NEW ZEALAND
CUSTOMS SERVICE
TE MANA ĀRAI O AOTEAROA

PROTECTING NEW ZEALAND'S BORDER

AIDE MEMOIRE

2 April 2020 RPT 20/057A

FINANCIAL IMPACT OF COVID-19 ON BORDER AND TRANSPORT AGENCIES

Cabinet Meeting on 6 April 2020

Overview

- Attached are proposed speaking points for the *Financial impact of COVID-19 on border and transport agencies* paper that you will presenting to Cabinet on Monday, on behalf of border sector and transport sector Ministers.
- s 9(2)(g)(i) OIA [redacted]
- MBIE has however reduced the funding sought though this paper, from $180 million to $100 million for this financial year. We understand that MBIE reduced the time horizon for its modelling from two financial years to one financial year (the same as other government departments). As a result, MBIE's required funding drops from $180 million to $100 million, and the consolidated department total (Customs, MBIE, MPI) of required funding drops from $270 million to $190 million.

SPEAKING POINTS

Action sought

On behalf of the Ministers of Economic Development, Transport, Immigration and Biosecurity, I am seeking Cabinet's agreement to establish a liquidity facility for border and transport agencies to mitigate the revenue shortfall from COVID-19.

Speaking points

- COVID-19 is having a significant impact on the ability of border and transport agencies[1] to collect third party revenue, with the collapse in traveller volumes and decline in goods imports and exports volumes.
- Each agency's situation is different, and the difference in operating models between public service departments and Crown entities means assistance is more urgent for some agencies than others. My colleagues can talk to the specifics of their agencies.
- I recommend establishing a funding facility to provide capital and operating funding across the border and aviation agencies covered in this paper:
  - departmental capital injections totalling $190 million to ensure affected departments remain solvent for the remainder of 2019/20
  - a non-departmental output expense multi-year appropriation totalling $236.6 million over 2019/20 and 2020/21 to ensure affected transport Crown entities remain solvent through to the end of 2020/21.
- From 1 July 2020, departments may call on their 2020/21 Crown funding – this will underpin some of their cash flow for part of 2020/21, but is not expected to replace all of it.
- As part of the Aviation Relief Package, Cabinet suspended all funding reviews across border and aviation agencies for 12 months. This will contribute to funding pressures for some agencies.
- Depending on the track of the pandemic, agencies may need to return to Cabinet requesting further cash support later in the 2020/21 financial year.

Financial implications of COVID-19 for Customs

- Customs receives nearly two-thirds of its departmental revenue from third party fees and levies. These are charged on international travellers and goods crossing New Zealand's border.
- On the basis of significant reductions in volumes of travellers and goods crossing the border, Customs faces a $30 million shortfall in forecast revenue for the four months to 30 June 2020 and a balance sheet position falling below a manageable level by May 2020.

[1] Border and transport agencies are: Customs, MBIE (Immigration NZ) and MPI (Biosecurity NZ) and MoT (Civil Aviation Authority (incl Avsec) and Maritime NZ). Waka Kotahi the NZ Transport Agency is not covered by this paper.

- The impact on the Border Clearance Levy memorandum account is significant. The account will move from a forecast deficit of $8 million to approximately $28 million by 30 June 2020. The deficit for revenue on goods is forecast to exceed $8 million.
- I am therefore seeking Cabinet's approval for a $30 million capital injection to Customs to cover this shortfall.
- I am also seeking Cabinet's approval to amend the Customs and Excise (Border Processing Levy) Order 2015 to enable the current Border Clearance Levy rates to be carried over into the new levy period starting 1 July 2021. This would give effect to Cabinet's earlier decision to suspend funding reviews for the next 12 months in respect of Customs' passenger clearance fees.
- To align with the suspension of funding reviews, changes related to Customs' goods clearance fees, set to take effect from 1 June 2020, will need to be deferred for 12 months, and I propose the associated report-back on the revenue loophole also be deferred.

Next steps and opening for colleagues to talk to the specifics of their agencies

- I recommend that border and transport Ministers provide Cabinet with an update of this paper, including re-forecasting the financial impacts for 2020/21, by the end of July 2020.
- I also recommend that border and transport Ministers report back to Cabinet by the end of November 2020, once agencies have a more firm view of what a post-outbreak rebound might look like. This report back would include proposed processes, timelines and parameters for future reviews of border and aviation fees for passengers and goods.

Annex A – Table of Customs-specific recommendations

Table 1: Customs-specific recommendations in the Cabinet paper

<table>
<tr><th colspan="2">Customs-specific recommendations</th></tr>
<tr><td>10</td><td>note that Customs receives approximately 61 percent of its departmental revenue from third party fees and levies and, on the basis of significant reductions in volumes of travellers and goods crossing the border, will face a $30 million shortfall in forecast revenue for the four months to 30 June 2020 and a balance sheet position falling below a manageable level by May 2020;</td></tr>
<tr><td>11</td><td>approve the following capital injection to Customs to give effect to the decision in recommendation 5 above,:
<table>
<tr><td></td><td colspan="5">$m – increase/(decrease)</td></tr>
<tr><td></td><td>2019/20</td><td>2020/21</td><td>2021/22</td><td>2022/23</td><td>2023/24 & out-years</td></tr>
<tr><td>New Zealand Customs Service:
Capital Injection</td><td>30.000</td><td>-</td><td>-</td><td>-</td><td>-</td></tr>
</table>
</td></tr>
<tr><td>25</td><td>agree to amend the Customs and Excise (Border Processing Levy) Order 2015 to enable the current levy rates to be carried over into the new levy period starting 1 July 2021 and enable greater flexibility in setting the duration of the levy period;</td></tr>
<tr><td>26</td><td>invite the Minister of Customs to issue drafting instructions to the Parliamentary Counsel Office to implement the decision in recommendation 25 above;</td></tr>
<tr><td>27</td><td>defer the implementation of changes related to Customs’ goods clearance fees, set to take effect from 1 June 2020 [CAB-19-MIN-0334 refers], for 12 months, to align with the suspension of funding reviews [recommendation 4 refers];</td></tr>
<tr><td>28</td><td>agree that Customs implement one of the changes related to recommendation 27 above – that Customs cease to require a $5,000 security from intellectual property rights holders;</td></tr>
<tr><td>29</td><td>s 9(2)(d) OIA [redacted]</td></tr>
</table>

Annex B – overview of Customs' cost recovery

- In 2018/19, of Customs' $201 million revenue, $124 million (62%) was from third party fees and levies, of which:
  - $66 million (53%) was for Border Clearance Levy
  - $43 million (35%) was for Import Entry Transaction Fees
  - $15 million (12%) for Goods Cost Recovery.
- In FY 2019/20, third party revenue from these fees and levies was forecast to make up approximately $132 million (61%) of Customs' total revenue.

Customs' Border Clearance Levy

- Customs' Border Clearance Levy fully recovers the costs incurred by Customs for processing international travellers at the border. The Customs and Excise (Border Processing Levy) Order 2015, provides Customs with the authority to fully recover its costs of processing international travellers through the Border Clearance Levy. Under the Order, Customs is required to review the levy rate, according to a set formula, before the commencement of the next levy period on 1 July 2021.

Customs' goods cost recovery

- Customs is responsible for clearing goods entering or leaving New Zealand. This involves assessing goods for risk, detecting error and fraud, and ensuring import and export control systems are complied with. It also ensures that importers and exporters declare the correct classification, origin and value of their goods, and pay the appropriate duties and taxes.
- All goods entering or leaving New Zealand must be cleared by Customs. The costs that Customs incurs are primarily recovered from importers and exporters and/or their carriers and agents, through the following charges:

Charge	Who pays
Import and export entries	
Import Entry Transaction Fee (IETF)	Fixed charges tied to entries paid by individual importers and exporters. Entries are required for all goods valued over the de minimis and provide detailed information about the goods.
Export Entry Transaction Fee (EETF)	
Cargo reports	
Inward Cargo Transaction Fee (ICTF)	Fixed charges attached to each cargo report paid by transporters and consolidators/freight forwarders. Reports are required for all shipments and provide summary information about the cargo for Customs' clearance activity. They are used to risk assess goods where there is no import or export entry. A report can contain multiple consignments from different importers/exporters.
Outward Cargo Transaction Fee (OCTF)	

- On 9 December 2019, Cabinet agreed to changes to Customs' goods clearance fees, Customs' hourly rate, and the recovery of costs related to intellectual property rights; to come into effect from 1 June 2020 [CAB-19-MIN-0334 refers].
- s 9(2)(d) OIA [redacted]

Annex C – Modelling the financial impacts of COVID-19

Modelling Scenarios

- Border and transport agencies coordinated modelled data to ensure all agencies used a consistent base to forecast the financial impacts of COVID-19. Some assumptions used in the model are more relevant to those operating in a domestic market while others focus on border operations. Two models were used: a best case scenario and a worst case scenario.
- Agencies were asked to use the worst case scenario to estimate the impact on their operating position. On the basis of significant reductions in volumes of travellers and goods crossing the border, Customs faces a $30 million shortfall in forecast revenue for the four months to 30 June 2020 and a balance sheet position falling below a manageable level by May 2020.

Table 1: The table below forecasts the revenue shortfall by 30 June 2020

	Best case scenario model	Worst case scenario model
Passenger volumes reduce by…	90% through to December 2020 Recovery period from January to September 2021	90% in March 2020, then 100% from April to December 2020 Recovery begins slowly from January 2021 and goes through to June 2022
Goods volumes reduce by…	a variable rate, averaging around 25% through to June 2020 Recovery begins July 2020; volumes return to a general reduction of 5% by February 2021, through to March 2022	50% through to December 2020 Recovery begins December 2020 through to July 2022

Forecast Cash position based on modelling scenarios

Table 2: Forecasting the revenue shortfall by 30 June 2020

	Best case scenario model ($m)	Worst case scenario model ($m)
Board Clearance Levy Memorandum Account deficit	(27.5)	(28.8)
Goods Deficit	(6.0)	(8.2)
less		
Current forecast Border Clearance Levy Memorandum Account deficit	(8.0)	(8.0)
Change in deficit 30 June 2020	**(25.5)**	**(29.0)**

Table 3: Forecasting the cash injection needed to maintain a target cash balance

	Best case scenario model ($m)	Worst case scenario model ($m)
Cash Forecast		
Cash position 30 June (incorporating forecast operating underspend and opening cash balance)	4.1	(9.1)
less		
Target cash balance	23.0	23.0
Cash/Capital injection needed to maintain a cash balance of $23m	**18.9**	**32.1**

Capital injection from the Crown

- To provide operational certainty and meet expense levels until 30 June 2020, Customs is seeking a $30 million capital injection from the Crown.
- The worst case scenario suggests a cash injection of $32.1 million. Customs is currently forecasting that expenditure will come in close to budget at year end. Year to date, the department is under budget by approximately $4 million.
- Customs will continue to reprioritise activities and investment decisions as they become more aware of the medium- to long-term impacts.
- In the worst case scenario, we would have a $20 million increase in the Border Clearance Levy memorandum account deficit and an $8 million deficit for goods.