

**SUBMISSION TO AUSTRALIAN PRODUCTIVITY  
COUNCIL**

**REGARDING**

**THE RULES OF ORIGIN FOR THE CLOSER  
ECONOMIC RELATIONSHIP (THE CER)  
BETWEEN AUSTRALIA AND NEW ZEALAND**

**FROM**

**THE NEW ZEALAND FOOTWEAR INDUSTRY  
ASSOCIATION (NZFIA)**

**OCTOBER 2003**

## **1. INTRODUCTION**

We are pleased to have been requested to make a submission on the Rules of Origin that should apply to the CER to the Productivity Commission. We were particularly glad that John Clark was able to discuss issues arising from the consideration of the Rules of Origin with Mr Cosgove and Mr Williams of the Commission on their visit to the EMA in Auckland on 29<sup>th</sup> September.

## **2. BACKGROUND**

The basis for Rules of Origin is the concept of “substantial transformation”. This requires that for a product to be deemed to be the product of a country it must have been through a production process which substantially transforms that product from its raw material or components.

There are three generally accepted ways of defining when “substantial transformation” has taken place.

- 2.1 By requiring that the local or area content (i.e. content coming from the country of origin or, in the case of the CER, from both Australia and New Zealand) of the product reach or exceed a specified percentage of factory cost.
- 2.2 By defining certain operations undertaken in the manufacturing process that must be done locally, - “specified operations”.
- 2.3 By ensuring that the raw materials or components used are from a different tariff classification to the finished product, known as a “change of tariff item”.

## **3. CURRENT DISCUSSION ABOUT THE RULES TO USE FOR THE CER.**

The need to re-examine the current rule of origin pertaining to the CER has arisen due to significant dissatisfaction over the way the rule affects trade across the Tasman under the CER.

The current rule requires that at least 50% of the factory cost of any product must originate in Australia and New Zealand for a product to qualify for duty free access into the other country under the CER.

We understand that the major concerns which have arisen are as follows:

- 3.1 The current rule works against those firms that improve their productivity in that this may reduce the local content of their product.
- 3.2 The current rule works against firms which utilise high cost imported raw materials or components (such as expensive fabrics in the apparel

industry) as this increases the outside area content, even though they may fully produce the product within the local area.

- 3.3 Variations in exchange rates applying to imported materials or components may cause the percentage of local area content to change without any intention or action from the firm involved.

#### **4. POSITION OF THE NZFIA**

The NZFIA bases its submission on the following principle:

“The rules should ensure that to benefit from zero tariff access under the CER a full manufacturing process must be undertaken locally rather than a “lick and stick” assembly operation.”

The NZFIA wishes to make the following points:

- 4.1 The area content rule though under pressure is understood by all parties.
- 4.2 There is a declared intention of both Australia and New Zealand to move towards a zero general tariff which will eliminate the tariff benefit of the CER and eliminate the significance of the Rules of Origin. This may however take some years to achieve.
- 4.3 It is important that the rules ensure a development of trade under the CER through the remaining years of its significance as a trade benefit.
- 4.4 The NZFIA prefers that the rules remain at a local area content of 50% of factory cost as this is the best means of ensuring that its expressed principle is achieved.
- 4.5 The NZFIA does however understand the concerns of other industries, notably the apparel industry, and would reluctantly accept a reduction of the required local area content to 40%.
- 4.6 The NZFIA would request further input if there is a move to adopt the “change of tariff heading” as the determinant of substantial transformation. Such a change would require a close examination of the tariff and must take into account the fact that whilst most finished footwear is included under chapter 64 of the tariff, this chapter also includes “parts of footwear”. A change of tariff heading would thus require an examination of at least the four digit tariff classification.
- 4.7 The NZFIA is not generally in favour of using specified operations as a means of determining substantial transformation as it is difficult to ensure effective description of such specified processes and any list would have to be revised as technology changes. The NZFIA does however consider that specified processes may be necessary to supplement a change in tariff heading should this determinant be suggested.

## 5. EXCHANGE RATES

The NZFIA understands that substantial fluctuations in the exchange rate can be a problem under the area content rule for substantial transformation.

Whilst the NZFIA does not see any way of eliminating this factor it points out that should a twelve or eighteen month moving average of exchange rates be used this would smooth violent fluctuations and give firms greater certainty that they cannot be ambushed by sudden fluctuations.

## 6. NZFIA RESOLUTION

At its Council Meeting held on the 30<sup>th</sup> September 2003 the NZFIA passed the following resolution:

Minute 9

*it was moved by John Robertson, seconded by Cushla Buswell that the Association pushes for the continuation of the % of local content rule at a minimum of 40% if the current level of 50% cannot be sustained. While the Association does not oppose “substantial transformation by means of change of tariff heading” we consider great care will be necessary in framing the rules of such a regime in order to avoid confusion- Carried.*

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