

# **Submission**

By

**Business|NZ**

to the

**New Zealand Customs Service**

on the

**Discussion Document for Key Stakeholders on  
Customs' Goods Clearance Activities: Review of  
Funding Arrangements**

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## DISCUSSION DOCUMENT FOR KEY STAKEHOLDERS ON CUSTOMS' GOODS CLEARANCE ACTIVITIES: REVIEW OF FUNDING ARRANGEMENTS

### SUBMISSION BY BUSINESS NEW ZEALAND<sup>1</sup>

#### 1.0 Introduction

1.1 Business New Zealand welcomes the opportunity to comment on the “*Customs’ Goods Clearance Activities: Review of Funding Arrangements*” (the Discussion Document). The Discussion Document provides a generally sound discussion of the issues which was considerably helped by input from various business groups in its development phase.

1.2 Business New Zealand notes that the Discussion Document (p.17) outlines three broad funding options as being potentially feasible (practicable) for funding goods clearance:

- full Crown funding from general taxation; or
- a mix of funding from those third parties who receive benefits from Customs’ border protection, trade security and trade support activities, and the Crown, or
- a mix of funding sourced from the users of goods clearance and the Crown.

1.3 Business New Zealand remains strongly of the view that Customs’ goods clearance activities are overwhelmingly in the nature of public goods and should therefore be funded out of general tax revenue. While Business New Zealand accepts that there may be some minor private benefits in goods clearance activities, these would be difficult to quantify in order to allocate such costs to the predominant beneficiaries.<sup>2</sup>

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<sup>1</sup> Background information on Business New Zealand is attached as Appendix 1.

<sup>2</sup> Business New Zealand, along with a number of other business groups, funded independent research by the New Zealand Institute of Economic Research (NZIER, February 2006) to determine whether goods clearance was predominantly of public benefit (which would support funding via general taxation) or private (which would support user pays funding). The NZIER report (attached) reinforces Business New Zealand’s position that goods clearance is overwhelmingly of public benefit: “*Given that the public benefits seem large relative to the private benefits, we would expect the Crown to meet most of the costs of goods clearance. It is the government that sets the standards and priorities for goods clearance according to the level of protection/security sought by, or on behalf of, society...*” (NZIER, *Customs Goods Clearance: Review of Funding Arrangements – Report to Consortium of Customs Clients* (February 2006)).

- 1.4 Currently the costs of goods clearance are shared between the Crown and users (importers, exporters, transport operators etc). The Crown will pay 31% (\$13 million) of Customs' goods clearance costs for 2005/06. Third parties, through a mix of user fees and other charges, will pay 69% (\$29.2 million). Under current government financial planning this will change to 20% and 80% respectively in 2006/07. The current share of funding, let alone projected funding, is totally unacceptable given the overwhelming public benefits associated with goods clearance as outlined below.
- 1.5 This submission is in two sections. Section 1 looks at issues surrounding the nature of goods clearance, and, in particular, public goods and benefits. Section 2 responds to the specific questions outlined in the Discussion Document.

### **Recommendations**

Business New Zealand **recommends** that:

**the full costs associated with customs goods clearance are funded via general taxation given the overwhelming public benefits associated with such activities.**

### **Without prejudice to the above recommendation:**

Business New Zealand **recommends** that:

**Virtually all of the costs associated with customs goods clearance should be funded via general taxation with a low level of contributions from the users of customs goods clearance services. At minimum, this would involve a complete reversal of the Government's proposed 2006/07 "20% Crown - 80% third party" funding approach to, for example, an "80% Crown – 20% third party" funding approach.**

## **Section 1: Discussion on nature of Goods Clearance**

2.0 Business New Zealand considers that in light of the NZIER report<sup>3</sup>, and indeed Customs' own Discussion Document, the Government should accept that customs goods clearance activities are of overwhelmingly public benefit and should therefore be funded out of general tax revenue.

2.1 In many respects, this fact is very strongly demonstrated in the Discussion Document (4.1 "Outcomes and Beneficiaries of Goods Clearance") which is worth quoting:

*"The outcome and output descriptions for goods clearance are set out in Customs' Statement of Intent.*

*The outcomes that goods clearance contributes to are:*

- **Revenue:** *All Crown revenue that is lawfully due is collected.*
- **Community protection:** *Risks associated with the movement of goods into and out of New Zealand are prevented from harming New Zealand's community, economy and environment.*
- **Border security:** *The domestic and international communities have confidence in New Zealand's border security and the security of New Zealand's trade and travel channel; and*
- **Trade support:** *Legitimate and compliant trade is fostered by efficient border regulation." (p.12)*

2.2 It is clear from all the desired outcomes and outputs of goods clearance, that these are overwhelmingly intended to protect the wider public interest of the New Zealand economy, its citizens and the environment, benefiting *all* New Zealanders, not just selective (private) groups or particular sectors of the economy but New Zealand Inc. The emphasis is therefore clearly on goods clearance being a public good.

### **Goods Clearance as a Public Good**

2.3 Business New Zealand strongly submits that goods clearance is a public good and that the Government's costs in providing a secure border should be met out of general taxation.

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<sup>3</sup>NZIER - *Customs Goods Clearance: Review of Funding Arrangements – Report to Consortium of Customs Clients (February 2006).*

- 2.4 The most widely accepted example of a public good is national defence where the Government seeks to protect its citizens from acts of war or terrorism. All will benefit from a reduced risk of an act of war or terrorism and none can be excluded from that benefit if they refuse to pay.
- 2.5 There is an incontrovertible argument that security initiatives aimed at incoming cargo and travellers are a public good and that expenses incurred by the Government in this respect should therefore be met out of general taxation.
- 2.6 Similarly, there is also a very plausible public good argument for security initiatives aimed at outgoing cargo and travellers. Improved security for the public (both in New Zealand and overseas) and an enhanced reputation for New Zealand ('clean, green, and secure') make these initiatives 'public goods'.

### ***Who Benefits?***

- 2.7 All New Zealanders benefit from international trade, for example through increased incomes, employment opportunities and tax revenues for the Government.
- 2.8 The Government recognises that New Zealand as a whole benefits from international trade and as a result dedicates significant resources to trade negotiations and export promotion. While individual businesses certainly receive benefits from these activities, the Government undertakes them to benefit the country as a whole. The same argument also holds for border and supply chain security.

### ***Business Community Already Meeting Costs***

- 2.9 The business community already faces significant compliance costs for transport operators (i.e., airlines and shipping companies) and facilities operators (i.e., ports and airports) in meeting the requirements of the various border agencies – including having to provide space to these agencies free of charge.

- 2.10 Moreover, there is no account taken of the costs incurred by those exporters that intend participating in the Secure Exports Partnership, such as upgrading their premises' physical security, training their staff, and upgrading their computer systems so that they can interface with those of Customs, to name but a few examples. Furthermore, significant costs are incurred by many businesses in meeting the regulatory costs imposed by other border agencies, such as the Ministry of Agriculture and Forestry, New Zealand Food Safety Authority, and the New Zealand Immigration Service.

## **Section 2: Key Questions for Consultation in the Discussion Document**

### **Question 1: Do you agree or disagree with the funding principles for this review and what are your reasons?**

- 3.1 The principles outlined on p.9 of the Discussion Document do not provide a satisfactory basis for determining user charges. They fail to define a benefit in terms of property rights, uncoerced willingness to pay, or consent to taxation. As a result, it is virtually impossible to use them to determine with any accuracy the precise nature of the “public” - “private” benefit split. Suffice to say that in the view of Business New Zealand, and implicit in the Discussion Document itself, the benefits are overwhelmingly public in nature.
- 3.2 Business New Zealand has particular concerns with the “principles” – that *“taxpayers or third parties should contribute to the costs of services where the outcomes provide a benefit to them”* or where it is *“practicable”* to levy *“third party beneficiaries or risk exacerbators”*. In our view the key test, and perhaps the only satisfactory test, of whether a service is being provided for someone's benefit is whether they freely agree to purchase that service at the given price or whether they freely agree to be levied to fund that service. Compulsory payments extracted without the consent of those on whom they are levied indicate that the benefits of those levies are being conferred on other parties. State actions that make payment mandatory point to the absence of a first party benefit commensurate with the cost.<sup>4</sup>

### **Question 2: Do you believe any principles should be emphasised over the others, and if so why?**

- 3.3 We concur with the Australian Productivity Commission's view that it is a “fundamental principle that cost recovery should be implemented for efficiency reasons, not merely to raise revenue”.<sup>5</sup>

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<sup>4</sup> For an in-depth discussion on this issue of cost recovery for imposed benefits see *“Assessment of Beneficiaries and Public Good Issues Relating to Cost Recovery for Supply Chain Security and Border Protection”* (Chapter 4, p.18-27) – A paper prepared for the Travel and Trade Industry Coalition by Bryce Wilkinson, Capital Economics Ltd, January 2004.

<sup>5</sup> Australian Productivity Commission, Cost Recovery by Government Agencies, Inquiry Report, August 2001, p XLII.

**Question 3: Are there any other relevant principles you believe are relevant to the funding of goods clearance, if so what are they and why are they relevant?**

3.4 We suggest the following additional principles:

- Benefits are indicated by uncoerced willingness to pay by individuals, or by the general uncoerced consent of members of a group to be levied;
- Individuals do not obtain a benefit from being allowed to continue to exercise their existing freedoms of action, contract and exchange and rights in property;
- A State requirement for mandatory purchase points to a public good rationale for State action;
- Public goods should be funded from general taxation unless they are local public goods – in which case they should be funded by levies on that local community, subject to its general consent;
- Individuals are not in general obliged to pay for goods or services delivered without their consent;
- Governments should not impose user charges for revenue reasons;
- The delivery of private goods and services should be competitive – citizens should not be forced to buy from a statutory monopoly.

3.5 Although it might not be considered a “principle” per se, it is important to acknowledge that by its nature, customs goods clearance is mandated by a state monopoly (i.e. non-contestable market) with limited (if any) ability of “users” to influence costs of service. The provisions of the Commerce Act should apply with particular stringency to cases of statutory monopoly.

**Question 4: What is your view on whether there are both public and private benefits from goods clearance?**

3.6 Overwhelmingly, as indicated earlier in this submission and implicit in the Discussion Document itself, the benefits of goods clearance are predominantly public in nature. This is emphasised in Customs’ Statement of Intent that the outcomes that goods clearance are to contribute to are essentially: Revenue Collection, Community Protection, Border Security, and Trade Support (see Discussion Document p.12). As the Discussion Document States (p.12) both Revenue and Community Protection can be “...characterised as being for the broad public benefit”.



- 3.7 The Discussion Document is more equivocal about border security stating, that it may be “...characterised as delivering both public and private benefits”
- 3.8 In respect to Trade Support, the Discussion Document (p.13) states that “The trade support outcome is difficult to characterise in either public or private benefits terms” but then goes on to recognise, quite correctly, the important effect customs’ processes can have, by fostering trade through efficient regulation and minimum impositions. All this is critical to the prospects of the New Zealand economy.
- 3.9 In a wider trade sense, the Government recognises that New Zealand as a whole benefits from international trade and as a result it dedicates significant resources to trade negotiations and export promotion. While individual businesses certainly receive benefits from these activities, the Government undertakes them to benefit the country as a whole. This would tend to support border security as having significant public benefits, and some, but much less, private benefit.

**Question 5: Do you have a view on the weighting or percentage split between public and private benefits arising from goods clearance?**

- 3.10 As indicated in response to question 1, and reiterated throughout this submission, Business New Zealand considers that the public benefits far outweigh any private benefits associated with goods clearance, and indeed the beneficiaries (both public and private) are dispersed. This makes it virtually impossible to determine any sort of weighing; suffice it to repeat Business New Zealand’s recommendation that given the overwhelming public benefits associated with goods clearance, funding should be via general taxation. The problem in trying to identify the private beneficiaries of goods clearance is that this will vary from person to person and also potentially will vary with the type of products being traded, and the markets for those products. This would make any sound allocation of the “private” benefits of goods clearance ad hoc and potentially economically and administratively inefficient.
- 3.11 Business New Zealand would support virtually all the costs associated with customs’ goods clearance being funded via general taxation with minimal contributions from users of customs goods clearance services. At minimum, this would involve a complete reversal of the Government’s proposed 2006/07 “20% Crown - 80% third party” funding approach towards, say, “80% Crown – 20% third party” funding.

**Question 6: Do you consider goods clearance to be predominantly public good or private good in nature, or a mix of the two, and how does this inform your views on how it should be funded?**

- 3.12 Business New Zealand considers that goods clearance is predominantly a public good.
- 3.13 Goods clearance meets the principles of a public good in that it is impossible to exclude people from its benefits (similar to the classic public good - national defence) and use by one person doesn't necessarily detract from use by another.
- 3.14 The outcomes and beneficiaries of customs goods clearance as outlined in Customs' Statement of Intent (Revenue, Community Protection, Border Security and Trade Support) largely reflect the public good aspects of goods clearance. All New Zealanders benefit from sound revenue streams, community protection etc and no New Zealander can be easily excluded from the flow-on benefits of an efficient goods clearance regime.

**Question 7: Do you have a view on who the primary beneficiaries of goods clearance are?**

- 3.15 As mentioned in question 6, the primary beneficiaries are all New Zealanders, who benefit through a sound system of goods clearance to facilitate trade in goods and services on which New Zealand is economically dependent for both employment and an improved standard of living over time. The primary beneficiaries are the same as the primary beneficiaries of any sound regulatory regime in respect to say banking or commercial law. The beneficiaries are ultimately the wider public.

**Question 8: Do you agree that the users of goods clearance partially drive the costs through their expectations of efficient quality service delivery? If so should they be prepared to contribute to the costs?**

- 3.16 To take an extreme and totally theoretical stance, it could be argued that if New Zealand did not trade then there would be no need for goods clearance regimes and hence no funding required. However, given that New Zealand is dependent on international trade for an improved standard of living for all New Zealanders, it would be logical to assume that as trade increases there could well be greater pressures on funding goods clearance.
- 3.17 The argument that the “users” of goods clearance partially drive the costs of goods clearance fails to acknowledge the primary purpose of goods clearance as outlined in Customs Statement of Intent (Revenue, Community Protection, Border Security and Trade Support). All relevant factors have strong to overwhelming elements of benefit to the broader public which go far beyond any concerns about potential “cost” increases associated with greater trade from “users”.

**Question 9: Are there particular characteristics of goods clearance that you believe should be weighted more heavily in consideration of the choice of funding option and if so, why?**

- 3.18 There are a number of issues which need to be considered here.
- 3.19 Given the unique nature of goods clearance where the precise split between public and private benefits is difficult to determine (and is likely to vary considerably from product to product and potentially different markets), any move towards even greater third party funding should be approached with caution.
- 3.20 A significant issue which cuts across all government services is what an appropriate charging regime is where there is no contestability in service provision. In normal competitive markets, individuals will make trade-offs between price and quality of service, along with a host of other factors. This issue is significantly different when legislation provides that in order to go about daily living (or in this case exporting/importing), it is necessary to meet specific standards set by Government and the only provider of those services happens to be a government department or its various agencies.
- 3.21 Where an agency seeks to recover some or all of the costs of service provision from the users or direct beneficiaries of that service, the public or individuals paying for the service need to be assured that the charges set are not excessive in relation to the costs incurred and take proper account of efficiency and equity considerations.

- 3.22 The danger with monopoly rights provided to government departments in respect to service provision appear to be threefold and are similar to the case of potential monopolies in the private sector.
- 3.23 First is the concern that price of service will exceed that which would occur had the provision of service been made contestable (i.e. the private business or in this case government department) potentially making monopoly profits.
- 3.24 The second is the potential for the government department to provide a sloppy service in the knowledge that there are no other competitors in the market.
- 3.25 The third (the corollary of the second), is the potential for government departments to provide a “gold plated” service in the knowledge that any increased costs can be simply passed on to private sector businesses and individuals. This was outlined in the Discussion Document (3.4.2.1, p.10).
- 3.26 The incentives on government departments (namely public sector employees) to provide a gold-plated service may well be driven by their desire to protect their own current employment prospects in a particular sector. This is similar to the incentives that may be evident for departmental employees in charge of large regulatory burdens. It may be in their own interests to ensure those regulatory burdens remain in force to protect their own employment prospects and current status.
- 3.27 It should be noted that the above is in no way intended to be critical of the current New Zealand public service or indeed to infer that such activity is widespread. What it *is* intended to do is show that there must be incentives on employees in government departments with large regulatory burdens (and the ability to pass on the costs associated with those regulatory burdens to the private sector) to ensure that those burdens remain reasonable.

**Question 10: Do you agree that the most feasible options are either full crown funding or a mix of Crown and third party funding?**

- 3.28 Business New Zealand believes the most feasible option is full crown funding given the overwhelming public benefits associated with goods clearance, with a mix of Crown and third party funding a distant second.

**Question 11: Do you have a preference for either of these options, and if so, why?**

- 3.29 Yes – see response to question 10.

**Question 12: If there is to continue to be a mix of Crown and third party funding, do you think the current mix is equitable?**

- 3.30 Currently the costs of goods clearance are shared between the Crown and third parties (importers, exporters, transport operators etc). The Crown will pay 31% (\$13 million) of Customs' goods clearance costs for 2005/06. Third parties, through a mix of user fees and other charges, will pay 69% (\$29.2 million). Under current government financial planning this will change to 20% and 80% respectively in 2006/07. The current share of funding, let alone projected funding, is totally unacceptable given the overwhelming public benefits associated with goods clearance.
- 3.31 Business New Zealand considers that the full costs associated with customs goods clearance should be funded via general taxation given the overwhelming public benefits associated with such activities.
- 3.32 If this is unacceptable to Government, then Business New Zealand would support virtually all the costs associated with customs' goods clearance being funded via general taxation with minimal contributions from users of customs goods clearance services. At minimum, this would involve a complete reversal of the Government's proposed 2006/07 "20% Crown - 80% third party" funding approach towards, say, "80% Crown – 20% third party" funding.

**Question 13: Currently third parties meet 69 percent of the cost of Customs' goods clearance activities and the Crown meets 31 percent. This will change to 20% and 80% respectively in 2006/07 under current government financial planning.**

**If you do not think the current mix is equitable, what in your view would be the preferred level of contribution by each, to improve equity and economic efficiency?**

3.33 See response to question 12.

**Question 14: What impact would you expect from any change to the current funding mix, particularly in the context of the funding principles for this review?**

3.34 The response to this question is dependent to some extent on how much “change to the current funding mix” is made.

3.35 Assuming that the position of Business New Zealand is adopted as advocated in this submission’s recommendations (i.e. preference for 100% Crown funding), then clearly the funding arrangements would more equitably reflect the strong public good elements associated with goods clearance and therefore contribute towards greater economic efficiency by ensuring that the beneficiaries of goods clearance (general taxpayers) pay the costs associated with this service.

**Question 15: Under the current funding arrangements, different levels of contribution from the Crown and third parties apply to imports, exports, international mail and excise. Do you have any views on the relative levels of contribution for each of these major transaction types and how are these views related to the funding principles?**

3.36 Bryce Wilkinson, in a paper for the Travel and Trade Industry Coalition<sup>6</sup> outlined in some depth the relative public good elements associated with the goods clearance of both imports and exports. Business New Zealand would recommend that the New Zealand Customs Service refers to this paper. In essence Wilkinson’s paper concluded in respect to incoming goods and travellers: *“there is an overwhelming public good case for mandatory screening of incoming goods and travellers for the benefit of the public at large – and therefore for funding from general taxation”* (p.ii).

3.37 In respect to outgoing goods and travellers Wilkinson concluded: *“there is a plausible public good case for mandatory border and supply chain security requirements for outgoing goods and travellers for the benefit of the New Zealand public at large – and therefore for taxpayer funding of the associated costs”* (p.iii).

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<sup>6</sup> “Assessment of Beneficiaries and Public Good Issues Relating to Cost Recovery for Supply Chain Security and Border Protection” – A paper prepared for the Travel and Trade Industry Coalition by Bryce Wilkinson, Capital Economics Ltd, January 2004.

- 3.38 Wilkinson also noted the importance of trade, and therefore effective goods clearance for the benefit of the New Zealand economy and its citizens in general: *“A public good rationale also applies in respect of a desire by the government to protect New Zealanders at large from the serious economic dislocation that could result from an event that abruptly deprived New Zealand of access to major export markets for a prolonged period”* (p.16)
- 3.39 Wilkinson’s analysis of goods clearance both in respect to outgoing and incoming goods as having strong elements of a public good, strongly suggests that Government funding is the most appropriate. Presumably, the same principles would apply in respect to international mail as with the movement of individuals and goods.

**Question 16: In respect to each type of transaction (imports, exports, international mail or excise), if there were a change to the funding mix what impact would you expect that to have?**

- 3.40 See response to question 14.

**Question 17: If a form of mixed Crown and third party funding is to continue into the future, are there any changes to the current administration of cost recovery that would in your view improve equity or economic efficiency?**

- 3.41 Business New Zealand is not in a position to comment on the details of the current administration of cost recovery but would recommend that the New Zealand Customs Service consults with export bodies as appropriate.

Business New Zealand **recommends** that:

**the full costs associated with customs goods clearance are funded via general taxation given the overwhelming public benefits associated with such activities.**

**Without prejudice to the above recommendation:**

Business New Zealand **recommends** that:

**Virtually all of the costs associated with customs goods clearance should be funded via general taxation with a low level of contributions from the users of customs goods clearance services. At minimum, this would involve a complete reversal of the Government's proposed 2006/07 "20% Crown - 80% third party" funding approach to, for example, an "80% Crown – 20% third party" funding approach.**



## **APPENDIX 1**

### **BACKGROUND INFORMATION ON BUSINESS NEW ZEALAND**

Encompassing four regional business organisations (Employers' & Manufacturers' Association (Northern), Employers' & Manufacturers' Association (Central), Canterbury Employers' Chamber of Commerce, and the Otago-Southland Employers' Association), Business New Zealand is New Zealand's largest business advocacy body. Together with its 57 member Affiliated Industries Group (AIG), which comprises most of New Zealand's national industry associations, Business New Zealand is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

In addition to advocacy on behalf of enterprise, Business New Zealand contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.

Business New Zealand's key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD (a high comparative OECD growth ranking is the most robust indicator of a country's ability to deliver quality health, education, superannuation and other social services). An increase in GDP of at least 4% per capita per year is required to achieve this goal in the medium term.

The health of the economy also determines the ability of a nation to deliver on the social and environmental outcomes desired by all. First class social services and a clean and healthy environment are possible only in prosperous, first world economies.