Consultation

Quota Allocation Mechanism Review (QAMR)

2023/2024

To all registered meat exporters

released: 16 February 2024

Feedback closes: 12 noon 15 March 2024 via survey link

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Background

At intervals not greater than five years, s.29 of the Meat Board Act 2004 (the Act) requires the New Zealand Meat Board (NZMB) to review each unrevoked allocation mechanism.

Access for beef and sheepmeat has increased recently with the advent of the UK and EU FTAs. New Zealand now has nearly 300,000 tonnes c.w.e. sheepmeat tariff-free access to the UK and EU, while total shipped exports are 392,000 p.w. tonnes of lamb and mutton.

Beef access has increased by 15,333 tonnes (12,000 tonnes p.w. plus 3,333 tonnes c.w.e.) to UK and EU respectively, with scheduled (3,980 tonnes p.w. and 953 tonnes c.w.e.) increases on an annual basis.

This quota allocation mechanism review (QAMR) is a scheduled review. It provides an opportunity to improve allocation and administration and better achieve the Board's object to facilitate the capture, for New Zealand and in the interests of the meat industry, the best possible ongoing returns available from quota markets (s.7, Meat Board Act 2004).

To support this quota allocation mechanism review, NZMB commissioned an economic study of allocation mechanisms by Castalia Limited (the Castalia Report). This focused on determining which allocation mechanisms (if any) would best assist the Meat Board in achieving its object. The report also included a comparison with the Australian quota management system.

With the results of the economic analysis of different allocation mechanisms and the associated review of both New Zealand and Australia's red meat quota allocation systems at hand, this review has looked at selected allocation mechanisms and evaluated them against: allocative efficiency, risk, fairness and administrative efficiency.

From an administrative perspective, NZMB now has responsibility for the administration of ten quotas (WTO – EU and UK S&G, EU and UK HQB, USB&V, FTA - EU and UK Beef, UK Sheepmeat, EU Sheepmeat chilled and frozen). It is preferred, for administrative simplicity and associated cost reasons, to minimise the number of allocation mechanisms.

The Castalia review identified six mechanisms and their strengths and weaknesses. Having considered these, rather than consult on all options, the Board wishes to consult on two quota allocation mechanisms for WTO (Production History (PH)) and FTA (Export History (EH)) quotas.

It is not proposed to go into a description of the existing Production History basis for the allocation of WTO quotas. This has been in effect, with minor modification, since the late 1990s, and is well understood by the industry.

As for the FTA quotas, the Board is proposing: a modification to the transitional Production History/Export History hybrid system currently in place, to one in which quota allowances are allocated based on Export History alone.

The proposed mechanism is outlined in detail in this consultation document.

Other proposed modifications include a simplification of the new entrant definition and allocation mechanism, as well as associated removal of consortium provisions. The current new entrant provisions for the WTO quotas are onerous, complex and expensive to administer. Given the increased access now available to the industry, compared with the late 90s and early 2000s, the Board considers them to be unnecessarily strict and administratively burdensome.

The Board is now seeking industry's views on the proposed amendments to the quota allocation mechanisms.

Allocation Mechanism

The performance basis for allocation of quota

The Castalia Report (found here) noted that while some mechanisms are more economically efficient than others, the difference is not so much as to outweigh the other factors that must be considered, especially when quotas are near to or fully utilised.

So, while an auction system was identified as likely the most efficient, there are issues of administration, level of costs, uncertainty surrounding cost recovery and returns, and overall uncertainty for quota holders that make it less attractive as a working mechanism that can be applied effectively in conditions of high and low demand for quota access.

Similarly, first come first served (FCFS) and High-fill trigger mechanisms[1] rely on the Board predicting quota utilisation over the 15 or so months (quota year plus advance allocation period) during which an FCFS mechanism would be in effect, or any change to an alternative allocation system is triggered. Such a predictive system carries risks and uncertainty for quota holders.

Bearing this in mind, the Castalia Report recommended: that either a production/export history hybrid or an export history mechanism would be the most suitable quota allocation mechanisms.

They did, however, identify that a production/export history hybrid mechanism, as has been employed for the UK and EU FTAs, has some problems such as:

"...

a. *Exporters that do not export into the quota market ... will still receive an allocation and then transfer that to an exporter, potentially obtaining a rent*
b. *If an exporter specialises in exporting to the quota market, their allocation from year to year will not align with the quota required to continue exporting at the same level"*

The Board has considered that while transfers are an important mechanism, by which the quota can be optimally utilised, it is preferable that quota is allocated to those entities most likely to use it. Furthermore, allocation mechanisms should ensure that entities with a history of trade in the market concerned, should be allocated quota to enable continuance of that trade, whilst making appropriate allowance for new entrants.

Transitional allocation mechanisms for the EU/UK FTAs

As previously discussed, the new FTAs provide substantial additional access at low or zero tariffs for beef and sheepmeat to the previously highly protected EU and UK markets.

In addition, the FTA quotas include products beyond those normally produced in traditional slaughter and boning plants.

[1] A modified FCFS system whereby at a certain trigger level (in Australia; 80% utilisation) a performance based allocation system is applied to the remainder of the quota.

Some exporters without production capacity have developed trade, into the UK market especially, despite the previously high tariff rates applicable.

These factors point towards an allocation mechanism based on a parameter other than production history of eligible product.

The introduction of an export history component to the transitional allocation mechanism for the EU and UK FTA quotas was to provide access for those entities that had exported to the quota market before the FTA, but which did not have production history. These entities would have been significantly disadvantaged without access to quota as of right.

At the same time the production history component maintained the historical allocation mechanism that had been relatively effective in the past and was well understood by industry.

The inclusion of a production history component, however, allowed companies with eligible production history that had not exported, or exported very little to the market concerned, to receive quota in proportion to their production (rather than activity in the market).

It has also been identified that, even with annual increments to the quota volume, as entities with production history increase exports under the quota in future years, export only entities do not receive sufficient quota to maintain their levels of exports.

An Export History Allocation Mechanism

For the reasons given above; a quota market export history mechanism is preferred (over a hybrid production history/export history mechanism).

However, it is necessary to avoid a situation where exporters receive an allowance considerably in excess of their historical use at the expense of producers of eligible product or exporters that export to other markets. Protecting these latter participants is an element of the Meat Board Act 2004, which requires that an allocation mechanism:

> *"24. (2)(b)*
> *must provide for the allocation of access to existing participants in the meat export industry who are prospective participants in the market concerned;"*

The Meat Board Act also has the following provision:

> *"24 (5)*
> *to avoid doubt, an allocation mechanism may provide for an allocation of access to quota markets to any person who is a registered exporter, whether or not the person currently exports meat products."*

Modes of allocation based on export history

Under an export history allocation mechanism, any person who is a registered exporter and/or existing quota participants (producers or exporters) but does not export to the market concerned, would be treated as new entrants to the quota system.

This means that there would potentially be a larger pool of new entrants to a quota than seen historically, because it would include those entities that have a production base but no history of export to the quota market.

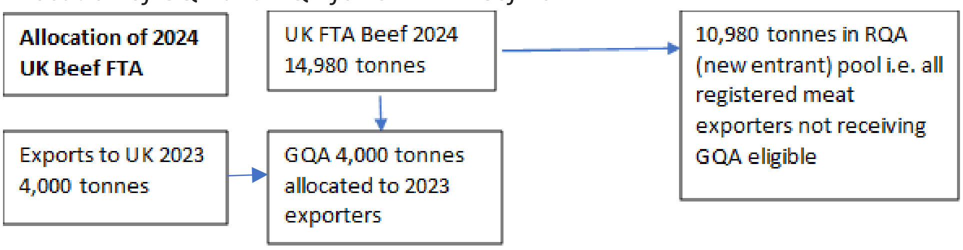
For the new FTAs, under an export history allocation system, (whereby the total quota would be distributed proportionally according to a share of total export history), this issue could be mitigated by setting aside the annual increments in the quotas for new entrants.

However, these annual increments, although larger than historical new entrant tranches, are unlikely to satisfy the increased volume capacity of new entrants.

To overcome this issue, export history holders could receive a quota volume (not proportional) allowance based on previous exports (general quota allowance, (GQA)). The remainder of the quota volume would become a reserved quota allowance (RQA) pool, made available on a FCFS basis to new entrants.

This mechanism provides protection to current exporters to the quota market, up to the level of their export history, while providing a substantial reserved pool for producers/exporters and any other export registered company that do not export to the market concerned.

Example:
Allocation of GQA and RQA for UK FTA Beef 2024



New Entrants have access to the RQA pool on a consignment by consignment (FCFS) basis, by application for a quota certificate. To avoid single large entities flooding the new entrants pool, the maximum access a single entity can obtain is limited to 30% of the RQA total. This limit is removed after the quota handback period and GQA holders have had further access to the residual quota.

Question:
Do you agree that quota handed back in October should be first made available to General Quota Allocation (GQA) quota holders and then to new entrants with the 30% limit lifted?
Yes/No
If not, why not?

Example:

New Entrant access to RQA and returned GQA

New Entrants Allocation

Eligible - all registered meat exporters that haven't received GQA

New Entrants receive quota on application for a quota certificate on a FCFS

Any new entrant can only receive up to 3294 tonnes (30%x10,980) of quota in 2024

Quota handback, including remainder of RQA occurs in October 2024

GQA holders gain access to handback, remainder made available to New Entrants on FCFS basis 30% limit removed

However, it limits the ability of GQA holders (i.e.; those with export history) to increase their export volumes. It also may mean that a large portion of the quota remains unused until quota is handed back to the Board and/or the unused portion of the reserved pool becomes available for general use (usually in the last quarter of the quota year).

To maximise quota utilisation it is proposed that; GQA holders may access the reserved pool once they have utilised 80%* (or some other proportion) of their GQA.

GQA Holder reaches 80% of its GQA allowance

Gains access to remaining RQA on an FCFS (per certificate) basis

It is possible that export volumes may reach or exceed (in the case of out of quota exports) the total quota volume.

In a case where the quota would be fully allocated to GQA holders, to ensure compliance with the new entrants provisions of the Meat Board Act, some part of the quota must be made available to those in the industry that are prospective users. It is proposed that the RQA pool hold a minimum of 3.5% of the total quota volume. This volume would be deducted from the GQA total, with the remainder to be allocated on a pro rata basis.

Example:

Comparison of full allocation vs New Entrants reserved quota

GQA Holders qualify for the whole quota i.e. none available for new entrants

Quota for 2024 = 14,980 tonnes Companies export 15,500 tonnes in 2023

New Entrants (RQA) pool receives 524.3 tonnes (3.5% x 14,980)

GQA Holders allowances are pro rated over the remaining 14,455.7 tonnes

Summary of proposed Export History-based allocation mechanism:

- Allocation of quota allowances be based on export history to the quota market concerned
- Allocation be volume based, that is; participants receive a general quota allowance (GQA) equal to their Export History volume

- New entrants to include any registered meat exporter that has not been allocated GQA for the period over which Export History is calculated.
- The remainder (Reserved Pool) of the quota volume to be available to new entrants up to a limit of 30%, on application for a quota certificate on a First Come First Served (FCFS) basis
- GQA participants gain access to the Reserved Pool once they have utilised a threshold proportion of their GQA (80% proposed)
- GQA volumes may be pro rated to ensure that there is a minimum of 2% of the total quota volume available for allocation to new entrants
- For holders of GQA for the WTO sheepmeat quotas, access to the FTA quota will not be available until they have fully utilised their GQA, or access is required for products that are covered by the FTA quota and not the WTO quota.

Question:
Do you agree that; for the new FTA quotas (EU/UK beef & sheepmeat and goatmeat),
The current production history/export history hybrid mechanism be replaced by an allocation mechanism based on export history?
Yes/No
If not, why not?

Question:
Do you agree that new entrants should have access to the new entrant pool (RQA) on a first come first served (FCFS) basis?
Yes/No
If not, why not?

Question:
Do you agree that new entrants access should be limited to a maximum of 30% of the new entrant tranche?
Yes/No
If not, why not?

Refinements to an Export History allocation mechanism

There are some refinements required to this allocation mechanism, should it be implemented, and feedback on these, as well as the base mechanism is sought.

Definition of Export History

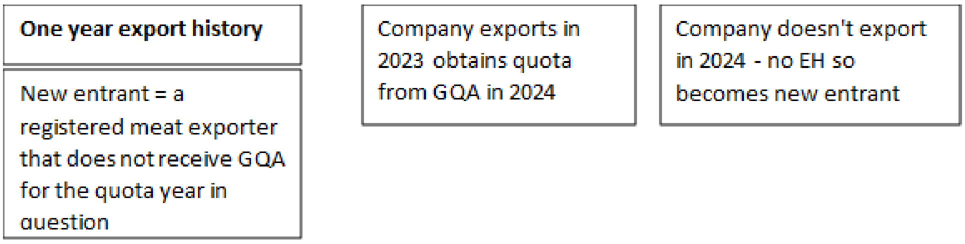
Export History is: a history of having exported quota eligible product, in tonnage shipped weight, over a defined period to the quota market concerned.

The performance period (i.e. production or export history) over which allocations are calculated has traditionally been three years.

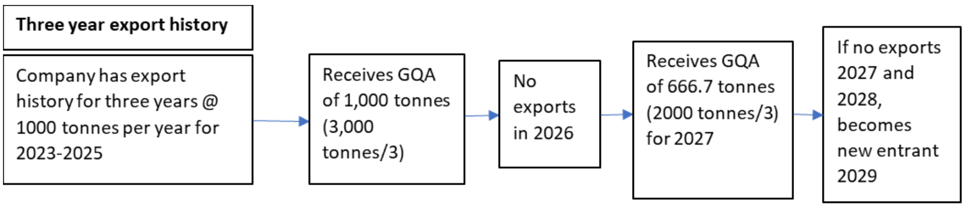
A three year performance period allows for smoothing of allocation across years. It also means that an entity will receive quota, even if they have not exported in the previous two years. Non-export for three consecutive years would revert entities to new entrant status.

On the other hand, if part of the rationale for using Export History is to ensure that those exporting to the market can at least maintain their level of exports, using the previous year's history may be more practical than a three-year average. This is because (in the case of increasing sales year-on-year); a three-year average will provide an allowance less than the previous year's exports. A one year export history period would also mean that once an entity has not exported for a year, they revert to new entrant status.

Example:
Comparison of 1 year vs 3 year Export History and potential effects



Vs



Question:
If an Export History-based allocation mechanism replaces the current system for FTA quotas, would you prefer it be calculated on the previous year's exports or a three-year rolling average?
1 year rolling average vs 3 year rolling average?
If not, why not?

If a three-year performance history period is preferred; a transitional period may be useful, whereby the rolling average allocation is based on one, two and finally three years.

Question:
If an Export History-based allocation mechanism replaces the current system for FTA quotas and a three-year performance history period is adopted, would you be in favour of a transitional period?
Yes/No
If No, why not?

Export History year - Production, Calendar or Quota year?

As a general principle, a performance-based period for allocation should be based on the most up-to-date information available. Systems are now in place to record both export and production histories one month in arrears, although production history is subject to audit.

To allow for unexpected delays, or system issues, and the time necessary to process applications, it is proposed; that allocation be based on an export or production history year, (depending on the allocation mechanism), ending three months before the quota year in question. For example, an allocation of a 2025 calendar year quota, would be based on data up to 30 September 2024.

Question:
If an Export History-based allocation mechanism replaces the current system for FTA quotas, do you agree that the history period should run from 1 October to 30 September?
Yes/No?
If No, why not?

World Trade Organisation (WTO) Quotas

Although the existing WTO quotas (EUSG, EUHQB, UKSG, UKHQB, USB&V) do not have the features of the FTA quotas, which necessitate an export history approach, an export history-based allocation system could also be applied to the WTO quotas.

Adopting a new system would depend upon the overall benefit of doing so.

As has been suggested above, an export history based mechanism is preferred for the new quotas. This will ensure access for entities that have substantial exports, but do not have production history to qualify for quota access and also the introduction in these quotas of processed products, that may be produced outside traditional meat processing facilities. In the case of the WTO quotas the former situation applies but the latter does not.

It is likely that if an export history basis is used for the FTA quotas, this will satisfy the need to provide access to exporters who do not have production history. If this is the case, then the two reasons for applying an export history do not apply to the WTO quotas. The current production history based allocation mechanism has ensured that access to these valuable markets has been confined to those that have invested in production facilities in New Zealand. The administrative systems are well known and understood by participants.

Although some production facilities are foreign owned or have significant overseas ownership, this has required significant investment in the industry and has not been a simple matter of setting up an export company to obtain access to export markets.

Having said that, it is likely that a substantial portion of the quota rent is obtained by the processing companies that supply the market eligible product to an exporter.

So, the arguments in favour of an export based allocation mechanism are fewer for the WTO quotas. Looking at the evaluation criteria, an export history based mechanism is slightly more efficient than a production history base. However, the difference is likely small, given the factors above, and it is possible that the costs of migrating from a production history to an export history mechanism could outweigh any allocative benefits.

There is room however to improve efficiency through a simplification of the new entrant process by removing the provisions that lead to the creation of consortia.

Question: **Do you agree with retaining the Production History based allocation mechanism for WTO quotas?** **Yes/No?** **If No, why not?**

WTO Quotas New Entrants provisions

Recently there has been very little demand for new entrant access to the WTO quotas, especially those for Sheepmeat. This is mainly due to under-utilisation of the quotas, which allows new entrants to readily obtain quota from GQA holders.

The current mechanism for the WTO quotas provides a specific tranche (2%) of quota be set-aside for new entrants. The process of application is complex and time consuming. It requires an applicant to be eligible on two of four criteria and to develop a business case which is assessed by a specially convened New Entrants Allowance Committee (NEAC).

For simplicity of administration, it would be preferable to completely remove the current new entrants system for WTO quotas, and to make the 2% new entrant tranche accessible to any registered meat exporter on an FCFS basis.

The fees structure for FCFS should include additional costs for onboarding and to compensate for the production history audit costs incurred by GQA applicants.

Question: **Do you agree that new entrants for WTO Quotas, who are registered meat exporters, should have first come first served (FCFS) access upon payment of appropriate fees?** **Yes/No?** **If No, why not?**

Question: **Do you agree that new entrants should be limited to a maximum of 30% of the new entrant (RQA) tranche (which remains at 2%)?** **Yes/No?** **If No, why not?**

Question: **Do you agree that new entrants should have access to the new entrant pool (RQA) on a first come first served (FCFS) basis?** **Yes/No?** **If No, why not?**

Other issues

Measures to prevent hoarding and to incentivise utilisation

Penalty thresholds

The New Zealand quota administration system imposes a penalty to:

WTO TRQs: EUSG, UKSG, USBV

- of 0.5% of the company's quota allowance, or 25 tonnes

FTA TRQs: UKFBeef, UKFSheepmeat, EUFBeef, EUFSG (Chilled) and EUFSG (Frozen)

- of 0.5% of the company's quota allowance, or 25 tonnes

WTO TRQs: UK and EU HQB

- of 0.5% of the companies' quota allowance or 30 kilograms

(whichever is the higher) remains unutilised. The penalty is 2x the unutilised volume.

The 30kg threshold for HQB was applied when the quota was only 300 tonnes. Thirty kilograms was .01% of the quota volume. The EU HQB quota is now 1,102 tonnes, so an equivalent proportion today would be 110kg. The 30kg limit is considered to still be appropriate for the UK HQB TRQ which is less than the original 300 tonnes.

Question:
It is proposed to increase the limit for underutilisation of the EU HQB quota without penalty to 0.5% of the company's allowance or 110kg whichever is the greater.
Yes/No?
If not, why not?

Consortia

The New Zealand system allows for applications by consortia. This structure was used by companies that could not meet the new entrant eligibility criteria alone but could do so when operating in conjunction with another company. Given that; for the FTA quotas, the only criterion is to be a registered meat exporter, a process requiring formation of a consortia seems unnecessary.

As far as the Board's quota administration is concerned, running consortium processes adds complexity and cost.

Removing the new entrants application process and replacing it with FCFS for WTO quotas would exclude the need for consortia.

Question:
It is proposed to remove the consortia provisions from the application process.
Do you agree?
If not, why not?

Question:
Do you have any other comments you wish to make?

Feedback Invited

Feedback on this consultation is welcomed to inform next steps.

It is preferred feedback be provided via the survey link here or visit the website.

If you seek clarification on any aspect of this consultation you may contact

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Consultation and feedback will **close midday on 15 March 2024** – please make sure your feedback is provided no later than this date.

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