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Vote Customs

Four-year Budget Plan

30 November 2010

Submitted by:

New Zealand Customs Service

Section 1: New Baseline and Summary of Changes

Direction of Change

Customs faces major pressures and opportunities from domestic and international sources, including increased economic activity by New Zealand businesses and in the Asia-Pacific, and increasing more complex risks. Customs' priorities over the next four years reflect these pressures and opportunities, and contribute to the achievement of the Government's priorities.

Customs will manage increasing demands within existing resources through better targeting of risks and resources, and innovation to achieve efficiencies and step change. Continued efficiency gains across the border sector are crucial.

There is one capital initiative that requires a decision in Budget 2011: further investment in automated border processing capacity (SmartGate) for increased passenger demand, and to build on the gains achieved from Government's initial investment in SmartGate. Further investment will provide economic benefits and enable the optimal use of resources while maintaining service levels.

Overall Impact

Operating	**Impact ($000s)**				
	2010/11	**2011/12**	**2012/13**	**2013/14**	**2014/15**
Current Baseline	136,159	148,295	155,915	156,168	156,168
Cost of new/increased activities - additional Smartgate capital investment	-	831	1,336	1,336	1,336
Amount reprioritised	-	-	-	-	-
New baseline	136,159	149,126	157,251	157,504	157,504

Capital	**Impact ($000s)**				
	2010/11	**2011/12**	**2012/13**	**2013/14**	**2014/15**
Capital proposals seeking decisions in Budget 2011	-	-	-	-	-
Capital proposals seeking new funding in Budget 2011 – additional Smartgate investment.	-	3,950	-	-	-

Section 2: Vote Priorities and Pressures

Achievements and links to Government's priorities

Over the next four financial years, Customs will achieve the following:

- more efficient, streamlined, and secure passenger facilitation, particularly for trans-Tasman and Asia-Pacific travel
- streamline and simplify trade facilitation, and promote secure and efficient trade, particularly with Australia and China
- increase disruption of supply chains and dismantle criminal networks, particularly for illicit drugs and people smuggling, and maintain responsiveness as risks change.

These achievements link to the Government's priorities to:

- grow the economy
- reduce regulatory and compliance demands
- step up infrastructure investment
- clamp down on criminal gangs and the 'P' trade and thereby reduce violent crime and make communities safer.

Major pressures facing Customs

Customs manages the movement of all people, goods, and craft across the New Zealand border: 10.2 million passengers, 70 million goods transactions, and 67,000 craft movements a year. Some of the outcomes from this movement are: over $80 billion of imports and exports, more than $10 billion of Crown revenue collected, and $9.3 billion of tourist expenditure.

Customs takes an integrated approach to managing the border and revenue risks from these movements, resulting in efficiencies for government and minimal compliance costs for traders and travellers. Customs provides and manages the key border infrastructure that supports other agencies (eg integrated border transaction processing and information systems, the Integrated Targeting Operations Centre).

Customs has an excellent international reputation for its role in border management and customs administration, adding value to New Zealand in terms of influencing global forums and in trade negotiations.

Major pressures and opportunities facing Customs include:

- increased economic activity domestically and in the Asia-Pacific
- increased risks and complex offending patterns
- increased demand for more secure and efficient global supply chains

- increased costs and increased activity
- implementation of the Joint Border Management System (JBMS) and SmartGate, and changed business processes to achieve the value from these investments.

Major drivers and risks include:

- **recovering volumes of people, goods and craft.** Passenger numbers have recovered to pre-recession levels, and are expected to grow: inbound travel by 579,000 passengers and outbound travel by 433,000 passengers by 2016.[1] Import volumes are expected to grow strongly in the medium to long term. Both imports and exports are expected to grow by 5.1% to 5.3% in 2012.[2]

  Recovering travel and trade volumes present a challenge for Customs with aging computer systems and high public and industry expectations of quick, seamless processing through air and sea ports. Capped Crown funding of passenger processing services places additional pressures on Customs' baseline.[3] This is being mitigated through reprioritisation and investment in initiatives like SmartGate — the trans-Tasman automated border processing programme.

- **increasing trade and travel with Asia-Pacific.** Free trade agreements (FTAs) have been developed with a number of Asian countries. The Government aspires to double trade with China by 2015. Inbound travel from China is expected to double by 2016.[4] Customs will support increased trade and travel with China and the Asia-Pacific, and manage the risks generated from the increased activity. This is being advanced through the development of enhanced infrastructure and organisational capability and new systems (JBMS and SmartGate).

- **international requirements.** These can be arbitrarily imposed and demand substantial resources from Customs, such as the new requirement to screen 100% of air cargo to the United States. This is being mitigated through the development and maintenance of effective international relations, and input into the policy and design processes where possible. Customs also faces increasing costs for the maintenance of international customs relationships, and negotiation and implementation of new FTAs.

- **border as an intervention point for government policies.** Some ten agencies now use Customs' resources at the border to cost effectively achieve Government goals, eg identify student loan borrowers, collect outstanding court fines, and other agency border alerts. This includes data sharing from Customs IT systems, which will be carried through into the design and implementation of JBMS.

- **increasing risk of people smuggling.** Customs is the lead agency for intelligence and interdiction in the event of a mass arrival of illegal migrants by sea. A people smuggling venture into New Zealand would impose significant costs and present other challenges.

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[1] Ministry of Tourism. *New Zealand Tourism Forecasts 2010-2016: Summary Document.* July 2010.
[2] New Zealand Institute of Economic Research. *NZIER Consensus Forecasts.* June 2010.
[3] Ministers have indicated they will not consider cost recovery for passenger processing in the near future.
[4] Ministry of Tourism, 2010. Chinese inbound travel will double by 79,000 to 180,000 passengers.

Interagency planning and related exercise activity is underway to minimise the impact of any such occurrence.

- **the Anti-Counterfeiting Trade Agreement** (**ACTA).** The ACTA proposes international standards for enforcing intellectual property rights. If the Government adopts the ACTA, there may be increased activity for Customs in terms of intellectual property rights enforcement and prosecutions.

- **New and re-started airports.** In 2008/09, Customs' baseline was reduced by $400,000 to reflect the closure of Palmerston North and Hamilton airports' international operations. Customs has since had to re-establish services at Hamilton International Airport and will soon be required to fund services at Rotorua, with no subsequent increase in baselines, and meet the re-establishment or on going operating costs of $420,000 per annum.

- **cost increases.** Customs will need to continue to absorb a range of cost increases including, rent reviews and other occupancy costs, ACC levies, and the impacts of movements in actuarial valuations of staff leave entitlements. There may also be additional cost increases to manage, such as payment of annual leave entitlements.

- **costs of employment agreements.** A new Collective Employment Contract, effective from 1 July 2010 to 30 June 2013, was settled within the established bargaining parameters in June 2010; before the expiry of the previous agreement. Achieving the settlement provides a stable platform for Customs to continue with productivity initiatives, and major projects and events such as JBMS and the expected 85,000 Rugby World Cup visitors. The cost of the Collective Employment settlement is being absorbed by Customs within existing baselines (see below).

Management of pressures

Customs will manage these pressures and risks through careful management of its resources and baseline, in particular through:

- **targeting of risks and resources**. Customs will continue to use resources flexibly and reprioritise task and efforts to focus on the highest priority activities. A new port model introduced in Wellington in 2009/10 takes an integrated approach to managing and allocating resources to activities at the port, airports and client services. A similar model for Christchurch is being explored. Recent operational activity aims to better achieve the outcomes for Customs' contributions to the Government's Methamphetamine Action Plan. The Integrated Targeting Operations Centre better targets border agency resources to address risk.

- **innovation to achieve efficiencies and step change.** The cost of the new Collective Employment settlement, forecast at $3.7 million over three years, will be funded by utilising resources more effectively and efficiently. This includes initiatives such as the port models noted above, and efficiencies made through investment in new technologies such as SmartGate and JBMS.

- **vacancies and scheduling recruitment**. Customs will continue to manage its vacancies taking opportunities to rationalise and direct resources to where they are most effective. Examples of this include moving a senior intelligence position from Christchurch to Wellington and continuing to leave three policy analyst positions vacant, which has resulted in a more limited but focused policy work programme directed towards achieving Government priorities.

- **in house expertise to reduce external recruitment costs.** This has been aided by lower staff turnover and easier access to skilled and qualified applicants. Savings have been made of over $200,000 per year.

- **accommodation and other operating costs**. An Auckland accommodation plan is being progressively implemented, including consolidation of locations, increased co-location with other agencies, and a Customs presence at the Port of Auckland. Operational efficiencies, benefits to industry, and cost savings are all expected to be achieved by the end of 2011/12. In Wellington, Customs moved to the Customhouse in the first quarter of 2010 with the old Customhouse fully sublet.

- **back office and procurement processes.** This includes the government procurement reforms, syndicated purchasing agreements, and savings that may flow out of the Treasury-led Better Administrative and Support Services programme.

Continued efficiency gains and innovation across the border sector are crucial to the management of pressures.[5] The border sector's goals through to 2015 are to increase productivity and manage resource demands within current baselines, and to improve the travel and trade experience. On 8 November 2010, Cabinet noted that the border sector has achieved important successes contributing to value for money, including streamlining trans-Tasman travel and consolidating major information systems [CAB Min (10) 40/5 refers].

Customs baseline for 2010/11 is $136.1 million of which $92 million is Crown funded and the balance, equating to 32% of total appropriation, is cost recovered. Over 65% of the baseline is people related costs with the balance primarily fixed costs of accommodation, equipment, and depreciation. The baseline is not expected to change materially over the forecast period.

Customs has also identified some activities where cost recovery from third parties would not only lower funding demands on the Crown, but also drive further efficiencies in services and overall value for money for the public and private sectors. In 2009/10, a review of the Import Entry Transaction fees was undertaken and changes were made to widen the fee base with effect from 1 July 2010. There are no baseline implications for these fee changes and this change, along with the slow but continued recovery of transaction volumes, is expected to eliminate the short fall in third party revenue that has occurred over the last two years.

A triennial review of goods clearance fees, together with the development of third party funding of the goods clearance component of the JBMS is scheduled to start in December 2011. The original timeframe in the approved JBMS business case for implementation of Tranche 1 was by 1 July 2012.

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[5] The border sector comprises Customs, Ministry of Agriculture and Forestry, Department of Labour, Department of Internal Affairs, and the Ministry of Transport.

However, it is likely to take longer than originally estimated to issue and evaluate the RFP and to then conclude contract negotiations. There are some risks around achieving the 1 July 2012 implementation date, with it more likely to now be 1 December 2012.

If the 1 July 2012 implementation date is not met, there is a potential revenue gap for Customs in 2012. However, there may also be one off operating cost savings through the timing of depreciation, capital charge, and maintenance costs which may help to offset the potential revenue shortfall. The details and timings around this are being worked through. There is likely to be greater clarity around the potential risks and mitigation options by May 2011.

Section 3: Proposed Changes for Budget 2011 (Reprioritisation)

Customs does not consider that it operates any activities inconsistent with Government priorities that should be changed or stopped.

Customs has identified measures to carefully manage its baseline and will continue to proactively make efficiency gains in the face of growing demands. Customs will invest in transformational initiatives such as JBMS and SmartGate. These initiatives are closely related to the Government's goals and priorities and need time and certainty for the benefits to be realised.

Further expenditure reductions over the next four years can only be delivered through reducing staff by more than is required to meet remuneration and cost increases.

In Customs' view, further reductions in staff would be counter productive: New Zealand would see more illegal imports entering the country unchecked; revenue loss; and reduced service to travellers and traders, creating bottlenecks, damage to New Zealand's international reputation, and delays that add compliance and supply chain costs to New Zealand businesses and impact negatively on the economy as a whole.

Instead, Customs recommends that it continues to focus on achieving Government priorities; and achieving a step change in performance through innovation and collaboration in border management. An example of this innovation and collaboration is a greater use of integrated border services to improve delivery for travellers and traders, and investment in technologies such as JBMS, SmartGate and intelligence systems to manage increasing risks and passenger and trade volumes.

New capital initiative

One capital initiative has been submitted that seeks new funding in Budget 2011. This initiative will contribute to the achievement of Customs' priority *More efficient, streamlined, and secure passenger facilitation, as volumes rise.*

Automated border processing capacity (SmartGate) for increased passenger demand

Further investment in automated border processing is required to manage increased passenger demand for automated processing, and to secure and build on the gains achieved from the Government's initial investment in SmartGate.[6]

Without investment, automated clearance uptake is likely to stagnate, if not decline, as eligible passenger numbers increase. Efficiency and effectiveness opportunities would be lost. The vision of the trans-Tasman travel experience being as 'domestic like' as possible could be lost.

Automating systems are a key strategy for managing forecast passenger growth, high volume low risk trans-Tasman travel, and to meet increasing pressures on Customs' priority activities and baselines.

Benefits from further investment in SmartGate include:

- **economic benefits.** Tourism contributes over $9 billion a year to the New Zealand economy;[7] and inbound travel from Australia is expected to increase. Providing tourists with a positive experience at the border is important for tourism generally.

- **optimal use of resources.** SmartGate enables more passengers to be processed cost effectively and within agreed service level timeframes. The technology also minimises the airport space required by Customs to complete passenger processing.

Future capital initiatives

There is one capital initiative that will require a decision in Budget 2012.

Joint Border Management System – Trade Single Window

Capital funding will be sought by Vote Customs and Vote Biosecurity for Tranche 2 of the JBMS–Trade Single Window (JBMS-TSW). Budget 2010 decisions confirmed a total capital investment of $75.9 million for Tranche 1, which is expected to be operational by December 2012. The current total estimated cost for Tranche 2 is $74.1 million.

JBMS-TSW will directly contribute to New Zealand's economic growth through streamlined and simplified border clearance processes for industry; protect New Zealand's community and biosecurity interests through improved risk management and drug harm avoidance; and provide a reliable border control infrastructure to deliver government policies.

To realise the full potential of the JBMS value proposition, investment in Tranche 2 is required which, once completed, has been estimated to provide total benefits of $717 million. The net present value over ten years of the Tranche 1 and Tranche 2 investment is estimated at $176 million.

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[6] SmartGate give eligible trans-Tasman passengers (ie adult New Zealand and Australian e-passport holders) the option to self-process through the Customs primary line.
[7] Ministry of Economic Development. *Key Tourism Statistics.* 21 October 2010.

Section 4: Summary of Financial Movements

With the exception of additional operating expenditure of depreciation, maintenance, and capital charge resulting from the capital bid for additional SmartGate equipment in Budget 2011, no other changes to the 2010/11 and outyear baselines are proposed for Vote Customs.