Administration of an Import Quota

LEARNING OBJECTIVE

Learn the different ways in which an import quota can be implemented to monitor and assure that only the specified amount is allowed to enter.

When a quantity restriction is set by a government, it must implement procedures to prevent imports beyond the restricted level. A binding import quota will result in a higher price in the import country and, in the case of a large country, a price reduction in the exporter's market. The price wedge would generate profit opportunities for anyone who could purchase (or produce) the product at the lower price (or cost) in the export market and resell it at the higher price in the import market.

Three basic methods are used to administer import quotas.

1. *Offer quota rights on a first-come, first-served basis*. The government could allow imports to enter freely from the start of the year until the quota is filled. Once filled, customs officials would prohibit entry of the product for the remainder of the year. If administered in this way, the quota may result in a fluctuating price for the product over the year. During the open period, a sufficient amount of imports may flow in to achieve free trade prices. Once the window is closed, prices would revert to the autarky prices.
2. *Auction quota rights*. Essentially, the government could sell quota tickets, where each ticket presented to a customs official would allow the entry of one unit of the good. If the tickets are auctioned, or if the price is determined competitively, the price at which each ticket would be sold is the difference in prices that exists between the export and import market. The holder of a quota ticket can buy the product at the low price in the exporter's market and resell it at the higher price in the importer's market. If there are no transportation costs, a quota holder can make a pure profit, called a quota rent, equal to the difference in prices. If the government sells the quota tickets at the maximum attainable price, then the government would receive all the quota rents.

3. *Give away quota rights*. The government could give away the quota rights by allocating quota tickets to appropriate individuals. The recipient of a quota ticket essentially receives a windfall profit since, in the absence of transportation costs, they can claim the entire quota rent at no cost to themselves. Governments often allocate the quota tickets to domestic importing companies based on past market shares. Thus, if an importer of the product had imported 20 percent of all imports prior to the quota, then it would be given 20 percent of the quota tickets. Sometimes governments give the quota tickets away to foreigners. In this case, the allocation acts as a form of foreign aid since the foreign recipients receive the quota rents. It is worth noting that because quota rents are so valuable, a government can use them to direct rents toward its political supporters.