a computer manufacturer, I could be getting my boxes from one company in the US, my motherboards from another company and my cabling from another company in another country. You could just go further and further. If you have different suppliers in different destinations, it comes in in a totally different number.

Senator MURPHY—I thought that may have been the case, but I wished to clarify it. It does not matter for the overseas manufacturer in this case.

Mr Muldoon—Contrast that with the same manufacturer setting up in a free trade zone in Malaysia. They would get the parts with no charges and make up a computer. You would then just have a single entry of those computers.

Senator MURPHY—Yes, no matter what they were. I was thinking about it being 50 or 60 screens, mouses or whatever.

Mr Muldoon—If they could get them from the same supplier, yes, that number would reduce dramatically; there is no question about that. I have put that there as an extreme example. The other charges would apply and, with the current way Customs is implementing this cost recovery removal, when goods do enter the Australian market there is a slight surcharge of \$5 above a standard entry. We thought we would not argue on that one.

Senator CHAPMAN—Mr Chairman, I think all the issues have been explored and clarified quite well by Mr Muldoon.

CHAIR—Thank you very much for your submission, your supplementary submission and for answering the questions of the committee.

[2.06 p.m.]

MORRIS, Mr Allan Agapitos, Member for Newcastle, House of Representatives, Parliament of Australia

CHAIR—Welcome. Do you have an opening statement?

Mr Morris—Firstly, I express my appreciation to the committee for examining this matter and, secondly, for agreeing to allow me to talk to you. I want to touch on two strands in this issue; most of it is in my submission. The first of the two strands is the idea of virtual bond stores, that we are still bound with a barrier mentality approach which dates back centuries.

Over the years we have simply computerised what was effectively a barrier system to collect the revenue on behalf of the Crown; that is what this system was. Modern manufacturing has moved on enormously from there. We now find that company stock is sitting in aeroplanes and on ships all over the world arriving just in time. There is minimal stock holding, highly programmed scheduling systems, highly sophisticated assembly methodology and the locations they use need a number of criteria. But what they need essentially are the processing systems available. Our systems are out of date. They are no longer relevant to what companies are using. Add that to the cost of recovery—

CHAIR—I am sorry, which systems are you talking about?

Mr Morris—Customs lodgment systems. We have moved on to electronic lodgment, which is simply a computerised lodgment of a paper form; it is simply an update of the old manifest from sailing ship days. Companies now have sophisticated stock control systems. They are managing their stock all over the world and, in many cases, in dozens of locations, and they are managing their input stock and their finished products. Our customs system requires them to pass a barrier and, when they pass it, they have to lodge other things to suit Customs. The cost and complexity of that to most companies, to my mind, is really daunting.

The foreign trade zone concept is now the MiB concept. When we look at it, what comes forward is the idea that we look at the barrier again and rethink it. The idea is that the barrier becomes a stock control system, not the physical barrier of either a port or the cargo bay of an aircraft. That is a big jump forward. The integration of those users with Customs needs to be compatible with their needs, not with revenue raising needs. Quite frankly, that has come forward in recent times, with the cost recovery process and the reporting processes of the Bureau of Statistics all being designed for our systems and being a real impediment to the users.

The idea of a virtual bond store and actually looking at stock control systems and seeing our computer control systems as our boundaries and not the actual barriers is a major conceptual shift that we need to make. We are making it now gradually. I think it will be evolutionary. It will not be a big bang; it will happen step by step. This hearing today is simply part of that process. I do not see it all changing tomorrow; what I see happening is that over time we will start to recognise it.

The second part is this question of consumables and duty on components or whatever. My view is that, in 10 years, our customs system should be transformed. If it is not, we will not be in manufacturing. The transformations will be in terms of the things we are talking about now. But we will also have picked up the things consumed in the manufacturing process—solder, lubricants, a range of other components—as not being dutiable because they will be seen as an input to manufacturing. Products coming out of those zones will be treated as though they are coming from offshore. Between now and then, there may be some changes

needed, and none of us can work them out. My view is that we need to build the process to allow that to evolve. I think both BHP and DHL were saying today that taking either side of that coin and locking it up tight will be unwise. I agree with that very much.

There may be a number of ways of building up filters. One may be the pre-licensing filter. The alternative may be an appeals process at the end; that is, if duty being levied on the finished product is damaging Australian industries, there would be an appeals process to allow that industry or company to seek redress or definition, because we do not wish to hurt our existing manufacturers. But put that with the virtual bond store and it means that the idea of existing companies and factories in more than one location needs to be part of it. We cannot create new factories simply to confirm with Customs' processing systems; we need to be able to integrate them in. That is why for stock control the virtual bond store is a logical development.

I was in Ireland earlier this year and spent some time at Shannon. I spent a fair bit of time with the Irish customs people, who were quite fascinating. Effectively, they have got within their computer systems a model for every product made in the Shannon foreign trade zone. If they want to, they can almost replicate how much of an ingredient goes into making any finished product, how much of it is wasted or whether it is an end product. The ease with which they can process and with which the clients can use those systems is really noticeable. When I spoke with the customs officials there about the virtual bond store concept, they thought that would be an enormous improvement on what they have because they are locked up with a physical boundary problem which becomes very artificial.

The real point that came across to me was that Dell Computers have just established in Ireland right now their design capacity. They started off with a manufacturing capacity. That has built up and up. In fact, DHL handle their transport all over the world, both in and out. They are now putting their design capacity in Ireland. They have 20,000 jobs attached to that foreign trade zone, and almost half the stock or material comes from ship and land. So, even though there is the Shannon airport, almost half of it comes by sea and land—to England by ship and then by trucks, in the main, across to Ireland. The way that operates is a real eye-opener. It certainly reinforced the fact that, if we are to be relevant to future investors, we have to fit their systems, not have them fit us. We know that does not work.

I should point out that my background is in computers, so I approach this, perhaps, with a different view to others. I encourage the committee today to recognise that this is an opportunity we have had now for a couple of years. When MiBs came in in the 1980s, quite frankly we did not understand them and the systems were not in place for the manufacturers. There were transport systems through Just in Time; the quality systems, the design systems, were not compatible. They now all are. The next wave of world investment, particularly in the Asian region, will go to the country not necessarily offering the cheapest prices or cheapest labour. Ireland is a high wage country. Ireland is very expensive. It has a two per cent duty. It does not have high tariffs. It does not have low wages. It is the very appropriate and well designed systems that make it much easier for the importers.

If we want to see ourselves attract investment in the future, we need to get close to those systems. It will take us a number of years to get the full benefit. But the first step is to be compatible now. I think a number of your colleagues in the lower House are also now more understanding of this. I suspect that the mood on both sides of politics now is that we need to make a shift. This one is too critical not to take very carefully and very thoroughly. This is obviously a pet topic of mine.

CHAIR—Thank you very much, Mr Morris. We have worked that out. We are pleased to hear from you today.

Senator MURPHY—The position you have explained in your paper is fairly clear. I do not have any questions other than those points that have been made with regard to the licensing arrangements. I read in the DHL paper that the licence fee is set at \$7,000 per year and \$4,000 per year thereafter. I want to ask the department a question about this. Do you want to make any comment about the licence fee? Do you have a view about whether there ought to be a licence fee and, if so, what the quantum of it ought to be?

Mr Morris—I have no objection to a licence fee. I think it will adjust over time. At the start, we are looking at MiBs as fairly large organisations who can guarantee the payment of duties, because we do not want them to go insolvent. The licensing fee will act as a deterrent and attract only serious investors in the initial systems. I think over time we will see many more smaller MiBs where single companies with multiple sites will be able to do that. The licence fee then may become an impediment to sensible investment. I think it will take us time to work that out.

What we are doing now is trying to develop a potentiality rather than a final result. Fees can be adjusted by governments and political pressure and feedback as we go along. But I do not see them as a major impediment in the short term. In the short term, we must not look as though we are too complicated or as though there is too much red tape. Imagine putting in 100 different requirements for duty on components in a complex material where part components are used—where part of a coil of wire is used. Imagine the horror in a manufacturer's mind at having to comply with all that to get into a scheme. He would say, 'It's easier to go to Malaysia', not because it is cheaper but simply because it is easier. We are seen as a very bureaucratic, red-tape bound country as a result of our tariff system. It is a system that is no longer relevant because tariff revenues now are so small in comparison.

CHAIR—I come from the manufacturing industry, so I understand what are you saying.

Senator CHAPMAN—You are supportive of the legislation with perhaps the adjustments that have been proposed this morning by BHP and DHL to provide that flexibility?

Mr Morris—Yes, with that flexibility. It is about not putting into legislation that the duty is on the component, and perhaps leaving it open to regulations and re-interpretation.

Another factor which needs to be thought about perhaps more clearly is that of the consumables. That may not require legislation; you may be able to do that through the regulations. We must show that we have the potential to understand that issue. I guess we need to show that we understand what the issues are likely to be and to leave room for those to be massaged and developed as we go along. Putting things into black and white legislation now would be, I think, a fairly serious impediment. I do not think we know the precise form we will end up with in five years. I encourage senators to give us the potential to evolve that.

Senator CHAPMAN—With that longer term potential, your proposal, as I understand it, is that the current concept of a physical barrier be replaced by a stock control system?

Mr Morris—Yes.

Senator CHAPMAN—It concerns what you have seen in Ireland and so on. Have you discussed that with our senior Customs people? If so, what sort of reaction have you had?

Mr Morris—I have talked about it to industry department people. I normally talk to them more so than to Customs people. I do not deal with Customs very often. In the sense that I have had a long-term interest in industry policy from way back, I see Customs, I suppose, as

an application of another policy rather than a thing in itself. But, certainly, I have canvassed it with Mr Webb. I have canvassed it with so many people. Certainly I have canvassed it with the Irish customs people, and they were very responsive to it. They were saying that they are caught up with the same problem. They have this existing system which is historical in nature. They have made huge changes to it compared with what it was around 30 years ago.

They are now at another kind of block point. They agree that the next step forward is to bust out of the physical zones. Just how they will do so is hard because they already have a big investment in those physical zones, which we do not have. We can start off with a bit more freedom. I do not think the current legislation prohibits it. I do not think the current legislation would be against it. Rather it would be in the licensing processes. Mind you, I am not a customs lawyer or a technician. I encourage you in your considerations to leave open those options or to leave them fluid so that we can constantly monitor and get feedback from industry to learn from it.

I should point out that this original support came from a committee looking at the steel industry chaired by David Hawker, as you may recall. That report was quite critical. David and his committee's involvement in that inquiry was quite useful in all of us getting our heads around this stuff. There was a fair bit of bipartisanship about it at the time. In fact, I still deal with David quite a bit on this sort of matter. So I hope this is an issue on which we are not sharply divided politically.

CHAIR—Thank you, Mr Morris, for your submission and your comments.

[2.20 p.m.]

JEFFERY, Mr John Harland, National Director, Commercial Division, Australian Customs Service

McCULLOCH, Mr Alan Barton, Assistant Manager, Customs Policy Section, Department of Industry, Science and Resources

WEBB, Mr Robert John, Manager, Customs Policy Section, Department of Industry, Science and Resources

CHAIR—I remind committee members that, under the parliamentary privilege resolutions agreed to by the Senate, officers of a department of the Commonwealth or of a state shall not be asked to give opinions on matters of policy. Officers should also be given a reasonable opportunity to refer questions asked of them to superior officers or to a minister. I welcome the witnesses. Do you wish to make an opening statement?

Mr Webb—Yes, thank you. I will talk generally about manufacturing in bond and where it came from. In particular, I will discuss another program which potentially will work together with manufacturing in bond. That might help to throw another perspective on some of the many issues that have been raised this afternoon.

The government announced that manufacturing in bond would be reintroduced in Australia in late 1997. It did that as part of its 'Investing for Growth' industry statement. That followed an inquiry into existing tariff export concession schemes. Those schemes are called Texco and duty drawback. I will not go into those schemes. Duty drawback has been mentioned this afternoon. During that inquiry, which was conducted under the legislation review schedule, under the competition principles policy agreement, both the Customs Service and us were coming to various conclusions as to how things could be improved.

The government accepted some of the ideas coming out of that review. At the same time, there was some community interest shown in examining whether foreign trade zones, particularly as they operated within the United States, would be applicable to Australia's situation. The government concluded that manufacturing in bond, while not the same as an American foreign trade zone, would offer all the advantages of the American foreign trade zone. At the same time as announcing manufacturing in bond, it announced that Texco—that is, the tariff export concession scheme—and the duty drawback scheme would be revamped into a new scheme to be called Tradex. There is quite a relationship between manufacturing in bond and Tradex.

The pressures for the foreign trade zone concept were fairly strong. Australia previously had manufacturing in bond, which was only withdrawn through changes to regulation. It was possible to introduce manufacturing in bond fairly quickly because we only had to revive the legislation. Manufacturing in bond existed in the late 1980s but in a very different form from that which is now available. It enabled the government to get manufacturing in bond up fairly quickly, to put it briefly, and that happened in March last year.

One of the acts in reviving manufacturing in bond was not to revive it precisely as it was in the past. It was confined in very specific sectors. It was not a generally available scheme. Indeed, it had a provision in it in those old days where you could choose which duty you would pay if you brought a good into the domestic market through your manufacturing in bond facility. But that was not the intent of the government in its 1997 announcement about the re-introduction of manufacturing in bond.

It is pertinent to look at some of the concepts that have come up this afternoon in the context of the tariff review, and that has been raised. It is also pertinent to look at it in the context of Australia's APEC commitment to move to free trade by the year 2010 as a developed country. I do not think there is any agreement that that means we are moving to a zero tariff, but that is positively the direction in which Australia is going. Obviously the Productivity Commission will be asked to look at the general tariff in the context of those APEC commitments.

The reality is that through APEC processes, for example, and in the WTO Australia has entered into a number of multilateral and bilateral arrangements whereby the tariff is gradually coming down. In particular, it is occurring in the area of instruments such as the information technology agreement and what has happened in medical and scientific equipment as a result of domestic review. So there are various processes. The 'nuisance' is the latest expression of that.

The general trend is that the tariff is declining. In the case of the TCF and passenger motor vehicles, there will be another tariff reduction on 1 July next year and then there will be a freeze in those sectors. But for the general tariff rate the number of goods which do attract a tariff are declining. So far, at the moment, in very round figures, 60 per cent of all goods—John is the expert—enter Australia duty free. Of the remaining 40 per cent, half are textile, clothing and footwear and passenger motor vehicles.

So we are really dealing with 20 per cent of imports. Something like seven concession schemes operate on that 20 per cent, of which manufacturing in bond can be considered one. The concepts being raised by Mr Morris take Australia in fairly new directions. I have tried to paint a picture of where things are going in the future.

When we came to look at the tariff export concession schemes, I think it was clear to both Customs and our department and industry, in view of the submissions we received, that that scheme was a remnant from a time when the tariff was much higher; that is, when there was a great deal of revenue. We really needed to look at it with more modern management practices.

What the government has announced is Tradex. There is legislation currently before the parliament on it. That scheme will take us a long way down the path of the virtual free trade zone. The scheme provides manufacturers and exporters with the capacity to move to an up-front duty exemption on their exports. The beauty of that is that you will need to be registered to use Tradex and to use that facility. There is no up-front fee as there is in manufacturing in bond. The previous schemes were not legislated schemes. They were schemes which were administrative in their sense. It was necessary to introduce Tradex backed up by some significant legislation. For that reason, it could not be brought up as quickly as manufacturing in bond. But there is a full recognition in our department and by the government that Tradex may make manufacturing in bond redundant. In fact, my hope is that we will not need it because Tradex will be generally available and confer most of the advantages.

In particular, Tradex will be quite different from what existed previously. It is a more light-handed approach to administration as a greater range of goods are included. It embraces some policies that are now Customs policy. There are issues such as periodic settlement, self-assessment and those sorts of things. We think it is a user-friendly scheme. It will have a cost flow advantage, because many people who currently export pay duty on imported components and then claim them back afterwards, and there is a duty drawback scheme for that. Because

of its very nature, it is a high compliance cost scheme. Our hope is that people will move out of duty drawback and into Tradex and derive those advantages. I will perhaps stop there.

Mr Jeffery—Mr Chairman, I think it is probably more productive for me to clarify issues as I answer questions.

Mr McCulloch—I have nothing to add at the moment, thank you.

Senator MURPHY—Am I correct in saying that the licensing costs are the same for every company?

Mr Webb—That is correct.

Senator MURPHY—Regardless of size?

Mr Webb—That is correct.

Senator MURPHY—How does that encourage small manufacturing companies versus larger manufacturing companies?

Mr Jeffery—The licensing costs and the user recovery charges are based on the cost to the Customs Service in providing the service. They are not individually tempered towards each company. The licensing costs have been there for many years, and we are ramping up with CPI. When MiB was brought in, we reviewed those costs and reduced the up-front costs from just under \$10,000 to \$7,000, and the annual cost from \$7,000 down to \$4,000. They are reviewed on a six-monthly basis to ensure that they and the user recovery charges are an accurate reflection of administering the schemes. They are applied under legislation for that reason. But they are not tailored to each individual circumstance; to do that administratively would probably be extremely expensive.

Senator MURPHY—I am not quite sure that I accept that argument.

Mr Jeffery—If we had to strike a cost with every person we did business with to reflect the rate of that business, the intrusion of the cost of that administratively—

Senator MURPHY—If you had a company doing \$0.5 billion or \$1 billion in business, I would have thought it would mean a greater administrative cost from your point of view than one that was only doing \$5 million.

Mr Jeffery—Not necessarily. Mr Morris mentioned doing business with Customs. Some people are aware that there is a major cargo re-engineering project under way in Customs to address the way we do business and the way industry does business with us. This is to go down the direction of us not imposing our requirements on business but being able to link in to their systems and services. If a very big company gives us direct access to their systems and we can do arrangements that way, it may be cheaper for us and that company than for a physical audit to be done where we have to provide individuals and go through a non-computerised system. That is a very simple example, but there are other examples such as that.

Senator MURPHY—In the paper there is the cost of licence fees. There is the minimum security normally taken for a single warehouse licence being \$20,000; and, if two licences are involved, it is \$40,000, a national security.

Mr Jeffery—A security is a security based on the risk assessment of the organisation and the type of revenue exposure they may have. Security can be documentary security, a bank guarantee or actual money. Very rarely is it actual money. It is usually documentary security.

Senator MURPHY—The paper says it must be guaranteed by a cash deposit lodged with the ACS or a bank.

Mr Jeffery—That is not the practice, I would have to say. We take securities in the form of bank guarantees and documentary securities, which would be a hold over something, and in the form of cash if cash is put up. It is very rare for people to put up cash. The cost of that to a small enterprise is extraordinary.

Senator MURPHY—Yes. That is why I was curious about it.

Mr Jeffery—If it says that, I think it is incorrect. I will check it and get an answer back.

Senator MURPHY—I am just getting it out of the paper. It says that security must be guaranteed by a cash deposit lodged with the ACS or by a bank or other acceptable financial institution acting as guarantor.

Mr Jeffery—Yes. That is usually documentary or a bank.

Senator MURPHY—I would have thought it might be a bit of a hurdle for some small businesses.

Mr Jeffery—My understanding is that these days we very rarely take cash as a security. The only time we take cash is for very high risks, and we no longer have responsibility for excise which is where the highest risk is.

Senator MURPHY—It would be helpful if we could clarify that for the purposes of this committee's consideration.

Mr Jeffery—We will do that.

Senator MURPHY—You have addressed in part the question of reporting mechanisms. If I understand what you have said, the ACS is essentially looking at this on an ongoing basis. If you have access to computerised systems, from the point of view of the manufacturer concerned it could reduce costs. I suspect that that will become the norm as time goes by.

Mr Jeffery—It is certainly our objective.

Senator MURPHY—Could that potentially reduce the cost of licences, if that were the case?

Mr Jeffery—We are looking at the cost of all our user charges in that sense. Part of our approach with industry involves things like periodic entry, deferred duty payment and partnership arrangements with industry. You would strike a cost regime with a major organisation working with us if they met all the criteria. That is in recognition of where industry is going with its systems and its way of doing business and where we stand at the moment with our business systems, which need to be re-engineered. That is a project that we are moving on over a period of three to five years. We are very actively consulting with industry at the moment.

Senator MURPHY—So the licence fees are essentially figures that you have arrived at on the basis of what you think it costs you to do an audit. Are those audits done annually?

Mr Jeffery—No. They are based on what it costs us to deliver that service, not necessarily to an individual but across the whole range of the warehousing service we provide to industry. We have within the organisation a very detailed split-up of the costs of delivering services. The user charging regime only applies to some of those services and they are costed out. The licences and the user charges are then based on those costs and they are reviewed on a six-monthly basis.

Senator MURPHY—Is there some sort of breakdown of that?

Mr Jeffery—I think you have seen that booklet that sets the user charges. They are part of the legislation at the moment. I can provide that to you. I think it is in that document as well.

Senator MURPHY—I see. So this goes on the cost recovery charges?

Mr Jeffery—Yes. The licence charges are reviewed in the same context.

Senator MURPHY—I might have misunderstood that. There are cost recovery charges listed here for items imported via sea, and they are lodged electronically. There is a fee for that. The licence fee is the compilation of these things, is it?

Mr Jeffery—No, the licence fee is a separate fee to licence a warehouse.

Senator MURPHY—What do they get for that? Just the licence?

Mr Jeffery—They get the entitlement to run a warehouse and the agreements about the way it is set up and established and the cost of us doing that.

Senator MURPHY—That is my question, I suppose. You have a cost recovery mechanism here in terms of charges. But on top of that you have a \$7,000 charge for issuing a bit of paper.

Mr Jeffery—I think it is a bit more than issuing a bit of paper.

Senator MURPHY—Can you explain to me what it is, then?

Mr Jeffery—It is reviewing the entitlement to a licence and establishing that the business is a business that meets the criteria. It is the audit functions that are carried out across the licensing arrangements. It is arranging for that warehouse to interact with Customs and its systems to check that. It is the facilities we provide to assist with that. I can get you a better break-down than that, if you wish.

Senator MURPHY—What is the licence fee under the cost recovery charges listed in here?

Mr Jeffery—There are no licence fees under that. These cost recovery charges relate to the nature of an entry. So these are for goods that are being entered. The issue that brought this inquiry here is that we would have charged an entry fee of \$22.80 for goods to be imported into an MiB when they would subsequently have been re-exported. The legislation provides that that will not apply for a good that is brought in and exported. It applies to every entry.

Senator MURPHY—I just want to understand the breakdown of the costs—that is, the \$7,000 initial fee, the \$4,000 annual renewal, and what are listed here as the cost recovery charges. There is a list of a number of things. One says licence fee for Customs depot, (a) \$1,000.

Mr Jeffery—That does not apply in these circumstances; that is an entirely different issue.

Senator MURPHY—It is just that it says ‘which could impact on MiB operations’.

Mr Jeffery—I do not believe MiB operations are involved in a licensed Customs depot. I would have to ask someone who runs one or who looks at running one. That is a Customs depot licensed for consolidating and deconsolidating cargo. Can I split the two issues for a moment?

Senator MURPHY—Yes, certainly.

Mr Jeffery—The licence fee that we are talking about is to establish and continue a warehouse licence. After that is done, and that will be the \$7,000 initially, the \$4,000 per annum renewal—

Senator MURPHY—I think that is what I asked you in the first place. I asked whether it was for the purposes of auditing.

Mr Jeffery—Yes. I can give you a greater split-up. Once that is done, and once someone operating a warehouse is doing business, there are the user charge fees that apply to entries whether or not they come into the bond or come direct or come by sea or document or electronically. That is what this split-up is.

Senator MURPHY—Yes, I can see that. It was just this other one that is in there.

Mr Jeffery—Yes. I missed that myself. A 17B warehouse is a specific warehouse for cargo. I am sorry I cannot go much further than that. Unless one of the people involved in MiBs can tell you a bit more, I do not think MiBs are usually involved in it.

Senator MURPHY—It sort of breaks it down. It says paid by (a) existing 17B operators, which is the point you make, whoever they are, and (b) new applicants, but it does not clarify who the new applicants are. Are they new applicants for MiB?

Mr Jeffery—New applicants for a 17B.

Senator MURPHY—Depots with less than 100 transactions per annum?

Mr Jeffery—That would be a 17B with less than 100 transactions per annum.

Senator MURPHY—What are all other depots?

Mr Jeffery—The annual fee for less than 100 transactions is obviously less than those for depots that have more than 100 transactions.

Senator MURPHY—Yes. What about all other depots? Is that the \$4,000 annual fee?

Mr Jeffery—It is the same as a renewal fee for an MiB, but it is not the MiB renewal fee.

Senator MURPHY—It is still 17B?

Mr Jeffery—Yes.

Senator MURPHY—What was suggested by DHL and all our witnesses was that a case-by-case assessment be made for MiB applications versus the charging mechanisms that might be available. That is, rather than having just rules, there might be flexibility in applying the rules depending on the nature of the business.

Mr Jeffery—My understanding of that comment was that it related to the way components would be treated for tariff purposes, not to user charges.

Senator MURPHY—Yes, that is right. My apologies. I just had it written down here next to the licence fee.

Mr Jeffery—As Mr Webb said, the policy we are operating MiB under now is somewhat different from what was in force in 1988 or thereabouts. At that time there was a regulation that allowed an operator to choose either. It was applied to a very restricted range of goods. If my memory serves me correctly, about 42 specified items could come into local manufacture and about 49 could go for export.

The policy direction that we are operating under for this scheme is export oriented. In that sense, the provisions in the act ensure that the treatment of a local producer of the product is no different from the treatment of an MiB manufactured good which enters home consumption; that is, it will be essentially competitive neutral. If for argument's sake there is a local manufacturer of computers who imports components, they pay duty on those imported components. If an MiB import manufactures components and imports the final product, the components are dutiable at the same rate.

There is a range of concessional schemes available where product is not made in Australia. Mr Webb mentioned the international technology agreement, which was brought in at the same time as MiB. There is also the tariff concession scheme and there will be Tradex. So, where there may be no local manufacturer of those goods, the facility is already available for the component out of a MiB to obtain duty free treatment and be in exactly the same situation as a local manufacturer.

Senator MURPHY—What about the example? I assume you have seen the DHL submission.

Mr Jeffery—Yes, I have.

Senator MURPHY—Can you respond to it?

Mr Jeffery—Which one?

Senator MURPHY—The one on page 3 of their submission. It relates to a domestic manufacturer bringing in computer components.

Mr Jeffery—I am sorry, that has gone back to the user charging issue. I am talking about the tariff issue only here. I can address the user charging issue separately. They are distinct issues. The best example is probably the one BHP mentioned where, if I recollect correctly, wire is dutiable but barbed wire is not. In that circumstance you allow the duty free entry of the wire into a facility that manufactures barbed wire. The barbed wire comes in at the barbed wire rate free. If the local manufacturer imported, he would have to pay five per cent on his imported wire or he could source it from BHP. In that sense, the reason for putting components at the same rate is to say that the product coming out of an MiB and the product manufactured in Australia are competitively neutral; they receive the same treatment. They do not have the option.

We recognise with the inverse tariff issue that the completed product is imported to Australia at a free rate. That is an industry policy issue. As Mr Webb and the Chairman have already mentioned, the Productivity Commission will be looking at it. But that is the situation that obtains at the moment. All that the arrangements in the legislation seek to do is not change the position as it is at the moment.

Senator MURPHY—But you acknowledge that it is in a disadvantageous position in that respect.

Mr Jeffery—I am not acknowledging that at all. I do not have enough knowledge of Australian industry to say that. Some will be disadvantaged and some will be advantaged. I suppose the government chose to go down this route so that this does not provide an incentive which will affect local manufacturing. Do you want me to address the issue of user charges?

Senator MURPHY—Yes.

Mr Jeffery—As Mr Muldoon mentioned, it depends on the way an industry structures its business. A simple entry at the moment is charged \$22.80 plus 20c a line for every line after the tenth line on that entry. That entry can be structured in any way the importer chooses it. In the example Mr Muldoon has used, if the computer manufacturer brings in 50 computers, it is a one-line entry. For 50 computers, he pays \$22.80. If that comes through into a bond store and is manufactured in bond, you have 50 computers. If they choose to bring those 50 computers out once, they will have one entry for 50 computers plus the requisite number of lines to determine what the components are. There might be 50 components. So it would be \$22.80 plus 20c for every line in addition to the first 10.

So the cost would be, in that case, \$22.80 plus an amount that I am not sure of. If they choose to release those from bond one at a time, they would pay \$22.80 each time. So it would be 50 times \$22.80. The best example that I can give you is the automotive industry. It imports the bulk of its vehicles into bond. It then clears them from bond as it needs them. So it will make a single entry and then it will import five, six or 10 cars at a time and pay a fee on them.

Senator MURPHY—But that is not what I understood when I asked Mr Muldoon about that. I thought something not dissimilar to what you have just cited. I thought he said that if they buy their boxes, frames and whatever else, which might be a number of entries in respect of the charges, they are costs they have to pay. On the other hand, the imported product would come in. The overseas manufacturer would bring in a single shipment of completed product.

Mr Jeffery—That is quite correct. But if the local manufacturer in Australia is manufacturing the goods and has to import those same boxes, bolts and screws and bits and pieces, they will face exactly the same issue as the MiB. If they have to get their boxes, circuitboards and bolts and screws from different sources, their entry will cover each of them individually. But if they aggregate them and bring them in from one supplier in one shipment, it is a single.

Senator MURPHY—What if they get them from different ones?

Mr Jeffery—If they import bulk screws and circuitboards from different suppliers, they will pay an entry for each of them. In that circumstance, it will be two lots of \$22.80, presuming that the product is coming in as homogeneous.

Senator MURPHY—It goes into the one end product.

Mr Jeffery—Yes.

Senator MURPHY—Why could it not be a single entry if it goes into the one end product?

Mr Jeffery—There are multiple reasons for that. Probably the main one is that, when the goods are imported many times, people do not know what they are going into and they may not be imported by the end user.

Senator MURPHY—I can understand that.

Mr Jeffery—And they are imported in separate shipments; they do not all come in at the same time.

Senator MURPHY—It seems to create an inequity for manufacturers who search the globe for suppliers and different components. They buy them in to manufacture one good from a competitive point of view. Then that good comes in after being manufactured externally.

Mr Jeffery—What we are addressing now does not change the inequity that currently exists.

Senator MURPHY—I understand that. That is not what I thought the government's policy of promoting industry growth was about.

Mr Jeffery—The change in MiB ensures that if the goods are imported from wherever in whatever quantities and are then re-exported there will be no charge. It is only when they come into the domestic market that the charge is applied. So if all those goods from a variety of sources come into an MiB or are all manufactured into a product and are all exported, there are no user charges and no input entry charges. That is what this legislation is designed to do. When that proportion of the goods that are not exported comes on to the domestic market, they will be treated exactly the same as if they were imported by a local manufacturer to do the same thing.

Senator MURPHY—An importer brings the stuff in and does not pay the charges or pays a single charge for the 50 computers. However, if you bring the stuff in and manufacture it here and want to sell it here, you are subject to a host of charges, or potentially you are.

Mr Jeffery—I will explain it this way. Leave MiB out for a moment. An importer of computers brings in a batch of 50 computers as a single entry. A local manufacturer brings in all the components to make 50 computers. If he brings them all in in one shipment—basically a CKD operation—it would cost him more than \$22.80 because there would be as many components as line entry rates. It would be \$22.80 plus 20c for any excess lines. In that circumstance, the importer of the single made-up unit is already at an advantage to the local manufacturer. In a MiB sense, all we have done is transposed to the goods entering the domestic market the same circumstances as would face a local manufacturer importing the components. We are not giving a completed component coming into the local market any advantage over the same locally manufactured product in the market.

Senator MURPHY—Perhaps Mr Muldoon might like to respond to your submission to the committee in writing. It concerns the proposal for MiBs from a virtual reality point of view, where they will not be located in zones and they will be located anywhere.

Mr Jeffery—The issue there is really why they are based on barriers and collecting at a point. I think a comment was made that revenue is a lesser interest. That is probably not quite accurate. We currently collect about \$3.3 billion in Customs duty. With the GST coming on imported products, there will be a liability of about \$12 billion at importation. As I said earlier, we are addressing the way we manage cargo. It will involve deferred duty payment, periodic settlement and a different form of entry. I am not saying that this will happen quickly. It will happen over time.

I think the BHP representative commented that we were already in discussion with them, as we have been with DHL, about a single warehouse licence and at a site which would cover the operations there. So it would not be a single liability holder who would take responsibility. That does not go as far as Mr Morris's comments, but it is moving in that direction. I think you will see occurring over a long time—I am not sure whether it will be over the 10 years Mr Morris mentioned—a further movement away from that strict border issue. But that really comes down to two issues.

One issue is the revenue that the government requires and the point at which it is to be collected. That relates to entries and acquitting and the risks that are involved with moving goods further back behind the border. But we are certainly addressing that issue and we are talking to industry about it. In fact, there is another bill before the parliament at the moment which will allow for deferred duty payment. So it is movement; it is gradual. It may be more gradual than outlined in Mr Morris's comments, but it is moving in that direction. However, the virtual warehouse for stock holding is probably a little further away.

CHAIR—Mr Webb, in your opening statements you commented on the proposal put by BHP that there should be a flexible scheme for whether the tariff is on the components or the final product. I got the impression from what you said that the Tradex scheme, if it goes through the parliament as it currently is, will virtually do the same thing. Is that what you are saying?

Mr Webb—No. I am sorry if I gave that impression. Tradex is a tariff export concession scheme. Basically that is what we are talking about when we talk about foreign trade zones. What are people after? They are after a system whereby exports, goods that are imported and re-exported either in their current form or in a manufactured form, do not incur sales tax or

a customs duty liability. If you go through an MiB facility, if you bring those inputs in and do whatever you do or send them out in their existing form, you do not incur sales tax, customs duty or the customs cost recovery charge. I think the difference between MiB and Tradex in that sense is really the up-front licence fee. Tradex would be generally available.

Senator CHAPMAN—Mr Jeffery, you indicated that it could be some time before we were able to implement Mr Morris's concept of removing the physical barrier as a customs facility and going to the stock control system. When you say that, do you have a time frame? Can you indicate what sort of technology Customs currently has that would allow you to move to that system, or what needs to be done to get to that situation?

Mr Jeffery—I am not sure that we will ever get as far as Mr Morris has suggested, but we are moving in that direction. We are looking at interacting directly with the systems of the people we deal with. Instead of their necessarily having to do paper entries or electronic entries, they will provide us with a simple advice and we will acquit it at a period down the track. That time period will probably be a month. The goods will flow through on a very simple advice—I am talking here for commercial reasons, not for any other Customs reasons—and will be acquitted on that. In a month's time they will give us all the documents or download them through Internet, through a specific system they have or through a bureau service. It will be whatever they choose to do that can interact with our own systems.

That is the direction we are moving in. We are talking to industry about it at the moment. We have requests for tender out at the moment on the gateway that will be used to intersect with us. The period we are looking at for that project at the moment is three to five years in order for us to come to that.

Senator CHAPMAN—When that has come to fruition, how much difference will there be between that scheme and what Mr Morris proposes?

Mr Jeffery—I think it will be moving towards accounting on stock holding, but probably on stock holding within Australia rather than—if I understood him correctly—around the world. This movement is not related to MiB; it is in our total activity.

CHAIR—Thank you very much for appearing before the committee today. That completes our hearing this afternoon.

Committee adjourned at 3.00 p.m.