Australian Government
The Treasury

Ministerial Brief

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FOR INFORMATION - Productivity Commission release of research report on the compliance costs of 'nuisance' tariffs; s 22 [redacted]

TO: Treasurer - The Hon Dr Jim Chalmers MP

KEY POINTS

Report on the Nuisance Costs of Tariffs

- The Productivity Commission (PC) will release a research report on the Nuisance Costs of Tariffs (the Report) on 5 August 2022. An embargoed copy of the Report is included in Attachment A. The key findings of the report are outlined in **Additional Information.**
  - The Report explores the structure of Australia's tariff system and examines the nuisance costs of the system, along with its fiscal and economic implications.
  - The PC defines 'nuisance' tariffs as those that raise little revenue for the Government, have negligible benefits for Australian producers, but impose compliance costs on businesses.
- The Report highlights the diminishing importance of import tariffs as a revenue source for the Government and the associated burdensome administration and compliance costs imposed on Government and businesses.
  - Australia's import tariffs provide little protection to domestic producers as most imports are either duty-free or have reduced tariff rates due to businesses accessing concessions and preferential tariff agreements (PTA).
  - In 2019-20, import tariffs collected $1.5 billion or 0.3 per cent of total Australian Government revenue, creating an average social cost of $0.59 - $1.57 per dollar of revenue collected. The average social cost is expected to rise to $1.41 - $4.81 (per dollar of revenue collected) once PTAs with India, UK and the EU are finalised.
- PTAs and concessions have increased Government administration costs and compliance costs for businesses, which are wholly or at least in part passed on to consumers.
  - The PC estimates PTA-related compliance costs to be in the range of $700 million to $2.2 billion in 2019-20. At the upper end, this is $700 million more than the total tariff revenue raised in the same financial year.
  - Around 63 per cent of imports facing a positive tariff were intermediate and capital goods. The imposition of tariffs on such goods raises production costs for businesses and reduces their competitiveness.

- The PC's findings suggest that the regulatory and compliance costs of nuisance tariffs on the Australian economy significantly outweigh any revenue or protective benefits they bring.

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ATTACHMENTS

A: Productivity Commission Report on the Nuisance Costs of Tariffs (embargoed copy)

B: s 22 [redacted]

ADDITIONAL INFORMATION

Summary of Nuisance Costs of Tariffs Report

Chapter 1: What this study is about

- The report sheds light on Australia's complex tariff system and investigates the claim that some tariffs are 'nuisance tariffs'.
- There is no unique definition of a nuisance tariff. For this reason, the study investigates costs associated with all tariffs, including government administrative costs in managing the system and business compliance costs.
- The study excludes the effects of other taxes, charges and costs that do not directly relate to tariffs. For example, excise taxes and GST as well as processing charges associated with quarantine, security etc.

Chapter 2: The tariff system

- Current import tariffs are levied at a default statutory rate of 5 per cent. However, businesses can access discounted tariff rates (usually zero) through a tariff concession order, PTA or other instrument. The importer must apply to obtain the discount rate, as it is not applied automatically.
  - In 2019-20, the average applied tariff rate on imports was typically much lower than the typical 5 per cent statutory rate due to the extensive use of preferences and concessions.
    - Of imports facing a positive statutory rate in 2019-20, 58 per cent fell into a tariff classification for which the average applied tariff rate was less than 1 per cent of import value, while 34 per cent fell into a tariff classification for which the average applied tariff rate was less than 0.5 per cent of import value.
  - However, even if a concession or preference is available, some importers choose to pay the statutory rate to avoid incurring compliance costs associated with obtaining a reduced tariff rate.
- In 2019-20, 90 per cent of imports faced a zero tariff rate either because the statutory rate was zero (49 per cent of imports) or a PTA or concession was applied (28 per cent and 13 per cent, respectively).
- Across the world, greater utilisation of PTAs by countries have contributed to the fall of average applied tariff rates (from 5.4 per cent in 1997 to 2.6 per cent in 2017). Some countries, such as Switzerland, have opted to unilaterally abolish tariffs as the associated compliance costs were not worth the small amount of revenue collected.

Chapter 3: Fiscal implications

- Revenue from import tariffs has decreased in the last 30 years. Import tariffs collected $1.5 billion or 0.3 per cent of total Australian Government revenue in 2019-20, compared with 2.1 per cent of total revenue in 2002-03.

- In 2019-20, the revenue foregone as a result of PTAs and concessions amounted to $6.2 billion, significantly exceeding the actual amount of revenue collected from tariffs. This gap will likely widen once the EU PTA negotiations are finalised, and the recently signed UK and India agreements come into force.

- Administration costs to Government are estimated to be between $11 million and $20 million annually, comprising processing costs and management costs. A small amount of this estimate is from collecting the tariff – managing the tariff system involves many moving parts, including providing tariff advice, administering tariff classifications and concessions, undertaking compliance activities and negotiating PTAs.

  - The PC caveats that these costs are likely to be grossly underestimated as it was not possible to account for all costs in the study.

Chapter 4: Economic implications of tariffs

- While tariffs may protect domestic producers from foreign competition, they impose compliance costs on Australian importers and also distort domestic production and consumption to some degree.

- Businesses that import goods to Australia face significant compliance costs from trying to access discounted tariffs through PTAs. Costs of this nature fell within the range of $0.7-$2.2 billion in 2019-20. In addition, costs associated with accessing TCOs amounted to at least $5 million in 2019-20 (the PC notes that this is likely to be underestimated due to the lack of data).
  - PTA-related costs involve meeting Rules of Origin requirements, imposed on both foreign exporters and Australian importers. Sometimes, these costs are passed along the supply chain to consumers.
  - Costs associated with accessing TCOs are not well-documented, but can involve engaging customs brokers to apply for a TCO, appealing to revoke an existing TCO or disputing the creation of a proposed TCO.

- The PC notes that instruments other than PTAs and TCOs can be used to reduce tariff rates. However, the PC has only estimated compliance costs associated with using the first two, as they are the most common methods.

Chapter 5: Why the nuisance costs of tariffs matter

- Australia's low-rate tariffs are likely to be inefficient as a source of government revenue, as the associated costs outweigh the revenue generated. This is compared to other forms of taxation, such as personal income tax.
- The introduction of new PTAs will add further complexity to the tariff system and will result in further administrative and compliance costs to Government and businesses. Compliance costs will likely grow by 22-23 per cent.
- Implementation of new PTAs for Australia will see a further reduction in the average tariff rate on imports. The PC estimates that implementation of Australia's PTAs with the UK, India and the EU will expand total preferences provided to importers by around 20 per cent and will reduce the tariff revenue collected to between $579 million and $664 million.
- The PC notes the value of future research on values and costs not in the scope of this study, such as the value of tariffs as leverage in trade negotiations, estimating the true costs of compliance, and perhaps implications for Australia's trade, border and industry policies.