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TRANSCRIPT OF PROCEEDINGS

PRODUCTIVITY COMMISSION

DRAFT REPORT ON COST RECOVERY

MRS H. OWENS, Presiding Commissioner
PROF J. SLOAN, Commissioner
DR R. STEWARDSON, Associate Commissioner

TRANSCRIPT OF PROCEEDINGS

AT CANBERRA ON FRIDAY, 15 JUNE 2001, AT 9.10 AM

Continued from 14/6/01

MRS OWENS: Okay, I think we will now commence. Good morning and welcome to the public hearings for the Productivity Commission Inquiry into Cost Recovery by Commonwealth Regulatory Administrative and Information Agencies. These hearings follow the release of the commission's draft report in April. My name is Helen Owens and I'm the presiding commissioner on the inquiry and on my right is Judith Sloan, my fellow commissioner and Robin Stewardson will be joining us shortly.

The purpose of this round of hearings is to facilitate public scrutiny of the commission's work and to get comment and feedback on the draft report. Hearings have already been held in Melbourne and Sydney and, for the last two days, in Canberra. We will then be working towards completing a final report to government in August, having considered all the evidence presented at the hearings and in submissions, as well as other informal discussions. Participants in the inquiry will automatically receive a copy of the final report once released by government. We like to conduct all hearings in a reasonably informal manner, but I remind participants that a full transcript is being taken. For this reason, comments from the floor cannot be taken, but at the end of the proceedings for the day I will provide an opportunity for any persons wishing to do so to make a brief presentation. Participants are not required to take an oath, but should be truthful in their remarks. Participants are welcome to comment on the issues raised in other submissions. The transcript will be made available to the participants and will be available from the commission's Web site following the hearings. Copies may also be purchased using an order form available from the staff here today. Submissions are also available.

I'd now like to welcome Qantas and I'd like to thank you very much for appearing. It was a bit of a surprise, but I think we're all eager to hear what you have to say and I welcome your participation - you participated last time and I think we got a submission earlier in the process - so thank you very much for coming and I'd like you each to give your name and your position with Qantas for the transcript.

MR LONG: Trevor Long, Manager Group Facilitation.

MR CALLAGHAN: David Callaghan, Manager Government Affairs.

MR BYSOUTH: Peter Bysouth, Manager Aviation Charges.

MRS OWENS: Thank you. I understand that one of you, or maybe more than one, would like to make some opening comments, or make an opening statement.

MR CALLAGHAN: Yes, thank you, we will make an opening statement and then we'll be happy to field any questions that the commission might have. We appreciate the opportunity to provide further input to the inquiry. Our initial submission outlined concerns held by Qantas regarding various aspects of charges levied by the Australian government. These included the passenger movement charge, or the PMC; payments to Air Services Australia; funding of CASA; meteorological charges; Department of Defence cross-charging; counter-terrorist first response charges and Sydney Airport pricing proposals. On this occasion we don't propose to

canvas all these areas, but there have been some developments which we believe require further comment.

On the passenger movement charge, since our initial submission and oral comments, the government has announced significant changes to the PMC. In the 2001-2002 federal budget, the PMC was increased form $30 to $38 for travellers effective from 1 July. This initially caused us some concern as at the time of the budget announcement some 376,000 Qantas tickets had already been sold for travel after 1 July 2001. All these reflected the old PMC rate, thus presenting Qantas with a potential shortfall of some $3 million, for which, under the collection arrangements in place with ACS, Qantas would be held responsible. For the industry the shortfall would have been in the order or 9 million. We are grateful that discussions with senior ACS officials have resulted in acceptance of our concerns by the government, with an amendment now to be made to the bill to provide the industry with a transition period that will only hold the airlines accountable for tickets issued after 1 July. This will permit full notification of the change to be promulgated worldwide and will minimise any immediate cost burden on airlines.

There are, however, some other issues related to the PMC to which we'd like to draw attention. The PMC was introduced to meet the full cost of customs, immigration and quarantine clearance of passengers as well as the cost of issue of short term visitor visas. However, over time, this emphasis on cost recovery has changed. According to evidence provided to the Senate estimates committee by the CEO of the Australian Customer Service - and this was to the senate legal and constitutional committee on 28 May 2001 - the PMC over-collects the cost of border services for passengers by some $80 million per annum. The new fee will, on the face it, extend the over-collection.

The airlines are concerned to know how the new arrangements to screen all passengers against foot and mouth will impact on their operations and the extent of any additional costs likely to affect them in the future. There has been no provision made to cover future infrastructure costs to accommodate the additional space requirements of x-ray machines, et cetera beyond an initial stage. Some $20 million has been allocated from budget funds for initial work, but we understand that further work will be required which may, for instance, cost up to $50 million at Melbourne airport alone. No funding has been made available for this work as yet, and we fear that recovery through increased airport charges on airlines may be used to pay for this work.

The new arrangements will require close to 600 additional AQIS and ACS staff to be employed at Australia's gateway airports. At present, airlines pay for the accommodation requirements of AQIS and ACS staff at airports, and without new arrangements the added costs of accommodating these additional staff will also fall on airlines. Regrettably, the increased costs will have to be recovered from the travelling public, either as discrete charges or through increases in air fares. Unfortunately, neither the construction nor the application of the passenger movement charge is transparent, therefore providing no initiative to improve efficiency by the border agencies.

Air Services Australia and CASA funding: the government has stated that the aviation fuel duty has returned $7.6 million more than anticipated in the past two years, but the duty continues to be levied, with its justification being that every cent is returned the industry in the form of increased funding for air safety. No-one will argue that appropriate funding to maintain the highest standards of air safety is a good thing, but we see it as unfair when financial burdens continue to fall disproportionately on the large scheduled service airlines. The government will continue to subsidise tower services at a range of regional airports, with small aircraft operators having their landing charges unchanged, while the jet fuel levy, mostly collected from Qantas and Ansett, is used to cover the lion's share of costs. We are concerned by this as it seems not to recognise user-pays as the guiding principle. CASA will receive additional funding, much of which is also derived from fuel levy, but much of CASA's enhanced activity will be directed at the general aviation sector of the industry.

Counter-terrorist first response funding. As outlined in our original submission, we believe the counter-terrorist first response charge, currently funded by airlines, should be borne by government. Given the ACS admission that an $80 million over-collection from the passenger movement charge, Qantas would submit that this presents a clear opportunity for the government to put some clarity into how the PMC funds are spent and to take the opportunity to use it to cover additional activities that are legitimately related to passenger movements through airports. To our mind, counter-terrorist first response would be in this category.

Government regulation in the aviation sector is not about the diminish and neither, it seems, is the requirement for airlines to meet additional costs of regulation. In our original submission we outlined a number of principles to guide government in ensuring that increased costs are fair, transparent and as close as possible to user-pays. We would again commend this approach to the committee for its consideration. Thank you.

MRS OWENS: Thanks very much, Mr Callaghan. Do either of your colleagues wish to make any comments at this stage?

MR CALLAGHAN: Not at this stage, I don't think, no.

MRS OWENS: Okay. I think what we might do is go through the issues and a good place to start would be the passenger movement charge and I don't know that we're in the position to undo a recent budget decision, just at this stage. All we can say is that if you applied our guidelines to this passenger movement charge, I don't know whether this outcome would be seen as being an appropriate outcome, because we are looking at it from the perspective of beneficiary pays or the regulated pays, and if you try to apply our criteria in our guidelines chapter, I think you would find that the passenger movement charge applies to outgoing passengers - - -

MR CALLAGHAN: Correct.

MRS OWENS: - - - and this is dealing with the potential for foot and mouth disease coming into the country, not necessarily via travellers, so I'm not quite sure whether.

MR CALLAGHAN: I guess the premise is that outgoing passengers are also going to be incoming passengers at some other time, because the overwhelming majority of traffic is two-way.

MR BYSOUTH: Just on that, the ease of collection is to put it on the outgoing ticket. The assumption that David has mentioned is that justification follows on from the administrative ease of putting it on the outgoing passenger.

MRS OWENS: But basically what the government is trying to do is protect the Australian public and Australian industry from the threat of foot and mouth disease. Now, the beneficiary, you could say, is the whole community in this case.

PROF SLOAN: And the farmers.

MRS OWENS: And the farmers.

MR LONG: It certainly seems, from our discussions with AQIS who are running with this issue, is that the beneficiaries are primarily the primary industry, protecting from agricultural disease and it's not just - and we need to be clear on this - it's not just foot and mouth that they've decided to look at. It's effectively any type of biological product which would come into the country and spread disease. There is, of course, the question as to whether or not this level of protection is appropriate, given the fact that foot and mouth and other diseases have been in existence for many, many years and there has never been an outbreak in Australia as a direct result of people coming in. But, be that as it may, the issue that we have here is the quantum of the passenger movement charge, the lack of transparency of where it's being used and the fact that there is, by the evidence of the CEO of Customs, a significant over-collection which we believe either needs to be adjusted by a review of the charging, or conversely utilising some of that over-collection to meet other costs which are being imposed on the industry which is directly related to passengers.

Now, we've addressed the issue of counter-terrorist first response. There is another issue coming down the track, which should be here next year, and that is additional security, which is being moved under a bill that's in parliament at the present moment, which will introduce a form of screening for passengers' baggage, for which the airlines will probably be required to pay for. That goes under the acronym of AAA - I'm sorry, I can't tell you what it means - but, nevertheless, it is there and it is another regulation that is being imposed upon the industry that we see there are funds here already being collected that could be utilised for it.

MRS OWENS: I suppose the presumption is that the airlines will then pass those costs on to the passengers.

MR LONG: As far as the government is concerned, I think it will be an airline cost. What we do with it will have to be a business decision on our part. Of course, we would like to recover it, therefore, we will have to pass it on.

MR CALLAGHAN: Inevitably, in this business our margins are so thin that we have little option but to pass these extra costs on, because they are considerable; they are on a per passenger pass through basis and whether you put an extra discreet charge on the ticket or whether you absorb it in fares, it's going to be passed on in some way.

MRS OWENS: And presumably all your competitors are having to do likewise, so it's not a competition issue.

MR CALLAGHAN: Yes, we don't stand alone on these things.

MR LONG: I think there's an issue there of scale. Whilst our competitors would have to it, their operations out of Australia is probably quite small, compared to Qantas' operations.

MRS OWENS: Coming back to this passenger movement charge, what we have recommended or we will be recommending in the final report is that all existing arrangements be reviewed over the next five years and I would presume in that review that these issues will get picked up and I think we are going to be also arguing in the final report that there be a consultation process undertaken in these reviews, so it will give you an opportunity to go and talk to somebody else about this, as well as us. All we can say is that probably if you apply our guidelines, you would not get this particular outcome.

MR LONG: Assuming the government takes the suggestion up, that would be welcome. Part of the complexity of the PMC is that it is administered by the Australian Customs Service, but it appears that the quantum of the PMC, and how it's constructed, comes from another department. Therefore, trying to pin down who's actually responsible for this is quite difficult.

MRS OWENS: It has become a form of a tax, really, hasn't it.

MR LONG: It's certainly a taxing legislation, but it's only a taxing legislation because it was the only way that the government could actually apply it.

PROF SLOAN: You are not paid a fee to collect the money?

MR LONG: We are not paid a fee to collect the money, no. We are paid an administrative cost to collect it and I must point out that this is a very unique charge. Every other tax that's levied in Australia is normally levied on people who are here at the time. This is actually levied on people who are coming here at some time in the future and over which, as an airline, we don't have a great of control over the travel agent who actually sells the ticket and therefore collects the charge. So the administrative aspects or weighting on us are quite heavy.

PROF SLOAN: Yes, I remember you told us last time too that there are some collection problems, but legally you are liable.

MR LONG: Well, we have an agreement with the Australian Customs Service under which we undertake to collect it on their behalf. The PMC legislation actually imposes the responsibility on the passenger to pay the tax. It could be said that we would be more than happy to give up the fee if the government would like to go back to collect it themselves.

MRS OWENS: But at least I think there was some degree of flexibility when you expressed your concerns about the implementation of this latest increase. There appears to have been some flexibility in terms of charging the arrangement.

MR LONG: Because it was a budget decision and with the normal sort of budget sensitivities it wasn't discussed with us as a charge prior to the decision actually being made. Therefore the pitfalls weren't readily apparent to government, though having said that, the last time they increased it we were actually given many months' notice within the budget which enabled us to avoid the shortfall issue that we've actually raised here. As far as the operations, that is what quarantine are going to do at the airports, that was discussed with us on very, very short notice prior to the budget coming down and we are still working through the very significant implications of what that's going to do to traffic through Australian airports with AQIS and with the Australian Customs Service.

PROF SLOAN: Yes, I would have thought that was more of a worry to you than the dollars really.

MR LONG: It's a combination - - -

MR BYSOUTH: The operational aspects are quite a worry because we're unsure of the outcome. With 100 per cent inspection - and people may have already experienced it now - with all of the bags being x-rayed after you've gone through the actual immigration part. Now, it's only if you have something to declare or you've fallen under some kind of watch, to be opened. The delays that can be expected will be proportional to the amount of extra facilities, extra staff, extra space which is put in there. So for the airlines there's either this cost, as mentioned in our opening statement which will be borne by accommodating the extra staff, a cost borne by the extra construction which will be needed to install the bays and the machines, which is not allocated to, and/or a cost in the actual physical delay of the passengers and the flow-on that will go - do they take their anger out on the airlines for delaying them; the poor customs official at the desk or the policy that has implemented it. We're unsure of those operational aspects at the moment.

MRS OWENS: I think I can guess which one.

PROF SLOAN: Probably all of them. What about CASA, I know you have quite an issue with the fuel levy and the view of Qantas and presumably the other larger

airlines that there are very significant cross-subsidies involved in that arrangement. I understand that CASA is actually currently reviewing these arrangements.

MR BYSOUTH: As it stands at the moment, the funding, as in our statement there, is coming through the fuel levy which is an over-collection. Qantas obviously supports the funding and the work of CASA, as we do, because you do have to work in aviation as a team overall. What's happened here, of course, is that there's a disproportionate amount of funding comes out of the levy on the fuel which in reality is paid by Qantas and Ansett as well as the main suppliers. There is a general community benefit from aviation safety overall and of course there is the direct industry benefit itself for all of industry, probably through easier administration, but the two airlines are paying a disproportionate part.

PROF SLOAN: What's the alternative to the levy though, because won't a levy always - I mean, it's always going to be a rough rule, isn't it?

MR BYSOUTH: There is the increased fee for service that many CASA inspection, certification regime - which could raise more money - it has administrative difficulties, overheads, and obviously political confrontation of not supporting light aircraft industry, raising the barriers to entry for people in the light aircraft, medium or charter type business, if they have to actually pay the actual costs for what it was for the inspection. So this is a cross-subsidy on the two major airlines.

PROF SLOAN: Although you don't want to provide false incentives for airlines to come into the industry who can't meet the true safety costs.

MR BYSOUTH: The low barriers to entry are being discussed separately in other areas. Did One Tel have enough cost to entry, that it got in too early, HIH charges and what else have you. But they're separate issues, totally outside of our - - -

MRS OWENS: Yes, you want to get the right signals to the different parts of the industry.

MR BYSOUTH: The right signals to go in. While the airlines are paying it, it is perhaps not sending the right signals.

MRS OWENS: Yes. I think when we first spoke to CASA and got their original submission - I think CASA is coming today, a bit later this morning, 10.15 - at that stage in their submission they were saying for the 2000-2001 financial year the service fees were about 2.5 million, which is only about 3 per cent of their overall revenue. I think they were talking about the potential to maybe change the balance, whereas the fuel excise made up 54 million which is about 60 per cent which is a very large chunk of that.

MR CALLAGHAN: Of which we are the majority payer.

MRS OWENS: But again you talked in your opening comments about - you said,

"We're concerned it does not seem to recognise" - this is the fuel levy, jet fuel levy - "does not recognise user pays as the guiding principle." But to the extent that the industry does have some responsibility, it does, and to the extent that the travelling public may benefit from having safe skies - I mean, some of that again potentially would get pushed through into the ticket price?

MR CALLAGHAN: Any extra charge will get pushed through into the ticket price in the end, yes.

MR BYSOUTH: All of the charges form the basis of our costs. There are two ways, I think David mentioned earlier. It's either buried, if I may use that vernacular, within the ticket price, or separately - say for example the noise levy - it can be put onto the ticket as a separate charge. Where a tax is involved, the parties agree and it is then installed via the IATA system as a charge in the construction of the fare.

MRS OWENS: But that idea was actually rejected back in - I think it was 1999, wasn't it - the idea of having it put directly onto the ticket. Does it make a building difference whether you pay it as a fuel levy or it goes onto the ticket? Are you suggesting actually the passengers would pay more if it went directly to the ticket than you could actually push back onto the passengers by just upping the charges?

MR CALLAGHAN: I think it probably works out about the same, but it's a matter of transparency.

MRS OWENS: Yes.

MR BYSOUTH: And time for the balance to be achieved.

MRS OWENS: Do you know why it was rejected at that stage?

MR CALLAGHAN: No, I don't.

MR BYSOUTH: No.

PROF SLOAN: It might have a slightly differential effect. I mean, it might be that the price of tickets for some of the smaller airlines would increase slightly more. If there are cross-subsidies in it, you presume that's what would happen. I suppose it depends on how they set the unit rate.

I mean, one of the things that we're concerned about is kind of agency efficiency and the link with governance arrangements and the like. On the face of it, bearing in mind that you don't necessarily want to believe all you read in the press, CASA seems to have had tremendous problems. Is there a kind of good interface between - well, let's say the airlines. I mean, they are users I suppose but there are kind of a whole lot of users in CASA in a way, aren't there - and you know, how their activities can be conducted efficiently and effectively. Is that a sort of productive loop at the moment?

MR BYSOUTH: They're all professionals I think, working at the floor level or the aircraft level. The actual people that are working in it are operators. I don't know that they're actually seeing any of these efficiencies in their day-to-day work that would lead to it. I don't know. David, do you know?

MR CALLAGHAN: None of us are flight operational experts who are here today.

PROF SLOAN: No.

MR CALLAGHAN: But you know, from my understanding the working relationship with CASA is extremely good and productive.

PROF SLOAN: But we have had examples - we had an example of the importers' relationship with AQIS and how over time that has proved to be a very productive relationship. In effect, AQIS costs have declined quite significantly because the industry has taken a very big interest and there seems to have been good interaction. It's hard to know whether the same story - we know the same story doesn't apply to many other agencies. We're not quite so sure it applies to CASA.

MR CALLAGHAN: I think in terms of CASA's relationship with the larger airlines it probably is true, but there has been I think a lot of concern out there about the smaller operators and I think that's where a lot of the extra CASA funding is going to be directed. But of course we are the larger payers so we see that as us subsidising those other areas of the industry and this is where the question comes down as to whether you have this wide industry perspective or whether or not it should be more directly funded by the people who are using the different services.

MRS OWENS: I think it's getting the right price signals into the right parts of the industry really, to promote efficiency and responsiveness. But I think my colleague wanted to ask a question.

DR STEWARDSON: When you were talking about the over-recovery under the passenger movement fee - over-recovery in relation to customs activity - were you talking about the situation prior to the recent increase and extra inspection because of foot and mouth?

MR CALLAGHAN: Yes.

DR STEWARDSON: Were you saying that you were unable to find out where that over-recovery money was going?

MR LONG: Well, we have no visibility, not transparency of the PMC. There was an initial ANAO audit of the PMC very soon after it was introduced, which identified that it was over-recovering $19 million per annum. Since then there has been a subsequent audit but the terms of reference of the audit didn't deal with what the recovery was versus the costs. It was only just recently, when the CEO of customs was asked the question, that we determined the quantum of the over-recovery. We always believed there was an over-recovery. We just didn't know how much it was.

There have been significant changes in what I would call CIQ - customs immigration quarantine - processing since the PMC was first introduced. Those changes have all gone towards greater efficiencies; that is, the movement of the issuing of visas for example, moving from missions offshore to airlines and travel agencies. Those efficiencies haven't been reflected in any reduction in the passenger movement charge. Therefore we knew that there were efficiencies being gained which weren't being reflected.

Add to that the fact that the minister for immigration decided that there would be a charge for the issuing of paper visas for passengers coming in, that obviously meant that elements of the PMC that were being collected for the issuing of visas were not going back to that department as part of their benefits. So we knew there was an over-recovery. We just didn't know the quantum of the over-recovery and this is the first time we've seen it. Whilst we have been saying for some time that we know there's an over-recovery, we just haven't been able to get anybody to say what it was.

DR STEWARDSON: You don't have to any formal mechanism of discussing this matter?

MR LONG: This comes back to the point I made earlier; that the PMC is administered by the Australian Customs Service, but the quantum of it is not decided by the ACS. Certainly they would probably be one of three broader agencies that would provide input into it, but I suggest that the decision on the quantum is either made by Finance or Treasury.

DR STEWARDSON: Thank you.

MRS OWENS: Coming back to CASA, what about CASA's cost recovery revenue? That's reasonably transparent, what they're doing to you? Do they talk to you about the fuel excise, or is that something that the decision is made elsewhere as well - or about their fees? Do they talk about the fees?

MR CALLAGHAN: I understand that is made elsewhere. I mean, we have an estimate of what the CASA charges should be on a direct return basis from Qantas and we believe we're paying a great deal more than that. Again that relates back to our previous discussion as to who should pay, and it is falling on us as the larger airlines.

MRS OWENS: Yes. I think all of these charges - and including the counter-terrorist first response funding - I think would get picked up at some stage in these reviews that I was talking about. One of the things we are trying to nut out a the moment is, how should the government prioritise the reviews, which ones come first, and we're having lots of people coming in and putting up their hands saying, "Well, we really think the therapeutic goods administration needs to be looked at early." You know, the charges that we are incurring are really unbearable and that that needs to be looked at. But we are trying to develop some criteria for

determining which ones should be the first ones off the - first cabs off the rank. I don't know if you've got any suggestions.

MR CALLAGHAN: I don't think these things are particularly critical to our future. They are important to us in terms of our overall costs and the fact that we are very low-margin business. But we're happy to be on the queue as you see fit, but so long as we are on it and it is part of the consideration of the commission, we're thankful.

MRS OWENS: Good.

MR BYSOUTH: My learned colleague probably doesn't have a budget as directly as I do. I think that the draft decision that you've come down with and the principles that it espouse could be applied right across the departments. The areas that we've listed here, in this opening statement, and we put forward before, have a number of issues where the airlines are paying a disproportionate part of a whole series of issues. We've mentioned there, and it's now been reported and came in the budget, the cross subsidies and the over collections. If the principles were there that there was visibility and reporting before parliament, of the costs and where it came from, overall, for all of these issues, then they would flow through in time.

The other is to implement fully the government's user pays principles. Some examples, one that we've mentioned there and, commissioner, you did raise, on the counter terrorist first response. As well as the airlines, there is also the shops, the other industries, the general people that work at the airport which now the government has directed, will be now what's called "duel till" - that's separate collection agent. They are getting free security protection from having those people there every minute of the day. They're not paying for it. The airlines are paying for it and professor Fels has been directed in the ACCC that he's not allowed to take these issues into account.

MRS OWENS: What about our other inquiry into airports. Is this an issue you've raised in the context of the other productivity commission.

MR BYSOUTH: It is one of the issues to be raised, on the charging, and was raised in Melbourne, that security has been provided separately for these other organisations, but it is the airlines that are paying. The next would be, the check bag screening. And Qantas and Ansett and the rest of the airlines, through the board of airline representatives, endorsed the security principles that are involved, but what will happen is the goods that are to be sold in the airport also go through a screening process. That is not paid for by those sellers. That is paid for by the airlines and indirectly though the airline passengers, through the collection of the fees. The same with the fuel level, so overall principles of visibility, overall principles of reporting to parliament and an extension of the user pays principles.

Some issues cannot be directly apportioned and there's an understanding for that. One, obviously would be with the increased charges related to foot and mouth. Whilst it would be the rural industry which is directly affected, it would be the

Australian economy and the Australian society, and the social dislocation that we've just seen in the rural areas of the United Kingdom would be enormous if it ever happened within Australia. It shouldn't just be the airline passenger or indirectly through the airlines that are just paying for that part. I think that is our clear message - clear support to the government on all of the issues - but let's take the principles of users pays and open governments to its end.

MRS OWENS: I think that was a very good way to finish this discussion. I'm afraid we're going to have to move on but I think you've made your point very well and I'm actually very pleased that you did come and we'll be talking, as I said, to CASA fairly soon, so you're welcome to stay around if you've got time. Otherwise there's more tea and coffee out there. So thank you, we'll just break for a few minutes.

MR BYSOUTH: Thank you very much.

MR CALLAGHAN: Thank you.

MRS OWENS: The next participant this morning is the Australian Food and Grocery Council. Welcome once again to our hearing and could you please give your name and your position at the council for the transcript.

DR ANNISON: Yes, my name is Dr Geoffrey Annison and I am the scientific and technical director of the Australian Food and Grocery Council.

MRS OWENS: Thank you. I understand you have got an opening statement you would like to make.

DR ANNISON: Yes, I have and first of all of course I would like to thank the commission very much for the opportunity to speak to you again. Actually, I was quite interested to listen to the previous presentation, particularly with regard to the issue of foot and mouth disease. That is an issue that we've had at least a watching brief on although fortunately no direct experience with at the moment, although we were affected by the government's import bans that were brought in in terms of some ingredients from Europe but I was fascinated by the discussion of the extra quarantine requirements being paid for out of levies on airline tickets.

However, I would just like to remind you, if it's okay, of what the Food and Grocery Council is. We are the peak body representing Australia's processed food and beverage and other grocery product manufacturers. It is our role to develop policies and strategies for the industry conducive to strong growth, sustained investment for greater competitiveness and profitability. Our membership at the moment comprises approximately 85 companies and subsidiaries and associates and that constitutes in the order of 80 to 85 per cent of the dollar value of the industry.

The industry is in fact Australia's largest manufacturing industry. It employs one in five of the manufacturing workforce and is characterised by not only having a strong domestic market but of course rapid growth in export markets. The Australian Food and Grocery Council is committed to effective regulation for Australia's food and grocery manufacturers. In terms of this inquiry I'm sure you're aware that we've made a second submission to the Productivity Commission's inquiry into cost recovery and of course we request that the policy positions presented in that previous submission are respected.

The second submission was of course made in response to the draft report and we congratulate the commission on that draft report. It was extremely comprehensive and covered many of the issues that we had raised in our own submissions and I'm sure were raised in many other submissions. I think it demonstrated that there is an absolute requirement for a credible and cost recovery policy and implementation framework. Cost recovery must contribute to the efficient, effective and equitable resource allocation both of public institutions and also the private sector but also cost recovery must be tempered by the necessity to protect public confidence in our institutions and the agencies of government must always have demonstrated independence, credibility and integrity and of course value must be protected.

I think the report has highlighted that the current arrangements are very inadequate. We concur with the major findings of the report that there is no current clear government policy on cost recovery and there's certainly a lack of transparency and accountability in the cost recovery arrangements or at least some of the cost recovery arrangements which currently exist. The report documented that market failure as a basis for government intervention is relevant in the cost recovery debate and of course this is relevant to the food industry. It's our consideration that food regulation fits best under the definition of public good and that public good of course being safe food. We don't think safe food can be construed as a negative externality or spillover. It needs to be constrained by government regulation and we concur strongly with the commission's observation that imposing cost recovery on top of inappropriate or inefficient governmental services will only compound their distortionary impact.

Perhaps the thing we welcomed most in the draft report was the guidelines that the commission has presented for cost recovery and we consider that those guidelines really are an imperative. As you know from our previous submission, we spent some time negotiating the Australia New Zealand Food Authority amendment bill of 1999 and those negotiations highlighted the need for a rigorous and systematic approach to cost recovery for regulatory agencies. In the draft report it stated that before cost recovery is imposed it should be considered whether or not the benefits of the activity are captured directly by the individual or firm charged or by the firm's customers and this is a critical issue and this really goes to the heart of whether the imposition of regulation bestows a particular benefit and to whom it was bestowed and whether that benefit was an exclusive capturable commercial benefit. We believe that the guidelines provide a path for determining exclusive capturable commercial benefit.

The guidelines are split up into several sections and I would just like to make some comments upon that, then I'll come back indeed to the concept of exclusive capturable commercial benefit. The guidelines - a discussion notes that there is a clear need for a robust and justified policy framework that must accompany the imposition of cost recovery. As I'm sure you're all aware, under the ANZFA Act the purpose of food standards or at least the objectives of foot standards are to protect public health and safety, prevent fraud and deception and to ensure the provision of adequate information for informed choice. Of course the food industry and the AFGC strongly supports these objectives.

However, it is our experience and our consideration that recently the food standards code has had amendments which perhaps regulated the industry in an overzealous manner in relation to those objectives, marginally reflecting those objectives and in some cases we would argue deviating significantly from those objectives. Indeed, the draft report states that if standards set for a particular product are too onerous and therefore higher than necessary to provide acceptable levels of consumer safety the firm's compliance costs will be higher than necessary. At the moment the food industry is experiencing a fundamental shift in the regulatory approaches and this threatens costly case by case approvals for novel products and novel processes and novel claims and particularly health claims.

We've already witnessed in Australia products and processes which have been on the market in Australia which have regulatory approval overseas and which have no demonstrated adverse effects currently being forced through regulatory approval systems and at least in one case has been an attempt by ANZFA to seek through recovery of costs, justified on the bases of exclusive capturable commercial benefit although we consider the criterion for that justification was dubious to say the least and it's our understanding that that charge hasn't been agreed to by the parties making the application. To impose cost recovery on an already costly regulatory system imposes more burden on the food industry and it's inconsistent with government policies, that's successive Australian government policies, for minimum effective regulation and it will ultimately undermine the competitiveness of the food industry.

The draft report states that the objective of the review is to ensure that cost recovery charges are based on efficient levels of regulation. Of course the corollary to this critical point is that cost recovery becomes particularly noxious when standards or regulations are not efficient or set efficiently and we particularly welcome the commission's approach in suggesting that these issues can be resolved by the preparation of adequate regulatory impact statements and of course the cost recovery impact statements which have been proposed in the draft report. We strongly support the concept of cost recovery impact statements where it will be required to demonstrate the net benefit to the community results from the cost recovery which is being considered by the regulatory agency or indeed the other agencies that might be considering it.

Moving on to determining who should pay we note that the draft report addresses the who should pay issue by differentiating between beneficiary pays and the regulator pays approaches, the former based on I guess public good and the latter is based particularly on containing negative spillovers. I've already said that food regulations are to protect public health and cannot be considered to be a containing of negative spillovers and we believe that in regard to food regulations the policy objective is detailed in table 9.1 of the report which is to enforce safety and quality standards to protect consumers. We would say however that in the area of food regulation quality standards are best left to the market and to the Trade Practices Act. There is little role for this in food regulations. Certainly it's not recognised in ANZFA objectives.

Consumers are the beneficiaries of food regulation under the frameworks that have been proposed and indeed in Australia consumers cannot practically opt out of consuming safe and regulated food. This is an important point that is not actually reflected in the draft report. We consider therefore that the benefits from the food regulations are very diffuse across the community. Everybody, every individual in the community benefits, and we consider therefore that levies directly on the industry are probably inefficient and inappropriate and they would almost certainly be passed on to the wider community and consumers in general. We consider that direct funding of the regulatory agency from taxation is therefore likely to be more practical and efficient.

We have concerns in the way levies may be implemented as well which could raise significant inequities. For example, the shortcomings of a single company or a small number of food companies, perhaps not producing food in the manner that is required by the regulation or a safe food, would lead to a perception in the community that regulations are indeed not rigorous enough and would force greater prescriptiveness into regulations requiring higher levies to be imposed on certain food companies. This would in fact penalise the vast majority of the industry for the inefficiencies and the ineffectiveness of a small minority.

We think there are issues of applying levies to food companies which are manufacturing in Australia. It is difficult to see how they could apply to food companies manufacturing overseas in an equitable way and this potentially undermines the competitiveness of our food companies which are competing in global markets both in Australia and overseas. Attempting to impose levies on imported products, to address that inequality may ultimately be viewed as a tariff barrier or an unjustified technical barrier to trade, depending on exactly how those levies were imposed and that of course can have implications on Australia's World Trade Organisation obligations. We consider that although the draft report has addressed these issues, before levies can be proposed there's a mechanism that is appropriate for the food industry. Much greater consideration of the World Trade Organisation implications have to be made.

With regard to pre-market regulatory activities, as we've stated several times, we have been a strong proponent for the concept of exclusive commercial capturable benefit and indeed in figure 9.3 on page 211 of the draft report a path for determining exclusive capturable commercial benefit in the guidelines is a useful one but we feel that the text fails to adequately capture the essence of the exclusive capturable commercial benefit as applied to food standards, in the food standard setting. It's our belief that firms enjoy commercial exclusivity to a product or a process through patent ownership or by holding secret intellectual property. ANZFA's role, however, in pre-market approval of goods or processes, is to assess whether those products are safe and whether the processes are safe and if those products are safe and the processes are safe and they provide approval for them and if those products and processes are exclusive to parties that might be seeking amendment to the Food Standards Code to allow those approvals, then ANZFA may impose charges on the basis of that exclusive capturable commercial benefit. It is important to realise however that this does not preclude other companies using the assessments and approvals provided by ANZFA if they can overcome the exclusivity provided by intellectual property ownership or by maintaining the trade secrets and intellectual property secrets.

In other words, ANZFA does not provide a licence to companies of products and processes which inhibits other companies from using the products or processes and this is critical and we don't believe it is captured fully in the report and yet has been used for the basis of ANZFA's charging. As regard to post-market and other regulatory activities in the area of food regulation there are three major post-market activities. Monitoring and surveillance is the first and this really is just a function carried out by ANZFA and it is a way of ensuring that ANZFA is allocating its

resources appropriately in the context of broader public health policy and ANZFA as you realise is in the health portfolio. We don't believe it's appropriate that cost recovery should be applied to this function because again the broader community is the beneficiary of this and it's diffused across that community.

Product recall has been mentioned in the draft report but in fact this is not a resource intensive activity. ANZFA coordinates product recall of the states and territories but it's the states and territories who enforce them. There may be significant resources - expenditure associated with product recall but these are usually by the industries or the companies that have been asked to recall the products as they're the ones that need to trace the products and determine exactly where they are in the distribution chain and how they have penetrated into the retail sector and then into the houses of its consumers.

There is an area though, the third area, where cost recovery is appropriate, and that is in the auditing and compliance of food safety standards. We're at the commencement or a new era if you like of food safety standards in Australia. Whereas previously there were prescriptive standards and the absolute requirement that food had to be safe it was for sale, ANZFA has spent the last seven or eight years developing food safety standards. These are now gazetted and they're being implemented at the state and territory level.

A fundamental requirement of those food safety standards is that companies have a food safety program which will be audited either by government agencies or by third party auditors, and there will be a fee for service associated with that auditing. Clearly the beneficiaries of the auditing services are the companies, but also the direct consumers of their products. We consider that auditing in this case and the costs associated with it can be equitably absorbed by the company and distributed between the company and the customer or indeed passed on in full to the customer. In that regard we consider that cost recovery arrangements for post-market activities be restricted to activities where the beneficiaries are clearly identifiable.

In terms of implementing cost recovery as opposed to regulatory arrangements, of course it is important to design arrangements which are equitable, efficient and effective, reflecting the real and reasonable costs of the regulatory agencies. They should provide overall benefit to the community and of course should be non-distorting on the market. The draft report states that, "Often it will be necessary to use a proxy for costs that are attributable to a particular firm in the industry." From the examples provided, though, we cannot support the proxies as suggested. They are certainly not applicable to the food industry regulation or applications to amend the food standards code.

Quite simply, cost recovery should not be varied on the basis of the riskiness of sectors of the food industry. All food should be safe and of low risk. Indeed, it is a fundamental maximum in food production that we have used over and again in discussing the issues of the riskiness of particular sections of the food industry that all food can be produced safely and, by the same token, all food can become

dangerous if mishandled. So it is inappropriate to suggest that estimating the risk associated with food operations might be used as a basis for cost recovery.

We are also opposed to imposition of higher charges on bigger companies. We just cannot see that this is justifiable on any equitable basis if the costs incurred by the regulatory agency are the same. We also consider that it is simplistic in the extreme to relate complexity of applicant in food standards and the workload of the regulatory agency with the size of the application using a measure such as the number of pages, as suggested in the draft report. We would oppose that that would be used as any basis for cost recovery.

In terms of ongoing monitoring, of course all government agencies should monitor their activities to ensure that they're operating effectively. Cost recovery will require close monitoring, but this indeed will add an extra element of complexity which ultimately might undermine the efficiency of the cost recovery arrangements. We consider that the regulatory impact statements and the proposed cost recovery impact statements can be used as a framework for the periodic review of cost recovery policies and implementation by regulatory agencies. In other words, if you're using regulatory impact statements in cost recovery to determine initially whether cost recovery is appropriate and it's appropriate to introduce it, then perhaps the same framework can be used as part of a review mechanism.

In our submission we address the other information requests, where we believe we could, that were made by the Productivity Commission, and we've been reasonably comprehensive in addressing those requests. We've provided in-principle support for the cost recovery impact statements as an adjunct to regulatory impact statements. However, that is an in-principle support. We consider that a lot of work will have to be done to determine exactly how cost recovery impact statements are developed and the criteria for doing that, but I'm sure the commission is well aware of that, and of course we would welcome the opportunity to play a role in that.

But one thing that has occurred to us - and that is reflected in our submission - is that further information was asked for about parliamentary scrutiny and the role of efficiency audit committees and the impacts on innovation, and we've provided comments on that. But one of the comments we did make is that the cost recovery impact statements and the regulatory impact statements, if pursued vigorously in setting up the arrangements, do provide a mechanism for minimising the degree of parliamentary scrutiny that is required for defining the role of efficiency audit committees but also to determine the impacts on innovation.

That will be one of the key considerations, one would hope, of cost recovery impact statements and regulatory impact statements. It really goes to the heart of the issue, which is that there is an imperative for a structured and deliberate approach for cost recovery within well-defined policy principles and according to clear decision-making frameworks, and it is the regulatory impact statements, using cost recovery impact statements as an adjunct, that will provide that clear decision-making framework and ultimately provide the justification that is required by government to impose cost recovery against each of the activities that it might

consider. That's the end of my closing statement, and of course we stand ready to provide further input to the Productivity Commission's inquiry into cost recovery after this time, should it be sought. So thank you very much.

MRS OWENS: Thank you very much for a very thorough submission and opening statement, Dr Annison. You've covered a lot of things in both, and I think very clearly. I think we're reassured that you think that the guidelines do provide a useful approach and that the cost recovery impact statement approach is a reasonable way to go, and I think you've also commented in your submission that you believe that there needs to be consultation arrangements with stakeholders. You've put it in the context of monitoring. I think in terms of just setting up the systems in the first place that consultation is also necessary, so we'll be putting greater emphasis on that in our final report. I also thought that your comments about applying exclusive capturable commercial benefit were useful for us as well. You've just taken it to that next degree of refinement for us. I'd like to thank you for that.

One issue in the context of food regulation, as you've noted, is this issue of who were the beneficiaries. You've made I think a pretty strong argument saying to the extent that consumers benefit, consumers really are the public, they are the community, so why have charging arrangements, why not just go down the track of funding through appropriation? I think that's probably where we would come out as well. If you applied our guidelines, it does make sense. You do set out in your submission I think on page 8 the objectives of the ANZFA Act, and when we are looking at whether you go through a beneficiary pays or a regulated pays approach, we say: what are the overarching objects of the legislation? As you've noted, they're to protect the public health and safety, which is protecting the Australian community, so under that objective it really is a community benefit, so taxation - it's funded through appropriate.

Prevent fraud and deception: I couldn't quite work out where that one fits. But the ensuring provision of adequate information for informed choice is again something where the consumer directly benefits, but then the consumer is everybody. So I think that works reasonably well in the context if we were following through our guidelines. So it does raise this question that you raise as to whether levies would be another way to go, and you've obviously got quite strong objections to having levies.

DR ANNISON: Yes.

MRS OWENS: I don't know whether my colleagues have a different view, as to whether levies would be appropriate in some circumstances, or not.

PROF SLOAN: I suppose the point is - and I think you were here for the Qantas submission - that they're a fairly blunt instrument, levies, which almost certainly give rise to cross-subsidies from the larger firms to the smaller firms. I just wanted to take issue with you in the sense that I think our idea that the cost recovery practice of rating according to riskiness was not some kind of veiled attempt to over-recover costs from large firms. In fact, I think the view would be that riskiness would be related to the cost-intensiveness of the regulatory process, and I think you have a

recommendation somewhere which we would agree with - on page 14 - that:

> the charges imposed under cost recovery arrangements reflect as accurately as possible the real resource requirements of the regulatory agency in undertaking the particular regulatory activity.

I think we would absolutely agree with that. I mean, that's really what we're saying: that cost recovery should be on an activity basis. I think, dare I say it, you might have overreacted to some small sentence there.

MRS OWENS: But I feel in the context of that recommendation you've made, which I also agree with, that the real resource requirements will reflect the degree of riskiness.

PROF SLOAN: Is that where you're differing from us?

DR ANNISON: I think it's possible that we may have overreacted, but I think perhaps it's because the term "riskiness" actually did press an old wound with us. In terms of the development of food safety standards, one of the key issues which has been addressed is, once the standards were gazetted, the roll-out of their implementation. Now, it's one thing to bring in regulations like the food safety standards and to require that companies have food safety programs and that they should be audited, but there was a real question on whether indeed the resources to audit all the food companies at the same time to accompany the beginning of the food safety standards existed in Australia. In fact, with possibly well over 70,000 businesses that would have to be audited and it being estimated that there were only 100 trained auditors in Australia, you could see that, unless the implementation was carried out in a very orderly manner, it was going to create havoc in the food industry. So the concept developed that food companies would be based and audited on their riskiness to public health and safety.

Notwithstanding the fact that we agreed that there was a real imperative to sort out the resourcing and to roll out the implementation smoothly, we presented numerous submissions and it is still our view that in fact you cannot audit people, companies, on the basis of riskiness, because there are - - -

PROF SLOAN: Because you've got no means of making some ex ante assessment of that? Is that - - -

DR ANNISON: That's right. The measures of riskiness have been brought in. For example, they have said that the size of business is a factor in the riskiness, and the reason for that is if you're a big business you can potentially poison 10,000 people as opposed to a small company that might only poison 100 people.

PROF SLOAN: Or kill them.

DR ANNISON: Well, poison and kill. But in fact the public health and safety data from food poisoning incidents indicates that in fact small businesses, particularly

corner shops - not corner shops but restaurants and that type of thing - tend to poison a lot more people than the big manufacturers. So in attempting to get some estimate of the riskiness of the food business, in fact it highlighted to us that it was just an inappropriate approach. So I think perhaps that when we saw those terms in the draft report it was a bit like a red rag to a bull. So if we have overreacted, then I apologise for that.

PROF SLOAN: I don't know where - we have to think about our drafting, but - - -

MRS OWENS: We were making really a link between riskiness and the possibly intensity of the activities of the regulator: the higher the degree of risk, the more intense the activities, hence the higher the cost, so the cost would reflect riskiness in some direct way. One of the other issues that has been raised by others is that cost recovery where it does exist can provide a useful means by which industry can then focus back on the activities of the regulator and ensure - keep them honest, if you like - that they are operating efficiently and so on. What you don't really have for ANZFA is that same sort of degree of interest in the activities of the regulators if the regulators are not paying, or is that not the case?

DR ANNISON: We would say that that is probably not the case, at least if it says "an issue" it's been addressed by other amendments that came in with the ANZFA bill of 1999 and now in the ANZFA Act. For example, ANZFA now is required to develop a work program and it must do that in consultation with its stakeholders and against a criteria. So the activities of ANZFA are monitored by the stakeholders, including the food industry, and we do have an opportunity to provide input into that.

MRS OWENS: That is really a sort of an overstated argument that cost recovery means that industry does take a greater interest because their dollars are at stake?

DR ANNISON: Well, it may be more the case for other industries than it is the food industry but we have at the moment the Australian Food and Grocery Council which very closely monitors ANZFA's activities and holds them accountable for being able to justify those activities. We really require them to justify them against regulatory impact statements and perhaps it has occurred to me that one thing we didn't say in the last submission that is perhaps worth noting is that the current ANZFA amendment bill - there's yet another ANZFA amendment bill going through parliament at the moment, ANZFA amendment bill 2001 - will require for the first time, it is my understanding, there's an amendment that will mandate ANZFA carrying out a regulatory impact statement.

I think this is particularly important because even though there has been an argument by the Council of Australian Governments for a number of years, and it's been government policy that regulatory impact statements be carried out, if you look at the reports into the ministerial councils and their activities and the development of regulatory impact statements, government agencies are still operating well below par in this area. So whereas we support very strongly the concept of regulatory impact statements - and indeed there's been at least one occasion in the last 12 months where we have forced ANZFA into carrying out a more comprehensive regulatory impact

statement than there might otherwise have done - off the back of concerns raised by the Office of Regulation Review, we would say that bringing in the cost recovery impact statement, as the Productivity Commission has suggested, is something we support very strongly.

But it's absolutely critical that there's a very strong commitment by government that those cost recovery impact statements will be prepared and will be adhered to, because certainly I think it's no exaggeration to state that in the case of the regulatory impact statements they're still not being implemented with the diligence that they should be.

MRS OWENS: With this concept of exclusive capturable commercial benefit, how subjective is that as a notion when ANZFA is trying to administer that, trying to interpret that. You mentioned that one instance recently where they had tried to impose charges based on that criteria. Is there a degree of fluidity about how you interpret that?

DR ANNISON: Well, we don't think there is. We think when we negotiated with ANZFA what it actually meant - and we also had discussions with the government and in fact both sides of parliament; it was important that they were involved in those consultations in order to get the amendments through of course - we thought we had a very clear idea of what exclusive capturable commercial benefit was and what it meant. We are concerned that since then ANZFA's interpretation of it has - not so much their interpretation but the way they have attempted to implement it has led to some flexibility in its interpretation. Indeed, this is why we're particularly welcoming of the guidelines that you're proposing because we see that as a less flexible and a more determined path to determining exclusive capturable commercial benefit.

DR STEWARDSON: How do you know about exclusive capturable commercial benefit in advance and indeed even how does our figure 9.3 help it - I'm glad you think it does. But I'm not clear about how it does because, as I understand what you're saying, if there isn't a patent which isn't applying in most cases, it's a matter of whether the competitors can deconstruct the product and guess what its composition is and then reproduce it. So I don't see how ANZFA or your or anybody else know in advance whether there is going to be an exclusive capturable commercial benefit because doesn't it depend on what the competitors do once the thing is approved on the market?

DR ANNISON: The food industry is interesting compared with other industries and perhaps our sister industry, the pharmaceutical industry, if you like, in that the foods are very poorly defined and are very difficult to reverse engineer, unlike drugs where the chemical composition of the drugs and the manufacturing process is very well defined and is extremely easy for companies to strike off generics, as you know. That's why they have the patenting system. If you have a particular blend of ingredients in a food product and the physical nature of the ingredients and the subsequent blend which is important for taste and for flavour and for mouth feel and for cooking properties and so on, if those have been engineered in a secret way, it is

extremely difficult to reverse engineer that.

It's not impossible to do it - and companies may indeed be able to do it - but if there is something that provides a unique attribute to that product that is held private by the company and it is clear from the application that - for an amendment to the Food Standards Code, and it might be the use of a novel process, for example, then the exclusive capturable commercial benefit becomes clear. It might be that there is something that is held in terms of intellectual property by the company and indeed we would see that that would be the majority of the situation but it might, for example, be a particular strain of bacterium which ferments a yoghurt in a particular way to give a particular range of short chain fatty acids which then have a particular health benefit. Now, if the company has the proprietary intellectual property over the bacterium that's doing the fermentation then that product is protected.

However, if another company works out a different way to put the short chain fatty acids into the products which are the actual agents that produce the beneficial effect and they might do that by using another organism or by just introducing them by a chemical means, then it's appropriate for food standards to prevent them marketing those products and making the claim about those products because they have already provided the permission to another company. So in other words, once a company can remove the exclusivity of that commercial benefit by some other means, either by overcoming the patent or by developing an alternative technology to the same end result, then we don't see it's appropriate for ANZFA to in fact restrict the introduction of that product to the market because then you do in fact have a licensing system.

DR STEWARDSON: That's what I don't understand; when the first product is tested, how you know whether the competitor is going to produce this other bacteria or whatever it was in your example.

DR ANNISON: We see that more of a risk of the company. If the companies in the food industry routinely in fact hold secret information about their products and often their success in the commercial environment is not predicated in fact in holding those products secret for an extended period of time but just to get a rapid entry, the first entry into the market. If they're given a lead time of 12 to 18 months that's often enough to establish a substantial market position which they can then defend. They would be happy, if you like, with the exclusive capturable commercial benefit and paying the fees in order just to secure that lead time.

DR STEWARDSON: So in most cases it would be appropriate to say there is an exclusive capturable commercial benefit to be charged.

DR ANNISON: Yes, unless it's absolutely clear that there isn't. For exclusive, if a company developed a particularly efficient way of extracting a dietary fibre from wheat and put it into their products and then wanted to make a health claim associated with that dietary fibre from wheat, there are a lot of other products on the market anyway that contain dietary fibre from wheat, and assuming they have got the same level and active level of the dietary fibre, it would inappropriate to then charge

the company for an application for a health claim, for example, because clearly it's exclusive, even though they might actually have a unique way of pulling dietary fibre out of wheat.

MRS OWENS: It's really a matter of where the onus lies. I mean, the incentive is on the company to say, "This isn't exclusive," so they don't have to pay the charge, isn't it?

DR ANNISON: You could say that but you could also say the onus is on ANZFA to demonstrate that it's exclusive and that's where we think the guidelines are actually useful because they're finding a framework that leads - or at least helping to lead - to the definition of exclusive capturable commercial benefit.

DR STEWARDSON: That figure 9.3 that you mentioned with approval, the first question is, will other firms be able to free ride on the approval of the first applicant? I take it that your answer to my questions is that in most cases the answer to that is, "No, they won't be able to free ride," and therefore you go down one particular half of that diagram, correct?

DR ANNISON: Well, if the answer is no, then that goes down to leading to a definition or the exclusive capturable commercial benefit, yes. In some areas that will certainly be the case that most cases you will not be able to free ride, for example, applications for food additives which are highly defined and often protected by patents and certainly by trade secrets in terms of their manufacture. But in other areas there may be a free rider which is clearly identifiable.

MRS OWENS: Thank you very much for that. As I said at the outset it was a thorough submission and we will take your expansion and your comments on board when we're finalising our report, so thanks for coming again.

DR ANNISON: Thank you very much.

MRS OWENS: We'll break for a minute.

MRS OWENS: The next participant is the Civil Aviation and Safety Authority. Thank you for coming and I'm sorry about the slight delay. Could you each give your name and your position with CASA for the transcript.

MR COMER: Ray Comer, Executive Manager Corporate Services.

MR ELDER: Rob Elder, Executive Manager Government Industry and International Relations.

MS BICKFORD: Sue-Ellen Bickford, Executive Manager Strategy and Development.

MR SHEEHAN: Walter Sheehan, General Manager Finance.

MRS OWENS: Thank you, and we have got some discussion points, but I understand, Mr Comer, that you would like to make an opening statement.

MR COMER: Thank you. I think the point that we wanted to come to you today on was to talk about the framework of the guidelines and where CASA sits in relation to that. Perhaps some of the opening comments would go to things like the fact that we are concerned that if we have a safety function which is mandated, and we charge a fee for a safety function and leaves the applicant a choice as to whether they do it or not, we have some concern that those imperatives have to be taken into consideration. So that importance of safety considerations shouldn't be overridden by economic factors. We had some concern in the generality of the guidelines that it is an attempt to establish a one size fits all and I think in an aviation regulatory environment that is a difficult task. We found that the guidelines are certainly helpful, but we do have some concerns with them which we will address with you during the course of the day.

We - as we put in our submission to you previously - believe that there are some activities of CASA's which shouldn't be the subject of fee recovery and that - I mean, in terms of the direct beneficiary fee recovery - and that has been borne out by a number of previous studies and we gave you quite a lot of detail on that previously. Our role, as CASA, is not to determine the policy that applies to fee regulation or fee recovery. Our role is primarily to provide advice to government. As we mentioned to you previously, CASA is embarking upon the rewrite of all its regulations. We have existing fees regulations which are now dated. We accept that they don't represent current pricing and that they do not extend to a full range of services that perhaps they might. The issue for us is now one of considering the new regulatory environment, looking at the services that will apply in that new regulatory environment and then providing advice to government as to the cost recovery aspects of that new environment.

We also mentioned to you previously - and I think it's worth just noting - that we have established a service centre in Brisbane. The primary role of that service centre is to coordinate out of one point of entry all of our regulatory services. They are progressively dealing with industry to try and establish delivery 'criteria', if you

like, so that there is an element of us accepting that before we start to extend the range of our fees, we must be able to do that in a very economically efficient way, that is, there must be a delivery timetable that we agree with industry so we can go to them and say, "Here's a range of services; here's a possible range of fees," and through a consultation process to negotiate that through.

The next step in that process, of course, is the RIS process, which is referred to in your guidelines. One of the points we have concern about in relation to setting up a secondary process for that with CRIS, if that's the acronym, is that that, to us, would not be a good move because it breaks the process of evaluation. The RIS process is primarily there to look at a regulation; its impact; its economic benefit, all that sort of thing. We believe that you cannot separate out cost benefit aspects of that into a separate process which is potentially a separate agency. So we would have some concern that that would be a separate function through a separate agency. We accept that transparency of costs in revenue is a big issue for the industry.

We are aware that Qantas met with you earlier this morning and that they have raised a number of points about cross-subsidisation or inequitable apportionment of revenue. CASA has had regard to this in the past, but I think my comment to you today would be that additional study needs to be put into the issue of cross-subsidisation. The airlines recover revenue for the travelling public as well as the industry and I think that is a point that is sometimes forgotten, that of the revenue that they collect, there is a very significant proportion of that which, under the beneficiary model, is attributed to the travelling public as opposed to the industry and we would take the opportunity to just confirm that point on the record.

So the points for us, I think, as we went through the guidelines, if we just briefly go through those. In relation to 3.1, we don't have a difficulty with that. I think any legislation has to make it clear that what the basis of the chargings are. Similarly, in relation to 3.2 we do that at the present time in our statements. It is transparent in the sense that it is possible to determine what is the cost recovery percentages and they have been reflected in the table that you have got in your draft report. As we indicated previously, we accept the role of the RIS and we also accept that it is hard for us to go through a full consultation process with industry, but we do that and we accept that we must make our revenues and costs more transparent. A step in that direction was taken in the last six months or so when CASA established an aviation safety forum. This is a forum of industry representatives who provide advice to our board and they meet on a quarterly basis and one of the items in their charter, indeed, is to look at budgets and costs' issues. So that is a forum which CASA will progressively use in relation to things like fee recoveries.

Items 4.1 to 6.4 in your report in the recommendations, we believe are matters for government to decide. There is a section in there dealing with information agencies that we don't have any comment in relation to. With recommendation 6.8, CASA regards the fuel excise as a cost-effective means of recovery which effectively covers the full spectrum of aviation users. We accept that there are some anomalies in that process at the present time and these need to be dealt with. There have been other options considered by government in the past because of the concern expressed

by major industry operators, and that is things like ticket tax and aircraft registration. Indeed, if you look at the most recent change in the level of excise, the government indicated that those factors had been taken into account when they decided to increase the excise last time round, but by point of clarification I should say that the government subsequently then decided to remove the CPI indexation factor from the excise calculations.

In relation to 6.8, I had a query which we might raise with you in relation to the difference between regulated firms and the beneficiary. We found those terms a little bit confusing in the context of that recommendation. The recommendation indicates that:

> Where the objective of the regulation is to provide benefits to the users of regulated products, a beneficiary pays approach should be considered or adopted. Under this approach, regulated firms would be charged for the cost of regulation only where -

and there's a set of criteria there. Is the words "beneficiary pays" and "regulated firms" being used synonymously in that context?

MRS OWENS: Well, we're basically saying if you use "beneficiary pays" - we are looking at it from two different directions. Beneficiary pays - we are thinking about the regulations benefiting particular groups, either the firms; the users, which is the travelling public; or the community, more generally, by having safe skies. The "regulated firms" approach is saying, "Is the main objective of the regulation, or having the regulated body, to reduce what we've called - because we're economists - negative spillovers," and if there was some concern that the existence of that activity was causing negative spillovers, then you would go and say the regulated firm would pay in that case because they are causing problems - negative externalities. In the case of CASA, I think it would probably go the other - it's about the primary objectives of the legislation and in the case of CASA, the primary objective is probably to - I don't know, I haven't got the words in front of me, but to have safe skies and so on. So there are beneficiaries which include the community, generally, because we don't want planes dropping out of the air, and includes the travelling public and it also includes the airlines.

I think the fact that you've got a fuel excise is probably an efficient way of possibly collecting from firms who benefit, and also the travelling public to the extent that some of that money, through the fuel excise, goes into the ticket price, eventually, to the extent it's passed on. So in your case I wouldn't be worrying too much about the regulated firms approach under recommendation 6.9, I think I'd probably be focusing more on the other. But it's just a different way of looking at the objectives of the legislation.

MR COMER: That's right, and that's where I think it highlights some of the difficulty in having guidelines as broadly expressed as they are because you have that interpretation issue about things like negative spillovers, regulated firms, because you well mount an argument that negative spillovers do apply in aviation.

MRS OWENS: Yes, you could, and it's just a matter of what is the main reason for having the regulation and what's the object of the legislation. There are some other areas where negative spillovers - it is a predominant issue unequivocally to the extent that companies may be polluting the environment. You may say, well, we're going to charge the companies for polluting the environment. You're not necessarily going to charge people at the other end from benefiting from the firms polluting the - or reducing their pollution - you are going to charge the firm for doing it. So there are some areas where it's very - you know, it's reasonably simply to sort out. In other areas, it will be less so. It's a bit of a grey area and we really have been struggling with this one ourselves, in the early stages of the inquiry, you know, how we dealt with this particular issue. So we can understand that you may have some concerns.

MR COMER: Because when you are reading things you tend to read them very closely and therefore you can run into problems. Just moving on, in relation to the request for further information, we still hold the view that the RIS process is an appropriate one. As I mentioned before, we didn't particularly support the idea of having a separate agency dealing with this. One of the reasons for that is the diversity of cost recovery method that might apply. It will differ, perhaps, from one particular type of regulation to another, so you won't necessarily have a common method that will apply. In relation to parliamentary scrutiny, we would submit that the annual budget cycle process that CASA goes through does, in a sense, validate or reconfirm the government's view about cost recovery on an annual basis.

This latest budget, as Qantas have drawn attention to, did include some additional funding for CASA. It acknowledged that there were some over-recoveries of revenue, so it does, however, though reflect the fact that the government has taken a deliberate decision in those particular cases. Qantas did mention in their submission that the additional funding, much of which is derived from the fuel levy, will be directed at general aviation industry. We would not agree that that's an accurate statement. In terms of the additional funding, there is a whole range of programs that that was being addressed to and a significant amount of that would go into compliance, but it also represents an re-engineering of all of our business processes which have common application right across the spectrum of our operations.

DOTARS made a comment in relation to efficiency audits in the previous submissions that were made and we support that. I mentioned previously that we have an industry forum now which provides advice to CASA. In relation to chapter - or the reference in chapter 9, I think it is, to the guidelines overall - we would submit that CASA is not in a position to, at the moment, endorse the guidelines. We are still working our way through it. We certainly agree that they represent a useful model. We have a lot of support within CASA for the beneficiary or user pays principle, but we feel that has got to be modified in relation to the assessment of the impact on the industry and that is a matter, primarily and ultimately, for government. But as we proceed down the pathway of rewriting our regulations, obviously we will give that far more consideration, but we would be concerned to be tied down to the guidelines at this stage when we are just now going through a review process for ourselves. We

are not convinced that the guidelines would be totally helpful to us, but they're certainly a useful model, in our view. Could we also take the opportunity to, in relation to table 4.3 in the report, to indicate that the Note C reference there is incorrect, or inaccurate. The note indicates that 50 per cent contribution goes to - compliance I think the reference is - if I can just go back to that for a moment.

MRS OWENS: It says CASA receives an appropriation for 50 per cent of its compliance monitoring and standards setting functions.

MR COMER: That's right. The original model certainly had that as its intention, but the government subsequently capped the contribution that it was making, so that percentage would not hold good in today's dollars, so you can't hold that up as being an ongoing model.

MRS OWENS: Well, we'll try and clarify that with you later and fix our final report. Thank you for that.

MR COMER: In relation to the diagram 9.3, if we could just reflect on that for a moment.

DR STEWARDSON: 211.

MR COMER: Yes, thank you. As you track your way through that diagram, there is a reference to free ride as an issue there. We didn't, in our assessment, see free ride issues applying to CASA, but it would be interesting to have confirmation that you would agree with that.

MRS OWENS: I probably would.

MR COMER: Okay, yes. So as you then follow your process down - is charging consistent with policy goals - I guess the policy goals in relation to that would be set by government in our context. Then the question gets posed, is charging cost-effective. Does the commission generally have the view that cost recovery should be full cost recovery? I know you've given a number of definitions in the draft report but are you always assuming that there is full cost recovery or would you see circumstances where that may be a percentage of cost?

The reason I raise that is that in almost all cases where CASA responds to a requested service you would generally speaking have more than one beneficiary but you might not have a full range of beneficiaries. As an example, if I'm required to have a licence to be a pilot, you might be quite pleased about that because I can only fly under certain circumstances. So simplistically - and you can take this across a raft of issues - you will have more than one beneficiary. So I just wondered where the commission were heading on that issue.

MRS OWENS: I think the jury is still out on that one. We didn't really make that particularly clear in our draft report but a number of participants have said to us, "How do you deal with the possibility of more than one beneficiary?" Sometimes it's

not an issue. The beneficiary may be the ultimate consumer and you may say, "Well, we can't actually charge the ultimate consumer because it's not going to be cost-effective, but we can presume that if we charge the firm that that will get passed on." But in some cases there have been people who have been saying to us, will we consider the whole issue of partial cost recovery. I think we're still thinking that one through.

DR STEWARDSON: Can we turn that back on you and ask you what you think. I mean, if you take perhaps not so much the airline pilot licence but the safety approval for the aeroplane itself, you have the people who travel in it - clearly beneficiaries. The airline operator may be a beneficiary. The people living under the path may be beneficiaries because it doesn't fall on them. How do you see the beneficiary position and particularly the balance of who are the major beneficiary in that case?

MR COMER: This has been the subject of many debates in CASA and also previous reports. The Anderson report and the Bosch report and a whole range of reports have tried to address this issue. I think it remains a complex matter. You can, if you want to, take a highly economic rationalist approach. You might go down a certain pathway. If you're looking for a pragmatic result you might take a different pathway.

I think the concept of user pay is generally speaking a valid principle; that you go to the direct beneficiary. I think that would apply across quite a range of government services. But the reason we're giving you I guess a reserved position in relation to the guidelines and particularly the matters of cross-subsidisation - it is a very topical issue. I believe it needs more study before you come to any concluded view about that.

DR STEWARDSON: But when you use the words "direct beneficiary" and "user pays", are you using those two terms to mean, in both cases, the airline company that is the one that is actually immediately and most directly being regulated, or are you using it to mean something else?

MR COMER: I think we should be focusing our discussion in relation to requested services, as opposed to compliance activities, in relation to that. So it might be the seeking of a licence is a good example, or some sort of an authorisation from CASA where it is a requested service by an external party.

MRS OWENS: If it's a requested service by an external party I presume that that person is going to - if they get a licence, they're the direct beneficiary and they would pay for that licence. I think that one is a fairly straightforward case.

DR STEWARDSON: So what about the mandatory ones?

MS BICKFORD: Yes, that's right. I mean, some of the services are licensed - although it's requested in a sense, it's also compulsory if you want to work in the industry. I think that was Dr Stewardson's example of the airline operator's

certificate, which is the certificate the airline has to operate in the industry - that there are clearly other beneficiaries in that example you gave, beside the direct user, which I think is what Mr Comer was referring to there as being the airline in the first instance is the direct beneficiary. But then there are the other beneficiaries, as you say. So that's even in the case of a quasi-service but it's a compulsory service.

PROF SLOAN: I'm interested why the government rejected the ticket tax idea - you know, because there seems to be a certain purity in that model.

MR COMER: I think you would have to ask that question - - -

PROF SLOAN: Was it an issue of cost-effectiveness of raising the money or - - -

MR COMER: The reference I made to that - CASA was not involved in any discussions in relation to that.

PROF SLOAN: All right, so that was just a government decision.

MRS OWENS: Because it is quite an interesting question, which I discussed with Qantas earlier - is that you can either charge through a fuel excise and it goes to the airlines, then they eventually feed it into the price of their ticket because they will try and pass that on. They were talking about how their margins are very small so they will pass it on. So you either do it that way or you do it more directly through a ticket tax. Now, do they have different impacts? One is far more transparent I suppose, which is the ticket tax, and the other one is less so, but maybe they have differential impacts and incentives.

MR ELDER: I think, as we mentioned during our last appearance here, one of the problems with a ticket tax is that we have what's a charter industry, where we don't have records of the passengers carried. So if you introduce a ticket tax the airlines will essentially pick up all the - - -

MRS OWENS: Even more, yes.

MR ELDER: So there may be a greater cross-subsidisation in a sense.

MR COMER: It's a complex area, this - and there could also be an argument that the major airline operators do benefit from having a general aviation sector which is in a sense a feedline to them in numerous ways. I think there is perhaps an argument that they do benefit from having an active general aviation sector. Now, whether they should contribute to that is another issue.

MRS OWENS: I mean, there is the issue about getting the right signals and the right price signals into the system. When you have cross-subsidisation those signals get diluted. So we tend to not like cross-subsidies very much, as you've probably gathered from our report. But you said in your opening comments that that whole issue of - you said that there needs further research on cross-subsidisation. I presume in the context of this - you've got this regulatory reform plan or whatever it's called,

due by next year - that that issue is being addressed. It's complicated.

MR COMER: It is complicated, yes. Our onus is to provide advice, as I said before, to government. But equally important, as you're drafting these regulations and looking at the new ways of doing things, it's imperative that we have an understanding of what services are reflected in those regulations and how that might apply under a cost recovery arrangement. So you're bound to do it in any case. The other mandatory thing for us is that our current fees regulations will become obsolete because terminology will change, services will change, so there is an imperative on CASA to reach a decision for its part and then to provide advice to government.

DR STEWARDSON: How would you see this question of beneficiary being resolved because we are obliged, whether it's a good idea or not, to have more or less a one model fits all or one model fits one or two categories.

MRS OWENS: With some degree of flexibility.

DR STEWARDSON: In the question of beneficiary, if we end up concluding, let us say as a hypothesis that we think the beneficiary of the regulation should pay for it, we've already discussed that there are a number of possible beneficiaries and maybe one can say they're beneficiaries and it's a different percentage of their total thing goes to each one or maybe one could say one is a predominant beneficiary but your case may well be different from other regulatory agencies. How would you see it being resolved as to who the prime beneficiary was for let us say your agency? Would it be agreement between you and the industry? Would it be agreement between you and the government?

MR COMER: There's a significant consultation process that goes on with industry and as I mentioned before, we are looking through our new service centre to set up a whole new range of delivery arrangements with industry so that they understand if they request a service it would be available in a certain time frame. We look at whether CASA would provide that service or whether we have a range of delegates in industry who can also provide that service. So there is a significant consultation process. We go through a notice of proposed rule making. We go through discussion drafts. They are circulated to industry. We go through the RIS process. So by the time something goes to government for approval it has had a significant input from various parties in relation to it and I think it will remain a vexed issue.

We have traditionally regarded standards development as being a direct appropriation and I believe that's a given. I don't think anybody would particularly dispute that. In relation to compliance work there has often been debate about schedule versus unscheduled compliance monitoring. That has been somewhat, I think, resolved in the sense that thus far that is not an industry direct beneficiary pays. It is done through broader cost recovery means.

MRS OWENS: What does that mean, "broader cost recovery means"?

MR COMER: There is degrees of your compliance activity which are recovered

through the levy representing the travelling public's interest in those processes. Then you get to that element of our work which would fit into the context of requested regulatory services. That's where we - - -

PROF SLOAN: So that's service user pays.

MR COMER: Yes, that's where I believe we would have to fundamentally start from a point of a user pay principle, look at who the direct primary beneficiaries are and then work our way through from there.

MRS OWENS: But you've already got some service fees. In the submission you gave us earlier in December you noted about 2.6 million in service fees, about 3 per cent of your overall revenue and I think at that time you said in terms of this review you're looking at this issue of whether you should be pushing more into service fees and out of the fuel excise and having a bit of a redistribution there. So presumably that's implying that there is a potential for more direct service fees in that last group or is that saying there's more potential to directly charge for some of the compliance activities?

MR COMER: No, I should correct that. There is a wider range of requested services that CASA could charge for which it currently does not.

MRS OWENS: Okay.

MS BICKFORD: But that also comes back to the question that we asked before in terms of the cost recovery level because that 2.6 or 7 million that we recover now is nowhere near 100 per cent of the costs to the direct user for those services and that would be a significant change to the industry and has been the subject of much vexed discussion in the past. Therefore that would be 100 per cent recovery from the direct user.

MRS OWENS: So what costs aren't you picking up in that?

MS BICKFORD: You've got to remember that those fees regulations were set in 1995, 4, and are unchanged so to relate those to the costs of providing those services is quite a challenging exercise now just because of the passage of time.

MRS OWENS: So it's just really time. It's not that you've excluded certain costs from the calculation. It's just that over time - those costs were set back - - -

MS BICKFORD: Originally they may have consciously excluded costs from them. That would be a difficult question to answer in terms of how long ago those costs were set.

MR ELDER: One of the additional difficulties in negotiating with the industry is that certain sections of the industry have for a number of years, for many years, believed that they're getting services that they don't need or want and therefore they don't want to pay for them. So we've been going around in that debate and

particularly your lower end of the private sector of the general aviation areas believe they are getting things that are there only for the airlines and therefore why should they be paying. It's not only just in relation to us but it's in air services and so forth. So there's that ongoing debate about whether we're over-regulating them when they don't need to be and that has been a difficult part of the debate.

MRS OWENS: Yes. One of the things we're suggesting, that there will be reviews of existing arrangements for different agencies over the next five years where presumably some of those issues would come to the surface again. You know, what are we doing and should we be paying for this and so on? We've suggested that they be undertaken using the RIS approach or CRIS's. I note from what you've said earlier that you're not particularly in favour of the cost recovery impact statements. One of the justifications we've got for introducing something different is there's a whole range of agencies that don't get picked up under RIS's like the information agencies but there are also - RIS's don't apply for regulations affecting individuals.

I think it's only relating to companies so we had to find another mechanism for that but also the regulatory impact statement processes that are in place now we don't feel adequately pick up some of the cost recovery issues that need to be picked up and at the moment we don't have guidelines but we want to ensure that the regulatory impact statement process picks up application of our guidelines and that's why we feel it has to be beefed up. It doesn't matter what you call it, it's just that if this is going to be done and taken seriously and the guidelines applied, we feel that they need to be brought into that process in some way. I think there is a bit of confusion about what we mean, and the fact that you have expressed concerns means we'll have to go back and make sure that we're expressing all this far more clearly.

MS BICKFORD: Because from our perspective in relation to services, our services are regulatory services, so they are services that are as a direct result of a regulation. So that's part of where the concern comes if you split that from the RIS, because you're consulting on the regulation through the RIS.

MRS OWENS: We're not trying to imply that it be split from the RIS; we're hoping that the RIS will absorb these things so that it becomes just part and parcel, because at the moment - - -

PROF SLOAN: Which it probably would be anyway, for you.

MRS OWENS: Yes. A lot of agencies that are doing cost recovery have never ever brought that into a RIS. There's been very few examples of RIS's actually looking at these issues in any depth. So what we're saying is it needs to be done as a matter of course really.

MS BICKFORD: I guess the other thing that flows from that then - and we wondered how much thought the commission you'd put into it - is the methods of collection of fees, for example: should those fees be - a fees regulation or is some other mechanism more appropriate in terms of the collection of fees, because of course a regulation is a very cumbersome thing to change. Our example of our fee

not being updated since 1995 in terms of making sure that they still are relevant to costs is one that becomes quite difficult when you're looking at managing it through a regulation, and we wondered if the commission had any views about whether were more appropriate ways of managing fee charging.

MRS OWENS: We've talked at a much more general level about having appropriate legislative underpinning, and I think you've given this very good example today about how your cost recovery can quickly get out of date by using regulations that were undertaken back in 1995. I think we will comment on that. It's slightly outside our terms of reference I think, but it's something is important because there's no point having a terrific set of guidelines and good cost recovery policies if you can't then implement those in an efficient way.

MS BICKFORD: And they may become unwieldy.

MRS OWENS: Yes. So we'll take that one on board too.

DR STEWARDSON: Can we go back to your very first statement please, that is, you said that the importance of safety considerations should not be overridden by economic considerations of cost recovery. There was an implication that you were concerned that perhaps we were suggesting that safety considerations should be overridden by economic considerations of cost recovery. If that is what you were implying, I'd like to know where you got that idea from in the report, because it would obviously indicate something we haven't written very clearly. We did say that if regulation was bad regulation then it's impact was made even worse by charging for it, but we certainly were not intending to say that it was our job to actually look at the regulation per se, and we certainly weren't meaning to say, if you felt we were, that good regulations should be watered down merely because they were being charged for. Now, you seemed to be concerned that we were saying that latter, that good regulation should be watered down because of the cost recovery considerations and, if that is what you got from the report, it would be useful to know why you got that impression.

MR COMER: No, in fact, I think the report does address the very issue we're raising there, but my reason for putting it on the record I think is to reflect the very serious sort of issue that CASA looks at in relation to this. We've had numerous discussions in our board, for example, and one of their major concerns is that we don't want the economic imperatives to override what otherwise might be the regulatory objectives, safety objectives, of what we're doing.

PROF SLOAN: We are keen to see that regulations are appropriate and effective, but that is outside the terms of reference. I suppose the point you particularly were making is that it's hard to completely separate the issue of cost recovery from some analysis of the regulations themselves and the views of participants about the necessity of these regulations. You can't really analyse them separately.

MR COMER: You get numerous arguments come up. There is an argument which says that regulations don't benefit, they modify, behaviour; that you can't apply that

economic argument that there is a beneficiary there, that all we're doing with our regulations is modifying people's behaviour. So those sorts of issues come up from time to time as well.

PROF SLOAN: Yes, well, presumably in the absence of regulations there are still pretty strong incentives for the airlines to fly safely.

MR COMER: That's right. We hope so.

MRS OWENS: We hope so. We all hope so. We've got to go home tonight. I think we'll have to break at this stage. Thank you all very much for coming in. I'm sorry about the slight delay. We'll just break for a quick five minutes.

MRS OWENS: The next participant this morning is the Bureau of Meteorology, and welcome. We welcome your second submission and thank you for the interest you've taken - ongoing interest - in the inquiry and we welcome the opportunity to have a further discussion with you on some of the issues which we did talk about at the workshop that we had last month. Could you each give your name and position with the bureau for the transcript.

DR DOWNEY: Bill Downey, deputy director research and systems, at the moment acting for John Zillman who apologises for not being here; he's overseas.

MR WRIGHT: Bob Wright, assistant director services.

MR STEWART: Bruce Stewart, superintendent hydrology.

MRS OWENS: Thank you. I understand you've got a brief opening statement you'd like to make.

DR DOWNEY: Very briefly. The bureau supports the general thrust of the draft report and the draft guidelines that were released in April. In our follow-up submission we've made a few comments on matters identified in the draft report. I won't list those but perhaps leave it to your questions to draw those out.

MRS OWENS: Thank you. I think there's quite a few issues you've raised. There's the issue of how we define core and non-core services. There's the issue of charging principles. We've got these flow charts in our guidelines and we want to ensure that we say - have something in the principles of charging and administrative costs; intergovernmental charging which I think we were very light on, quite thin in our report, and we'd like to have a bit of a discussion with you about that, and differential charging, the issue of ability to pay. I think there's probably a number of other issues relating to the guidelines that may come out in discussion and relating to what we've called cost recovery impact statements. So maybe a good place to start would be this whole vexed question of the distinction between core and non-core activities. I think it's tied a lot of participants up in knots.

There has been a presumption when we talk about core activities that's the important things that the agencies are doing, and non-core in some ways are things that aren't important. I think what we were trying to do is in some way following, I think, the bureau's lead to say there are certain activities which are central to the agency but which really have broader public interest criteria where potentially there should be no charging and there are other activities where charges rightly should be imposed. We're trying to find a way of bringing those ideas together in a way that people understand and accept. I think we said just before we started today that it possibly is a problem with terminology but it may be more significant than that and I was just wondering if you would like to comment further on that issue, if you can help us with this problem we've got.

DR DOWNEY: Yes. I think it largely depends on what one tries to define as core and non-core. Our public services we consider to be up at the extreme public good

end of the materials that we produce but we wouldn't necessarily say that they are any less core than the services, for example, that we provide to the aviation industry or to defence. But because one lot of material goes out via the airwaves, largely, and you can't necessarily identify who the recipients are to recover the costs of it, even if you wanted to do that philosophically; the others are clearly different, you can identify the users and it is appropriate under government policy at the moment anyway to recover those costs.

Then of course there's the commercial activities which we see as being done, I guess in open competition with the private sector, so they are certainly a different category again.

MRS OWENS: I think they're the most straightforward services actually, the commercial ones, to the extent that you should be undertaking commercial services. There's always a question mark about that. But nobody is really disputing whether that is a chargeable activity and usually charging at full cost or the market price, depending upon the degree of competition out there for competitive neutrality reasons. There's this grey area somewhere in the middle. I suppose aviation and defence falls a bit into that grey area.

MR STEWART: I think to some degree it's more an issue with the words "core and non-core: - sorry, just the word "core", I suppose - in that agencies sort of feel that if they identify something as non-core people will say, "Why are you involved in it at all?" and that's where I think the issue is. I suppose that's why the bureau sort of tends to refer to things as the basic service rather than the core service. There are things that are on top of the basic service that we would charge for and then move into the commercial side.

PROF SLOAN: It may just be a semantic issue. I mean, we've had a lot of opposition from the information agencies about the term "core and non-core" because of precisely that, that they see, I suppose - it invites a questioning of any non-core activity that they undertake. A lot of agencies have probably quite rightly pointed out that they in a sense regard all their activities as core, otherwise they wouldn't do them. So maybe basic services is - - -

MRS OWENS: Well, some people might also question that term, but I quite like that term "basic". What's the opposite - non-basic?

MR WRIGHT: The opposite is "specialised" - "basic and specialised". Within specialised you can have cost recovery or commercial.

MR STEWART: I suppose one example that has caused us some problems on this core-type issue is that when a certain degree of privatisation, commercialisation went on in the water industry, one of the functions that those agencies used to support us in - and still do to a large extent - was the flood warning service. A number of the agencies didn't identify flood warning services as being core business. So when we then approached them later on, they would say, "It's not part of our core, therefore we won't be involved in it." That's why I think there is this concern over that

terminology.

MRS OWENS: I think we've learnt that to our cost really because it's actually been a bit of a distraction from the main game, and I don't think in anything we wrote we were actually questioning your approach because I think we quite liked it. We were just saying this grey area in between where you can identify the users like aviation and defence, if you're going to charge - and it's appropriate to do so - if you go down our figure and say "Who are the beneficiaries?" and so on. If you're going to charge we're saying you charge an incremental cost because you're building on the activities, the public interest activities of the bureau and I think it's probably not to make it clear for your organisation because I think you're very clear about how to approach these things, but some of the other organisations have had different sorts of approaches. Although we've generally been more favourably disposed to how the information agencies have tackled these vexed questions I think than some of the regulatory agencies. But it's just trying to make it clearer. I think maybe "basic" and "specialised" may help us.

PROF SLOAN: I think your representative at the workshop - some of the information agencies were not really keen on our using - and I mean, we weren't trying to use it too strictly but the notion of public goods as a defining characteristic of where you move to in terms of the cost recovery regime. But I think the bureau representative was actually quite happy with that idea that there are some basic services presumably that you produce which really do have the characteristics of public goods, that they are clearly non-rivalrous and non-exclusive and that you really found that - you can use that tree quite effectively. I mean, is that your more senior view?

MR STEWART: Yes.

PROF SLOAN: And that's workable for you.

DR DOWNEY: Yes, and the other terms work for us. But I can see how they wouldn't work necessarily for other organisations.

MRS OWENS: Although we do need a set of terms and a set of guidelines that is roughly transferable. That's the challenge we've got.

DR STEWARDSON: Dealings with other government departments that you mention, is maybe less significant for you than for some other people, such as the various agencies of AFFA. But you put the two alternatives for how to treat other government departments, like a commercial deal, in some way just cost recovery or even free, and you favour the latter situation. I just wonder if you would like to elaborate a little on the advantages of the option you would choose.

DR DOWNEY: I guess where it's considered that both agencies of government are acting primarily in the public interest, it doesn't seem to make too much sense to put it on some sort of commercial footing. The general arrangement, I expect, would be that you would seek only to recover the cost of transferring the information that you

might have that is of interest to some other government agency.

MRS OWENS: Yes, it's quite an interesting question, the whole issue of intergovernmental charging, because on the one hand some government agencies would say, "You have a purchase provider arrangement and that could promote efficiency in our organisation. If we have to pay for this we're going to watch the pennies," and so on. But the downside of that is that if it's something in the public interest more generally they might ask for less of that particular information or product or service than is economically desirable, so it may provide a perverse incentive. There's arguments that go both ways, and the administrative costs can outweigh any of the benefits too.

DR DOWNEY: Yes. I can see the sort of rationalisation of demand-type argument where if someone approaches you and they want a certain amount of information, if it's readily to hand and the cost of transfer is not an issue, it's a relatively small amount. If, however, on the other hand you have to go to enormous lengths to generate new information of some kind that's perhaps never been generated in that particular form before, and it chews up a lot of your resources, then you may need to look at it and say, well, this is - you know, the cost of transfer does involve a substantial labour component in here and this is what it's going to cost and we think it's reasonable to recover some or all of that.

MRS OWENS: And you want the other agency to be aware of that, but then they may be wanting that information for some really worthwhile purpose, which is actually hard for you to judge, I mean, it's very hard for you, in the bureau, to look at some other agency and say, "Oh yes, that's a very worthwhile activity, isn't it."

DR DOWNEY: Yes, but we have this at this very moment. AGSO, and I don't know what the new name is, but geological survey people have a project called the cities project where they're attempting to do risk assessments for various natural hazards, everything from earthquakes to meteorological related disasters and it's in our interests to be in a sort of partnership arrangement in that because we have responsibilities of a certain kind. They're mostly in the warning type area, but in terms of preparedness for disasters, there's a lot of climatological information; historical information, that needs to be massaged to get it into a proper risk assessment format. Now, how far it is reasonable for us to go in terms of devoting resources, or diverting resources to that sort of thing, can become an issue.

MRS OWENS: But if you're working in a partnership arrangement then you're in a much better position to judge that, aren't you, than if it's just another agency saying, "We're doing this work and we want your information. What we're doing we think is really important." It's one of the things I think some other agencies - I don't know whether they want to second guess but there is the potential for some price discrimination based on what they think the worthwhileness of that activity or who the person is who's asking for that information. It's quite difficult sitting in one agency to make those judgments.

DR DOWNEY: There's a debate been running for almost a decade within the

so-called Spatial Data community or spatial data arena involving AusLIG and a whole range of other agencies and I think it's fair to say that historically a lot of those agencies have different arrangements in place for the way they treat their data. But after a long, somewhat tumultuous process I think they have now reached the conclusion that it's very much in the public interest for all this information or as much of this information as can be reasonably made available to be out there in the public domain to get the best use of it. It has been after all collected at taxpayers' expense and the Internet for example offers a whole new opportunity to have that information sitting there on someone's server and accessible to a whole lot of people with a few key strokes. So I think driven partly by philosophy partly by technology that things are changing there.

PROF SLOAN: There seems to be some inconsistency. We had - I think he's mainly an agricultural consultant but he has quite specific scientific skills and one of the things he tries to do is kind of advise clients where they might want to plant vines or mahogany trees which seems quite a sensible thing to be promoting and I think the thing is he faces very differential - you know, he might be able to establish rainfall relatively cheaply but soil type, there are a lot of inconsistencies in the cost recovery policies across the agencies and of course - and the ABS he might want to use but he feels particularly prevented in building up a socio-economic pattern of an area.

DR DOWNEY: That's why your inquiry is important.

MRS OWENS: There's also differences between how some of the Commonwealth agencies approach these things, I think like AGSO, and the equivalent state bodies. Some states don't charge at all. Then there's differences between what we do here in Australia and he was citing instances of going into South Africa and the US where there's very low charges because the idea is to encourage some of this activity. So there is a challenge there.

PROF SLOAN: I'm interested in your policy in the more specialised tailored services that you basically don't differentiate between the user, do you. So if Sir David Fortescue Smythe with his 10,000 acres in the western district rings up for a particular service and farmer Bloggs in the Wimmera rings up and asks for essentially the same service, that's the same price.

DR DOWNEY: Yes.

PROF SLOAN: So is the view that whatever equity considerations might be involved in that, that's not for the Bureau of Meteorology to be taking up in their pricing structure?

DR DOWNEY: You can't discriminate, I don't think, on who is on the other end of the telephone or the other end of a Web server.

MR STEWART: Certainly if you're in the cost recovery business to recover costs and not to make money then you shouldn't.

PROF SLOAN: So the policy is to generate cost reflective charging and for that not to be - the nature of the user not to be a consideration. Sir David would probably be very disappointed actually.

MRS OWENS: David probably does provide you with assistance with your measuring rainfall and so on. You do have people all over the countryside that do work for you, I gather, for no recompense except a chart, a nice thing they can put on their wall.

DR DOWNEY: About 6200 of them.

PROF SLOAN: We found that out from the calendar you sent us, didn't we, Helen?

MRS OWENS: Yes, I also found it out - I went and stayed at a homestead after Christmas and they had been doing this for umpteen years and had a nice little plaque up in the hallway from the bureau thanking them for their services.

MR STEWART: We also give them a calendar each year too.

MRS OWENS: The calendars are very nice. We like our calendars.

MR WRIGHT: It can extend back over many generations - - -

PROF SLOAN: Presumably that's common throughout the world that there are kind of volunteer activities needed to support this kind of service. What about governance? Governance is an issue that has been raised with lots of agencies and you have a board, don't you, or you've got some new thing coming out?

DR DOWNEY: We've got one coming up we think. For many years we did have what was called a meteorology policy committee. The new version of that is going to be called a Meteorology Advisory Board or something like that. The reason I say "we think" is that a review has been undertaken. Recommendations are currently with our parliamentary secretary. That is one of the recommendations. It will happen in due course.

PROF SLOAN: What do you think will be the advantages of that?

DR DOWNEY: We did have such a body up until - gosh, I can't think how long ago it was now, maybe 10 years ago. It was in existence from about 1977 through till say the mid-90s or early 90s. The advantages are I guess that you have access to users or user groups. People who have been on that committee or who were on that committee included at one time the editor of The Australian who was there representing sort of the general public. Ron Yates was there - in those days I can't remember whether he had retired at that stage but he's a former chief executive of Qantas airlines, a major user group; others there from agriculture and a range of other interests. So you've got access - Henry Bosch was there at one stage. You've got access to people who have both business acumen and who can represent a sector that

we have our primary dealings with and they can offer advice on user perspective but also bring their own experience from the business world or whatever to it. It was disbanded somewhere there in the early 90s because I think the minister of the day decided that he was quite happy to take all his advice I think from the director of meteorology rather than the board.

PROF SLOAN: Very streamlined processes.

DR DOWNEY: We've always thought it was a pretty good idea. There is an overhead of course in servicing it but we think it's a good idea.

MRS OWENS: I just wanted to go back to something you said on charging principles in para 20 of your submission where you say it would be valuable to have a further set of charging principles - and this comes back to the point that Judith was making about price discrimination and so on. You say in that paragraph:

> Information may be being used by a research organisation for a study that has a potential flow-on benefit to the science of meteorology. In this case it would be an advantage to have a principle that enables the waiver or a reduction of a charge on that basis.

You might be able to make that judgment in that particular case but it's a matter of where do you draw the line there? This comes back to what I was saying before. It somebody else came along and said it has got really important flow-on benefits to geology or whatever would you be able to - how do you make that judgment?

DR DOWNEY: Largely gut reaction I would say. Yes, if a student walks in the door and wants to photocopy a certain amount of information for a thesis they're doing or something it notionally might be $10 or something then I don't think you worry too much about it. If it's somebody else who is doing lectures at a university and wants to work up a certain amount of data we do have memorandums of understanding with major universities that have meteorological type interests - Monash, Melbourne, to name a couple. Then under those sort of arrangements to within a reasonable limit we will allow them to access data.

PROF SLOAN: Our guidelines would provide for that.

MRS OWENS: I think it comes back to what you see as being your basic service and maybe these are the sorts of things that fall back into that.

DR DOWNEY: Yes, you can argue that in many of those cases there's a return to the bureau because it's either improving people's understanding of what it is that we can provide or contributing to the public good generally. On the other hand, if they want $10,000 worth it becomes an issue.

MRS OWENS: Yes. The other thing you've got here is that in the next para you say that - again we're talking about our flow charts.

> A principle that cost recovery will not apply to services or products of less than a minium amount may be cost-effective.

I was just wondering whether you can have hard and fast rules about a minimum amount. We do talk in our guidelines about, you know, is this going to be cost-effective and whether you can make that judgment based on some hard and fast rule, I'm not quite sure, and I just wanted your advice.

DR DOWNEY: No, I think you've got to somehow have in your principles that there is scope as appropriate to waive charges and I think the good example is the $5 variety where if someone's need can be satisfied with a simple photocopy of something in five minutes of somebody's time in the library or whatever.

PROF SLOAN: That would be covered where, you know, is it cost-effective to charge? The answer would be no, don't. You don't say in your submission that there's a cry for flexibility but I'm not entirely convinced that they aren't pretty flexible actually. You could see for example in that case that would lead you in the direction of not charging; in the case of the student and the lecturer you could generate the external benefit so that would - - -

DR DOWNEY: We have a number of offices around the country, observing offices which might be in rural areas and quite often they will be called upon for requests. It's difficult for those offices to handle money for example, to have a cashbox, a safe or something. I'm told that it takes $60 I think to process a cheque within our organisation so you've got to somehow balance these things out.

PROF SLOAN: You could just give them to us, the cheques.

MRS OWENS: I think you've got to be very pragmatic, yes. The other interesting idea you had in the submission was in relation to our guidelines. We are trying to make them simple and user friendly for the final report but you did suggest somewhere in here - I'm not quite sure where it is - that there should be some sort of education program to educate people about how to actually apply them which I thought sounded like a reasonably good idea because I think, having run these workshops and seen how people tried to apply them, and we've tried to apply them ourselves - we've had a bit of a go at applying them - I think it would probably be something we might recommend that that needs to happen.

MR STEWART: Certainly I think without that there will be people who attempt to apply them in the most strict sense without sort of realising the level of flexibility that you've built into them and I think we're probably guilty of not recognising that level of flexibility as well. So, yes, I think that would help from that point of view.

MRS OWENS: I think we're trying very hard not to be prescriptive but on the other hand ensure that there are certain constraints on behaviours so it's a matter of getting that balance right and getting people understanding that. I think people at senior levels understand that. I think it's when you get down to the people that will be the actual practitioners who may take a more rigid view about this and trying to

understand what a spillover is or a positive externality or whatever. We've used all this terminology which we're going to try and dispense with as well. We may not be entirely successful.

DR DOWNEY: This is why these so-called principles can be valuable. I mean, we have people at the lower levels of the organisation who are providing a service of some kind and they've got a simple table and it says the cost of this particular job or whatever it is, X dollars. But they don't really understand necessarily why it's $6 or - but if they can grasp these sort of principles, it sets out for them the philosophy on which the charging is based and so on, then I think it helps them.

PROF SLOAN: No, that was very clear. Thank you once again. Is there anything else? Yes.

MR STEWART: Just one point of clarification, I suppose. In the document, I was a little bit confused when you were talking about cost recovery not including overheads. I read in one area, and I can't remember the exact sort of part of it, but it sort of suggested that, yes, cost recovery shouldn't include an overhead component, and then elsewhere they talked about the direct overhead being okay but not a broader overhead. I suppose I was wondering which was the commission's way forward. I mean, our approach at the moment is that we don't charge the total overall overhead for the bureau. We charge a specific overhead associated with the incremental cost, and we felt that was a reasonable way to go.

MRS OWENS: Well, my inclination is to say that that's a reasonable way to go. I'd have to go back to the actual pages, maybe after we've finished with - - -

DR DOWNEY: Page 229.

MRS OWENS: Yes. I think we'll have to go back and check that because, I mean, like most of our reports, different authors do different bits and they may be slightly - there might be a slight inconsistency we're not aware of. But I mean, I think that we haven't given a lot of guidance actually on the costing issues, as you're probably aware, because again sometimes it's horses for courses and individual agencies have got to work out how they measure an incremental cost. You've probably got more experience than a number of other agencies, and given that Mr Dwyer's here in the audience, he might say that we should be talking about marginal cost. But I think that we would see - if you're measuring the overheads, it should be those associated, you know, at the margin with that particular activity.

MR STEWART: Yes. I think it was an issue of terminology. I think you do use directly associated overhead at one stage, and that made more sense than what I read earlier.

MRS OWENS: So there was one reference on page 229 and another reference on some other page.

MR STEWART: Yes. I'll have to get - - -

MRS OWENS: Well, we might come back to you on that because I think we better make it very clear in our own report, what we're talking about.

MR STEWART: Okay.

MRS OWENS: So thanks for bringing that to our attention. Okay, well, thank you all for coming, and we'll now break for just a couple of minutes.

MRS OWENS: I think we might resume now. Terry, before we resume, do you - - -

MR DWYER: Dr Terry Dwyer, visiting fellow, Asia Pacific School of Economics and Management, Australian National University. I would like to just make some opening remarks. I've lodged the submission. I assume you've had a look at it.

MRS OWENS: Yes, we have.

MR DWYER: Firstly I'd like to say I was very pleased that the report has taken up some of the points we made about marginal cost pricing and its desirability, and the distinction between user charges and taxes, and we're very pleased with the quality of the report and the fact that obviously people have put a lot of time and work into thinking about it.

MRS OWENS: Good, thank you. Yes, we've had a lot of participation. It's one of those inquiries that's warmed up as we've gone on, and there has been a lot of people who have taken an interest in this, including yourself, and I think we're very grateful when we get the people that are actually, you know, looking behind some of the issues, to issues like marginal cost, which is one of those issues that keeps moving, that's always there. You've taken a particular interest in giving us a few comments about APRA and ASIC as well, which I think is useful for us. Now, I think your colleague who we spoke to the other day - I don't know whether he is a colleague, but you do work together - - -

MR DWYER: Yes, we do work, yes.

MRS OWENS: He has expressed concerned about our I suppose loose interpretation of marginal cost pricing, and sometimes thinking about incremental costs rather than marginal costs, and I don't know whether you want to say more about that, but I think in our defence, often it's worthwhile being pure when you can, but when it comes to actually implementing something, it can be that much more difficult to do so, especially when it's not us that's implementing it. We've got to allow these things to happen out there.

MR DWYER: Well, you know, I think you've got to err on the side of the taxpayer or consumer on this, and I think that if too much discretion is given on the measurement of marginal cost, you'll have all sorts of absurdities. I don't know if you saw it in the Financial Review in the other day, but the High Court has been complaining about not being able to fund a public information officer, and the registrar of the High Court wrote in, saying that they were being hit with a user charge and the cost of capital of the High Court building. Well, all I can say is if I were the chief justice, I think I'd be saying, "Well, let's go looking to rent another place and let the Department of Finance find someone else to take the damn building." I mean, that is a tax on litigants in the way they're done it. So I thought it was quite amusing to have a budget for the High Court, half of which goes to a building which was purpose-built for that institution, which has to sit there and has no alternative use. I thought this is an interesting concept of the functionability of

capital, which is actually sunken concrete, stone and glass.

MRS OWENS: Now, you've said on the first page of your submission - you've said, "Where an activity of a government agency is mandated by a public act of parliament, then there should be no question of cost recovery, but the activity should be financed from general taxation through consolidated revenue." Is that implying then that organisations such as CASA and AMSA and the TGA and others should all be budget funded? They're got acts of parliament.

MR DWYER: Yes, because the only exception I'd see on that is beneficiary pays, but the trouble is beneficiary pays is sometimes rather loosely used. Take for example CASA. Everyone has assumed that the only beneficiaries of regulation of plane safety and stopping jets falling off Ansett planes or whatever, are the travelling public. Well, actually, the public on the ground is also a beneficiary. I mean, I would not be very pleased having a jet engine go through my house. When the Concorde went down, in Paris, it wiped out a few people and houses on the ground, and nobody could identify in that sense who the beneficiary is. I mean, any one of three and a half million people in Sydney could have a plane come down on them. So the too - being too quick to identify the nearest user as the appropriate beneficiary, I think may be a mistake.

MRS OWENS: But there's also the other attributes of cost recovery, which is to provide, you know, the right sort of signals in the system to promote economic efficiency, and if you in all instances say, "Well, the community generally is going to benefit from having these regulations and these bodies doing their work, that means that you then no longer have the advantage of getting the signals where you need to get them. Isn't that right? I mean, it's a matter of who - you know, we do take the point there are different beneficiaries say for CASA. We were talking to them this morning. But the travelling public is also a beneficiary of those activities, as are the airlines. You know, they have to satisfy certain safety requirements. I mean, you might say they do that anyway, but I do wonder about it.

MR DWYER: Well, you can have a bit of an argument about beneficiary, because the - and I'll give the Yapper example because it's analogous to the airlines because the strong airlines and the safe airlines with the good safety records would say they're not beneficiaries, that they would prefer to have no CASA at all and rely on their public reputation as being well run because basically in a totally unregulated market, there is always a premium on the quality institution. The Bank of England, for example, when it had private accounts in the 19th century and had no - was basically a preferred bank, as National Westminster or National Provincial Bank versus the country banks. London would have been strong enough to say, "Well, we don't want regulation." In a way, you could argue that regulation enhances the quality of the smaller operators.

PROF SLOAN: Can I just butt in there, because I think quite - I mean, I like your submission, but I'm not sure it's going to help us much, I might add, because it's sort of, you know, out of the ballpark, if you know what I mean.

MR DWYER: Well, we'll talk about that later.

PROF SLOAN: Well, let's take - about CASA. Let's say, you know, the plane crashes, in the case of YL Airlines and the relatives of the deceased, you're saying they would have no ability to sue CASA or certainly investigate whether, you know, the negligence of CASA - - -

MR DWYER: Yes, see, this is the point. It's a very important point because - - -

PROF SLOAN: You know, there's no real contract with CASA.

MR DWYER: There's no quasi contract, because if you're going to say it's user pays, then you have to say - - -

MRS OWENS: We call it beneficiary pays.

MR DWYER: Beneficiary pays, you still have to say what is the service for which they're paying. Now, in a normal commercial, competitively neutral environment, under our normal principles of law, if I pay you to give me advice or do something for me as my agent, then I am entitled to expect that you will do it with the due and appropriate care and skill, and there's a liability on you, both in terms of contract law and tort law, that if you don't perform the service, then I can sue you.

Now, take for example - I've got a very practical example of this, and this is one of the reasons I put in a supplementary submission. I happen to be a trustee of a deceased estate for a widow and three orphans. Through the negligent action of a financial planner, that estate has lost $150,000, which we have to sue for. The professional indemnity insurer was HIH. We had no choice about who the financial planner insured with, but I was personally morally outraged at the attitude of the Commonwealth government, having collected millions and millions in regulatory fees for a service that was negligently performed to anyone's measure, as the evidence is coming out, turning around and pretending it had no moral liability at all to chuck out tuppence ha'penny.

The only thing that forced any honesty on them was an outraged public reaction similar to mine, which started to say, "Well, if you have regulation, then who is the regulation for?" Obviously it's not for the benefit of shareholders; they take their risks. But the reason we have public regulation and banks and insurers is for the protection of the third parties who contract with those bodies, namely the depositors and the policy holders. Now, I found it totally unacceptable to see this business of user pays being turned to a revenue source for a Commonwealth government that hasn't performed it. In the case of insurance, for example, I know there has been some very naïve sort of stuff written in the Financial Review saying, "If people take their risks - they chose to insure with HIH. They got cheap premiums. Why should anyone bail them out?" I have a little bit of sympathy with that - - -

PROF SLOAN: Well, that's one class of policy involved.

MR DWYER: One class actually did it.

PROF SLOAN: There's those one who actually purchased it.

MR DWYER: Yes, exactly.

PROF SLOAN: There is another class - - -

MR DWYER: I can see some argument for that, except that what that argument ignores is we don't operate in a free market with full caveat emptor, as I've tried to say. We live in a regulated market where it is legally impossible for an Australian resident to take out insurance with a foreign insurer. I, for example, have a policy with New York Life Insurance, which I took out when I was a resident in the United States. I've maintained it but I cannot increase it, because it's illegal to do so, and they've declined my request years ago to increase it. A couple of times I've tried. Actually, I checked out the Life Insurance Act. I think I could, but they weren't going to get into fighting the Australian prudential authorities.

But this is what I'm driving at, is for the Commonwealth to say, "We are passing legislation to prohibit you as an Australian consumer using unlicensed airlines or unlicensed insurers or unlicensed drugs, prohibiting it, then saying caveat emptor, and by the way, we're charging you for the benefits we've given you, even though we may have stuffed up completely." I think it's totally unacceptable.

DR STEWARDSON: What would be the practical alternative, though - what would be the practical affect of the alternative, of saying that the regulator could be sued every time an HIH went belly-up?

MR DWYER: The practical conclusion would be that we'd be forced to have an honest system or regulation, instead of this dishonest stuff in the nether world where we may or may not be able to count on policies or bank deposits. We would - the Commonwealth would in effect be forced to operate a proper commercial actuarially sound reinsurance or deposit insurance system, and then people would know where they stood. I mean, it's better in the United States. You know that if you've got a deposit under $100,000 and you're a customer with a small savings bank or whatever, you know you're insured up to that amount. You know where you stand.

PROF SLOAN: Also I understand there is a kind of choice, if you had more than that, that you can - you deposit it with someone and there's a transparency and the fact that there's insurance, that, you know - and so for that you may in fact pay a price, lower returns, or you can go off and put your deposit in a - - -

MR DWYER: Well, when I was in America, I had a choice. I could put money in a savings bank and that was insured with the FDIC, or I could money in a cash management fund. That was where they came from to this country, and that was not insured, but then it was caveat emptor so I looked around at fund manager and checked out fidelity and (indistinct) and so on. So what I'm driving at is that as I've

said, APRA and ASIC are, instead of delivering value for money, they're worse than useless, and I'll give you another example - - -

PROF SLOAN: Well, because they're providing a sense of false comfort.

MR DWYER: False comfort, false security, false information to a market. I'll give you another example of ASIC's delinquencies. When Allan Cameron was at ASIC - you'll remember the first NRMA demutualisation. I read through the prospectus very carefully. It's something I do, I suppose, as bedtime reading. Sort of a sick hobby, I suppose; you'd have to be a masochist. But I noticed that on the face of it, they had breached the provisions in the Corporations Law on a company becoming a member of itself through becoming a member of the subsidiary.

Now, it was done for good, sensible tax planning reasons, and you could see why they didn't want to trigger capital gains tax on the whole portfolio, but it was nonetheless a clear breach of the Corporations Law, because - anyway, basically, to cut a long story short, I raised that in a formal letter to the ASC, pointing it out. Nothing happened. They got thousands of letters from members. Nothing happened. The enforcement was not due to the ASC, the enforcement was due to Dawn Fraser and Richard Talbot willing to put their houses on the line and go to the Supreme Court, and ASIC at the time had a commissioner who was in fact a director of the NRMA; a hopeless conflict of interest.

Now, if that's the sort of regulatory enforcement you've got, I'd prefer to have none of it. Sack them; save ourselves the money. The other thing is that the theory behind having a corporations commission or whatever goes back to the 19th century, and the idea was freedom - as John Stuart Mill put it - freedom with publicity. You should be free to trade with limited liability, but there should be publicity about your affairs. Now, what we've done is got - we've got freedom in a way, but publicity if you're willing to pay for it. So when you go online - I noticed your comments about online access to information. If you go online to the ASIC Web site and search a company, you get hardly anything about the company. You've then got to pay.

So it seems to met the whole rationale for ASIC is pretty dubious. They don't inspect prospectuses any more. They don't vet them in the way they used to. I'd prefer actually a totally deregulated market, a genuinely deregulated market where people didn't have this illusion that there was a regulator or a nanny looking after them. Then at least we'd have our eyes wide open.

PROF SLOAN: Because I think that issue - ASIC is both a regulatory and information agency, clearly. I mean, you know, the notion that you'd have to pay for the information which is actually being compulsorily required of companies seems a bit strange, doesn't it?

MR DWYER: Exactly. I mean, the information is collected in the public interest because of this theory of freedom of publicity and then withheld from the public. But it's funny: you look at the Yannon transaction; I'm not saying whether anyone is guilty or innocent or anything, but you just have to shake your head and say, "If this

is the sort of regulation we've got, why don't we scrap ASIC? Why don't we amend the Corporations Law to simply say that any shareholder can inspect any document of the company after a maximum of say six months and leave it to the market to enforce itself?" because a lot of fund managers would be crawling over companies. I mean, if you had a truly laissez faire economy, you'd go back to the old law of partnership, where any partner had a right to inspect the documents of the partnership, and that would keep directors very honest.

So I just raise that, but in terms of APRA and ASIC there was this classic case of insolvent trading, it seems, occurring over a long time. Both of them were asleep at the wheel, both of them were negligent on any commonsense view of the legal obligation, and why should the public have been charged tuppence ha'penny for this? But the point is, having charged a fee, the Commonwealth cannot now deny a moral responsibility.

MRS OWENS: Can I just come back to this whole issue of taxing and not taxing and so on. You've got a fairly well-defined public finance principle of taxing particular groups in society for the provision of government services that only they consume, what's called the benefit principle. Isn't it true that on equity and efficiency grounds the taxes that target that particular group may be superior to general taxation?

DR DWYER: It can be, and I certainly wouldn't want to deny the benefit principle or the externality principle. In fact, I've been a strong advocate of both of those in regard to public utility financing, and I was pleased to see the word "externality" turn up here, where you'll scratch to find it in reports on public utilities, where I think it's in fact equally or as important. I mean, obviously roads and railways and pipelines add value to the surrounding lands and there's a logic to rating those lands to recoup, and as a form of benefit taxation, those infrastructure costs.

The only thing I'd say, though, is in terms of the benefit principle we have to be a little careful about what we mean by "benefit" because, as I've said in the concluding remarks, because if you applied that consistently you would, as I say, say to people, "We supported your parents in an assets-test-free house on Sydney's North Shore. The house is worth over half a million. They were able to live in it five or 10 years because you weren't having to pay for their maintenance or chose not to. We will recoup by way of a tax the Commonwealth expenditure on maintaining your deceased parents so you can inherit the house. I mean, who are the beneficiaries of the social security system? You would have to say in many cases the indirect beneficiaries of the socials security system are children relieved of the burden of supporting their parents and who inherit their houses in cities like Sydney.

PROF SLOAN: But maybe our children will be relieved of that burden when we get old so it all just passes down. I think it's a generational thing.

DR DWYER: Yes, but what I'm driving at is when you talk about the beneficiary principle in fact the whole object of much government policy in the redistribution area is precisely to benefit people without charging, which is why people who get so

angry about the welfare state. People who pay their own way for their own independence and their own health and insurance get extremely annoyed when you talk to them about the amount of redistribution going to people who aren't asked to pay for the benefits they're getting, which is why of course the government has got so far politically with this concept of mutual obligation. People are now in some way objecting to it. So that's why I did want to make the point that to some extent the application of beneficiary pays is somewhat arbitrary and treasuries seem very adept at thinking of ways to extract money from good middle class taxpayers, but anyone who questions the extent of redistribution which is not recouped somehow is swept aside. But that's a philosophical issue which I know is outside your remit here, but I just thought it was just worth noting.

MRS OWENS: We're actually not doing an inquiry into ASIC either but, you know.

DR DWYER: Yes.

PROF SLOAN: I think this all raises some interesting points, and the kind of user pays idea when regulation is compulsory and provides dubious benefits - you can ask some philosophical questions about that. Presumably your point about this is that it's just hidden forms of taxation essentially.

DR DWYER: Yes. That's why I was very pleased at your discussion on taxation. I noticed the solicitor-general gave you what, if I can be rude, I thought was a rather typically snaky legal opinion on how we're really okay.

PROF SLOAN: For which we paid.

DR DWYER: You got charged for that, did you?

PROF SLOAN: Of course.

DR DWYER: You should have charged him for reading the propaganda.

PROF SLOAN: Governmental charging, definitely.

DR DWYER: Yes, I noticed AGs had a high level of cost recovery there. But what amused me, having read that, was to go on the Web and note that the Corporations Law charges are now being reformulated as taxes. So I thought, "Yes, this is the old game of we'll pretend everything is in order but we'll run around fixing it up." I thought, "Yes, they must think you're silly."

PROF SLOAN: But is not one of the themes that come out of that discussion that for obviously technical reasons but philosophically, if it's a tax, call it a tax and put it through tax legislation and - - -

DR DWYER: And be done with it.

PROF SLOAN: - - - therefore through appropriate parliamentary scrutiny. Let's not - - -

DR DWYER: Precisely, scrutiny. Let's not shillyshally around and play games with user charges and undisciplined things which are really legally dubious. Let's be honest, let's call it a tax. Call it, if you like, a benefit tax and let people debate whether there is a benefit, and list it in the budget papers as a tax so that we don't get this artificial gain of fiddling Australia's tax to GDP figures by sweeping revenue that is really tax revenue into fees, charges and so on. The truth of the matter is treasuries have been extremely adept at fiddling the statistics on taxation by shifting things off budget. In fact, you could say the super guarantee levy is in a way an off-budget tax designed to save expenditure on the age pensions. Mind you, they've stuffed it up, so they're not going to save so much because they didn't require dollar for dollar income testing, but that's another story.

So if you really want to get serious about it you should say, "Call a spade a spade. Be done with it and justify it to the public and to parliament." That's honest, and that's partly why I was inspired to write this little submission. The dishonesty of the systems of regulation that don't deliver, and the dishonesty of politicians who then pretend that they've got no responsibility even though they've passed acts about solvency of insurers and everything else, really did get up my nose a little bit.

MRS OWENS: Can I just clarify something in your submission. It might have been because I read it late at night, but you've got a paragraph here where you start talking about water. I think I picked up on this and put a question mark on it because you accused us of being logically inconsistent. I couldn't actually understand why I was being logically inconsistent because I didn't understand your argument.

DR DWYER: Actually, I will go back to that. It was a very interesting point because I was saying, "Look, I agree with you totally on the importance of externality in this inquiry." That was actually an Industry Commission report, so - - -

MRS OWENS: I was on the Industry Commission as well, so I have to take responsibility for any logical inconsistency, so I'd better find out what it was.

DR DWYER: I'll explain it to you. In the report on cost recovery for water - - -

MRS OWENS: I wasn't involved in that.

DR DWYER: Yes, that was the one there. There was a discussion on user pays for water, and the argument was made that you should move away from land rating charges to access and per volume charges for water, as being more efficient. My objective to that was: hang on, it ignores the externality argument, because if I lay water mains along this street every block in this street rises in value, even though nobody chooses to connect for 10 years. In fact, William Vickery, who got the Nobel prize in public economics, actually has a discussion of this in one of his articles in terms of infrastructure in the USA - that when you run roads or whatever and railways everyone gets a benefit, even the people that actually don't get

connected, because there's no way you can avoid the improvement of your physical - you're coming closer to the infrastructure. It adds value to you, and of course real estate speculators know this and that's why they hang onto land on the outskirts of cities, waiting for the infrastructure to get there and increase the value of their land.

PROF SLOAN: And that's why you have nimby movements too.

DR DWYER: Absolutely.

MRS OWENS: I think I now understand.

DR DWYER: Anyway, if you go back to that water inquiry, there was a very interesting note which gave away the whole argument. They said we should go to user pays to be more efficient and get rid of water rates and just access charges, and then in the footnote it said, "But of course rents might rise to reflect the lower charges on the land." In other words, the footnote admitted the true beneficiaries were the landholders who were getting the benefit of the externality from the improved infrastructure. So in fact the people who wrote that report had sort of contradicted their recommendation. In a way, the land rate was a perfect access charge, because it really should have been an availability charge - not actual access but availability, and the land rate was that, so in a way the externality argument in the public utility area has been put aside when it shouldn't have been, because in fact it is the perfect method of financing your access charge. So that's why I made that comment, but it may be a bit unfair.

MRS OWENS: No, I just picked that one up and I said "Ooh".

DR DWYER: But don't take it personally.

MRS OWENS: Have we got anything - - -

PROF SLOAN: That's fine. I think it was useful.

MRS OWENS: That was very interesting, so thanks very much, Dr Dwyer, for coming once again.

DR DWYER: Yes, thanks for your time.

MRS OWENS: We'll now break and we'll resume at 1.15.

MRS OWENS: I think we will now resume. The next participant today is the Department of Agriculture, Fisheries and Forestry Australia and related agencies. Thank you all for coming and could I get each of you to give your names and positions with AFFA or with your organisation for the transcript. Maybe we'll go from right to left.

MR CARLTON: Tim Carlton, general manager business strategy, Australian Quarantine and Inspection Service.

MR READ: Greg Read, acting executive manager, Australian Quarantine Inspection Service.

MR JONES: Brian Jones, general manager innovation and operating environment, AFFA.

MR INGHAM: David Ingham, manager, innovation and operating environment, AFFA.

MR ROSE: Roger Rose, chief research economist, ABARE.

MR SMITH: Ron Smith, corporate business manager, Bureau of Rural Sciences.

MRS OWENS: Good. Thank you very much, everybody. We've got a joint submission. Earlier on we've had a number of other submissions from some of you individually and we've now got, I think, a very, very useful joint submission which covers issues for us for both information and regulatory agencies. So I'd like to thank you for all the trouble that went into that submission. Mr Jones is going to make an opening statement, but if anybody else wants to say something up-front, please feel free to do so.

MR JONES: Thank you, commissioner, for the invitation to appear at the hearing today. We regret that we were unable to get our submission into you until yesterday - apologies for that. By way of introduction I'd like to remind you that AFFA is perhaps unusual in that we have both regulatory and information agencies in the one house. As we mentioned in our first submission to you, the cost recovery arrangements operate in the following areas of AFFA, there's ABARE and BRS on the information agency side. On the regulatory side we have AQIS national registration authority for ag and vet chemicals and a number of other areas. Today we have representatives here from AQIS, ABARE and BRS.

I thought it would be useful to make a few general comments before we invite your questions. First, we agree about the need for cost recovery guidelines for government agencies and in the case of AFFA the regulatory agencies at the moment are broadly consistent with the proposed PC guidelines, although that's less true for the information agencies. In the latter case I understand that there's been discussions with the commission in the workshops on this subject, so you're probably reasonably familiar with some of the issues. Other than the guidelines for the information agencies, the comments in our submission mostly deal with grey areas and practical

implementation and so the issue there for us is flexibility and application. There's also a number of points of balance and emphasis that we're pointing to. As you will have noted, our main issues are summarised in the executive summary, but I will just ask colleagues from AQIS and ABARE if they'd like to draw your attention to particular points.

MR CARLTON: Perhaps I could just add something from the AQIS perspective. I think from AQIS's perspective the draft guidelines are a useful document and with a few exceptions the existing AQIS arrangements are consistent with the recommendations in that. I guess there's three areas of which AQIS has some concern over. The first one would be the focus which is on stage 1. The guidelines consist of about 34 pages of which about 23 are focused on stage 1. It's been AQIS's experience that the issues covered under that policy review stage and are normally considered and decided by an external authority, generally in our case cabinet. So I guess we would like to see a change of the emphasis to see more emphasis on the stages 2, 3 and 4.

The second one may be a little peculiar to AQIS in that client consultation is an extremely important component of AQIS's government's arrangements concerning cost recovery dealing with nearly every stage of the cost recovery starting from the development of budgets and the development of costs base, the development of recovery systems, recommendations which go to the minister to vary fees, the monitoring of financial results and the effectiveness of the cost recovery mechanisms. I'm not suggesting that the AQIS model is appropriate for all other agencies but the guidelines could be expanded to cover the possible inclusion of client groups in an overall government's frame work.

The third one is in relation to the proposed cost recovery impact statement which AQIS would support, but not if it's a duplication of the regulatory impact statement. If it's a statement to be used where regulatory impact statements aren't use, we would support that, but we wouldn't want to see two separate processes.

MRS OWENS: Does anybody want to say anything at this stage?

MR ROSE: There are some specific things to do with information agencies that we'd like to comment on. I think ABARE's original submission and in the evidence at the initial public hearings we discussed some of the background and to an extent some of the difficulties in defining core activities. What we define as the core activities on the role of ABARE as it turns out is a very much broader public policy role than what appears to be the space left for us in the draft submission. In essence ABARE sees its role as providing policy and related information that is central to the policy process regardless of the manner in which that's funded. We have a broad role across agriculture, forestry, fisheries and related resource base and resource management issues and minerals and energy.

As best we can interpret the set of guidelines in the draft submission, we would be expected to define the role narrowly as core business being that business which could be directly appropriation funded by a host department which is AFFA and that

would seem to rule out the relationship that we have with DISR and to rule out the relationship we have with the rural R and D corporation. Those two relationships are central to delivering a substantial part of that core policy-related information that we deal with. So while we're cognisant of the difficulty in defining core activities, because it's something that's on our mind in a continuous basis in making choices about what we do, making choices about work we bid for, we feel that the guidelines as they exist in the draft basically fail to recognise in ABARE's specific case those two broad sets of relationships and really fail to recognise the underlying processes of government which have developed those kinds of relationships.

In essence virtually all of the things that we do, except for some - as we pointed out in our initial submission that are purely private - virtually all of the things that we do are central to Commonwealth policy. We don't stray outside those area except occasionally when we simply have better information than anybody else has on a commercial basis that's really a spin-off on the public policy process. These are core activities. They're core government-funded activities with the exception of the RDCs to some extent. We're dealing with things that are not national public goods in all cases, but are often public goods within an industry or within a sector. Hence one of the primary reasons for setting up the RDCs under a partially government, partially industry-funded set up.

So it's not that what we are doing that is not directly funded through AFFA appropriations is not central to government, it's simply that it comes through different departments, there's a base set which comes through AFFA and DISR. So there's two departments involved to start with and there's other work that we do for other departments. There's work that we do for the RDCs which is still essential government work but it is not all line funded with a simple one department, one organisation line up. There's no obvious administrative or economic reason to suggest that governments should be directed to do that in a simple line function. It's not the way that government has moved in recent years.

There's another - I think it's ABARE specific, but Ron Smith may want to add something about BRS in this sense as well - there's a suggestion in the draft report that ABARE's farm surveys data collection activities be directly government funded and that ABARE make all of the information available on the Net. Now, we go as far as we can in making that information available. We recognise the public good argument underlying the commission's suggestion in that, but there are some fairly obvious limits. In the first place, some of this information is not purely government funded and shouldn't be purely government funded because it harks back to the industry R and D corporation issue that I just raised. Some of this is substantially funded by industry and that places both - it provides us with some opportunities within industry, it also places some limitations on what we can do. It certainly places some limitations on how much of should be government funded in a direct sense.

There a couple of other limitations on how far down the track of accepting that once the data is collected that the information is a public good. One is that we have very strict confidentiality requirements. We gather the information from individual farmers, individual operators in fisheries, and occasionally in other industries, on the

understanding that we guard the confidentiality absolutely and we do that. That means that sometimes, and not infrequently, people ask us for some of that information and for particular views about that information. We can provide you with a version of the information which protects the confidentiality but gets them as much information as it's possible to do with that requirement. But that's often fairly expensive if they have particular requirements and it wouldn't be possible to make all of that available, to give free access to individuals. So in general we charge the additional cost, we charge the marginal cost for that additional activity.

In a more general sense, to the extent that we can provide the information in an aggregate sense or in various breakdowns, the number of permutations and the number of ways of allowing access is almost infinite. It's not as if this is simple, straightforward information that we can just place on the Net in one form and allow everybody to have free access to it from there on. How far we take the manipulation, how much detail we put in makes an enormous difference to how costly it is. So what we do currently is make a judgment on the basis of requests that we get, on the basis of discussion with industry groups and with the research and development corporations where they're co-funders, about the form and the detail and which represent it.

We can't, as is suggested in the draft report, expect government to front up with a huge slab of money that would be necessary to make it freely available in a widely accessible format. We can't go that far.

PROF SLOAN: I don't see why not. Plenty of other groups do.

MR ROSE: I doubt it.

PROF SLOAN: We do.

MR ROSE: It's very detailed information. We have to both protect the confidentiality and present it in a form in which it makes sense.

PROF SLOAN: But isn't that why you're there?

MR ROSE: Yes, that's why we're there and we do that as far as we can. But the suggestion that the commission makes is all available in a purely open-ended fashion is impractical. It costs more to put it up in more detail. There's enormously more detail in the farms' surveys information than is currently available on the Net and it would cost a lot more money to set it up. There is no obvious reason that we should do that.

PROF SLOAN: Except that you have to make sure that what you do is absolutely consistent with emission, because otherwise we may as well sell you off to the private sector and get them to do it.

MR ROSE: And they are not going to make that kind of information clearly available and government is not going to fund them.

MRS OWENS: We received submissions and confidential material from organisations with whom we were carrying out inquiries. We don't particularly like getting confidential information, because then we can't really keep it or use it in any way, but all our information, everything else that we do, ends up on our Web and it is freely available for anybody who wants and cares to look at it and use that information. Now, if they want to include and research reports and all sorts of things, if they want to take it further, then they are free to do so. But we see our mission as providing I suppose a public good for people.

MR ROSE: Which is why we make a set of industry aggregates and much lower level information freely available currently and we continue to work to make that more accessible and accessible in a more detailed form. But the very nature of this information is that it is confidential and that confidentiality has to be protected. This is detailed information on all of the production and business activities of individual farmers, so obviously it has to be aggregated to a much higher level than that before we can make any of it available. We are talking about a very large data set over a very long period.

PROF SLOAN: Although they are small with what the ABS deals with. I mean, it's not as if you are having to invent the wheel here. This is an issue confronting all information agencies and it's really where you draw the line. I mean, obviously the issue of maintaining the confidentiality is important. There seems to be very different policies across information agencies and across information agencies around the world. In America there really is a policy of providing a tremendous amount of data free, so it's not as if it can't be done.

MR ROSE: I'm not arguing it can't be done. The government - - -

PROF SLOAN: And I'm not even sure - it's not about theory, it's really about pragmatism.

MR ROSE: There is no way that any government or research and development corporation is going to give us twice the budget to produce the information in twice the detail.

MRS OWENS: I was wondering whether Mr Smith wants to make any comments about BRS and there is a range of other issues we wanted to discuss.

MR SMITH: Thank you, commissioner. In respect of the first point that Roger is making about the core and non-core activities, we actually had similar sort of concerns, so I was going to say that we don't have DSIR as a major client, but we do have the Research and Development Corporation and we do have other government departments, so we face exactly the same issues as far as the intergovernment transfer pricing question goes. In terms of the farm survey, that is not an issue for us. We do actually place on the Web data sets and things that are freely available, so our issues are not the same as ABARE's in that respect, but in most of the other issues we run a similar line to ABARE.

MRS OWENS: There are a range of issues that we would like to discuss and I think one of the issues which we have discussed with other agencies dealing with information issues is this issue of core versus non-core. I think the terminology has tended to trip people up. We had a quite useful discussion just before lunch with the Bureau of Meteorology who suggested maybe we should think about it in terms of basic and specialised services, or use some less emotive language. But I don't think we were ever trying to imply that "core" meant in some way something important and "non-core" is something that is less important. It is really just those services for which an agency could charge and those services where it may be appropriate and it may be appropriate in the case of ABARE to charge marginal cost or whatever, or even at market rates, if we are talking about a service or a product which is competing on a commercial basis with other suppliers.

So I think we are trying to deal with the terminology and see if we can get a better way of describing what we have been thinking about and I think that in the case that we were talking about with ABARE, a lot of the work you are you doing is really basically intragovernmental if you like and I think one of the weaknesses in our report to date, which I really do acknowledge, is that we haven't dealt with that issue barely at all. We certainly haven't dealt with it well and that's something that we are going to be trying to improve in the final report. But I think there are a set of important issues that we need to understand and tackle in relation to intragovernmental or interdepartmental, interagency charging and that is the underlying rationale for doing it.

We would really like to get your views on what are the advantages and disadvantages of funding an agency's activities through some sort of transfer funding or purchase of provider arrangements or whatever you want to call it. Does anybody want to make a comment about that, because we are going to extend the guidelines and discuss this issue and we are just wondering if you have insights. If you are at ABARE and you are charging DISR for some of the work you are doing for example, what are the benefits of doing that and are there downsides from taking that approach?

MR ROSE: I guess going back to the time in which the decision was made to move Minerals and Energy activities to DISR and form AFFA as a larger agricultural resource department, there was a point where we had to ask ourselves the question and when I say "we", that's the management of ABARE and of both departments. It doesn't make sense to peal off the economic research of ISR, or would it be better to hold it in some form in ABARE. The pros for holding it in ABARE really are questions of research economies. There are a lot of similarities in the data collection, even in some of the data sources, but less on that side, and many more similarities in the analytical methods and the issues that are involved across the whole resource sector.

So we believed that we could do it more efficiently by maintaining one organisation with that whole brief, rather than splitting off into a couple of smaller organisations. Part of that is a question of size economies and much more of it is a

question of economies of scope and having people in a larger organisation which allows you to have a greater degree of specialisation in terms of delivering particular services and styles of research across a wider scope. I think that works. I think we have demonstrated that that works, largely to the satisfaction of both departments and to our own satisfaction, managing it as an organisation.

It is not without its costs, because we always have at least two masters and several ministers and although we are not two steps removed from the policy process, that gives us some fairly interesting resourcing decisions and management decisions at times when there are different pressures coming from different sources.

MRS OWENS: If you are going some work for example that is of interest to DISR - we won't talk about your R and D core at the moment - but if you are going some work for the other department, do you charge - is there some sort of transfer of funding for that work?

MR ROSE: In essence, how it works is that we have an agreement about how much work we will do and what the budget for that work is, with each department and those resources are quarantined to do that work. They are quarantined in the sense that that's what we spend.

PROF SLOAN: So is that purchaser provider split? Is that the model?

MR ROSE: Yes, but we have the freedom to use the services of individuals on our staff across both of those and in a sense to join some of the project work where we have people with skills which are useful, not only people, but analytical models. GTEM for example is used freely across both of those and indeed, some of the funding of greenhouse work is a mixture of DISR, AFFA and sometimes AGA funding for common projects or common sets of projects. So that's where we get some of the advantages in terms of being able to deliver a set of products from a common set of resources that would be much more difficult to deliver for a couple of different organisations.

MRS OWENS: I'm just really trying to tease out what the incentive effects of these sorts of arrangements, because basically what you are doing, if you are working and doing something that is of interest to, say, DISR, it's basically work I presume with a public good characteristic.

MR ROSE: Yes.

MRS OWENS: If DISR is going to have to allocate some of its budget for that work, does that mean it's going to influence the amount of work that they are going to want to demand, because they are going to have to pay for that, albeit through the budget amounts that are allocated through appropriations. It might conceivably mean that there is an undersupply of that sort or work, or is this drawing a very long bow?

MR ROSE: I'm not sure if I can answer that one.

PROF SLOAN: Why don't they just give the money to you and be done with it?

MR ROSE: Why don't they give the money to us?

PROF SLOAN: Yes, through the appropriation. What's the value added in having the split? Because that's how it used to be for you. I mean ABARE was never a cost recovered agency in the way it is now.

MR ROSE: No, but in essence while we had some more flexibility because all of that money was from one department, we still had to negotiate with policy areas of the department on what projects we did and what the split was between minerals and energy projects, agricultural projects and fisheries projects. Apart from the fact that the demands now come from two completely different departments, I don't think much has changed in terms of our responsibility to map out what we think are the important issues or the departmental responsibility to come back to us in response to our suggestions or to be proactive in outlining areas that it wants work done.

DR STEWARDSON: Can I ask you, am I correct in thinking that the key to ABARE's problem, in terms of our guidelines at the moment, is simply that where our guidelines are talking about taxpayer funded, there's an implication that it's an appropriation that maybe comes via department but that it's coming via one department and it is the appropriation, and your problem is that you have a number of sort of master departments. You belong within AFFA but you get what we're, in our terminology call funding, from a number of departments. That's the key point I make.

MR ROSE: Yes, it is.

DR STEWARDSON: So what presumably the solution is is to try and define appropriately the funding you get from those other, if you like, master departments, other than AFFA, but it's slightly complicated because at least some agencies, and probably ABARE too, do have dealings with various other government agencies and/or departments that are more in the nature of a commercial dealing, such as they might have with private industry, and some are sort of a bit both ways. I mean, for example, I think with the ABS, they basically have their primary funding, but some government departments can say to them, "Look, you know, we think it's highly desirable that you do this particular thing," and they can fund that, which is a sort of in between stage perhaps between core funding and doing a commercial job, as it were, for an outsider.

So I guess the problem lies in defining boundaries between those three types of money coming from other government agencies. I don't know whether you've got any suggestions as to how we do that defining, but that seems to me to be what in effect you're telling us needs to be done to make our system work for ABARE.

MR ROSE: Yes. I think that's certainly true.

MR SMITH: From a bureau's perspective I'd agree with that. I mean, I think I said to Linda just recently, for this current year, 50 per cent of our funding is coming from what I would call external sources. But the external sources are other government departments, research organisations and the R and D corporations, and our core, if you like, is AFFA. But even some of those R and D corporations from within the agricultural portfolios - so they're coming from somewhere, but not necessarily from the budget appropriation funded things. That really is our issue in terms of what - - -

MRS OWENS: So does that mean you're going to be more responsive to the demands of those other departments and agencies because they're providing funding, and so what you're going to do is actually going to be influenced by what they're paying you to do.

MR SMITH: Because they are in effect our client. Being a scientific bureau, we're providing scientific advice for evidence-based policy. That might be for EA transport and regional services as well as AFFA. What we do is make sure that the work that we do is linked to the AFFA outcomes, but our key client is AFFA, because that's where half our money comes from. But our other client is the organisation that we're contracting with, and we quite often go into competitive bidding to get some of that work.

MRS OWENS: I was going to ask you if the work you're doing is in some ways contestable.

MR SMITH: It's a mixture. If it's a government department, we go for full cost recovery, excluding competitive neutrality. If it's outside the government, we go for full competitive neutrality when we're bidding for the work. Whilst we might have a full cost attribution policy, our pricing policy may differ depending upon what we negotiate with the client. So we have a variable pricing structure, depending upon who the client is and what the nature of the work is.

MRS OWENS: But with say - you say the client is not AFFA, but the rural R and D corporation. Would you set a different price for the R and D corporation to AFFA?

MR SMITH: We do, because the R and D corporations, for example, won't pay full, indirect overhead costs. They have a set amount that they are only prepared to pay, and they won't pay any more. So if you want the work - we have to make incoming contributions probably to match what the full cost of that job might be.

MRS OWENS: But what we're saying in our report is that the charging arrangements are meant to in some way reflect the costs of providing the service, and what you're saying is that you've got differential pricing.

MR SMITH: Well, we have had different pricing policies in the past. If we're going to AFFA, for example, we negotiate the project budget with the client, who is one of the divisions within AFFA. In that case, we don't charge any indirect

overheads. It's actually the direct cost of the project, because otherwise we'd be double counting. In terms of another government department, we will normally recover the full cost of providing that particular project.

MRS OWENS: This is maybe a question for AFFA, but if you're purchasing particular work from ABARE or BRS, does that then - and you're having to pay for that - does that then influence your interaction with say a third party that may want some information. If you've had to pay for that information from one of the agencies, then does that mean - and even though it may be a public interest-type, almost a public good, does that mean that AFFA then would feel inclined to charge for that because it has paid for it, or doesn't it work like that?

MR INGHAM: Sorry, I don't really understand the question.

MRS OWENS: Well, it's a matter of supposing - I can't think of an example, but supposing you got some work done by ABARE, you commissioned some work and you got some work done, and it was work that was being done, you know, as part of your responsibilities in the department, and then somebody else came along to you and said, "Well, we're really interested in the results of that work," and you've commissioned ABARE to do it and there has been a transfer of funds, a purchaser provider arrangement, would you feel inclined to charge for that because you've paid for it, or do you just say, "Well, this is part of our - what we've called core, and this is a public good, and we're not going to charge." Does it influence your interaction with a third party that's seeking that information?

MR JONES: I don't know the answer in all cases, but there's a number of examples where for instance AFFA would make a submission to some inquiry, and as part of getting that submission, they might draw on material that they'd got from BRS or ABARE, and that's part of their submission, and it's a public submission, so clearly you don't charge.

MRS OWENS: You can't think of instances where the others would come out?

MR JONES: I can't think of any examples of our area where we would have charged for information we provide.

MRS OWENS: We're just trying to establish principles, you see. If we're developing guidelines which are going to embrace intragovernmental charging, we've got to sort of just think through all the ramifications of doing that, and I think we've always accepted in the past that, you know, it actually can be very positive to have these sorts of arrangements between departments because it provides price signals and potential for demand management and so on. But there's also the potential for maybe some perverse outcomes that we're just trying to work through and see if there are any potential, you know, holes in the argument.

MR JONES: Yes. Well, from the division I'm in - we're in essentially a policy advising area, so we don't charge for our services. But I'll take the question on notice for other parts of AFFA, see if there are other areas that do charge. But other than

the main regulatory agencies and BRS and ABARE, I can't think offhand who that might be. But we'll check if there are exceptions.

MR ROSE: Can I offer a view from the other side?

MRS OWENS: Yes.

MR ROSE: When something that comes up which is a new priority in terms of - either it's new in absolute terms or its priority - on the amount that needs to be spent on it in the department's view, is a priority - is new, and they come to ABARE for advice. Now, whether we can do it or whether we'll be the appropriate organisation to do it or how to do it - their choices, if they want ABARE to do it, are to get us to take something off the program that we've already set, and not to do something that we - preferably something we haven't already devoted some resources to, and do the new work instead.

So there's no cash transfer, it's just something that AFFA thought that it was going to get, it's no longer going to get from us, because it's going to get the new product, or when we discuss that possibility, they might look at it and say, "There's nothing on there that we want sacrificed." There are some other organisations in here who have some interest in there. Why don't the three or more organisations go and discuss this and see if some of the other organisations that have an interest, whether they're government or in some cases private organisation, also have an interest in this, and see if we can find some joint funding arrangements.

But I guess the purchaser provider model across government does put some sharper edges on those choices than existed a few years ago. There's not as much flexibility. It's much - from ABARE's point of view, when somebody asks us, "Can you do this?", the first question we ask is, "Well, have you got money or are you offering something up that we've already got on the program, that you don't want any more or you don't want as much as you want this, or is there somebody else around here who has an interest and should be contributing to it?" Those kinds of questions probably didn't get asked as quickly and in as much detail as before.

MRS OWENS: It sounds like quite a sort of a positive process from your point of view.

MR ROSE: In that sense it is a very positive process, because the policy areas of AFFA, ABARE, if it involve ABARE, and whatever other government or industry agencies there are that have an interest in this, have a very strong incentive to get together and talk about the nature of the work and the likely cost of the work and what the options are to optimise those, and who should be contributing; what the opportunities are.

PROF SLOAN: Well, I mean, it would want to be positive though, because there are transaction costs associated with doing it.

MR ROSE: There are transaction costs, and sometimes they're quite substantial.

PROF SLOAN: Yes.

MRS OWENS: Mr Rose, I asked the question before - we talked a bit about BRS's services in some cases being contestable. Do you have competitors out there that are doing the same sort of work as ABARE, or is what you're doing unique?

PROF SLOAN: That's a leading question.

MRS OWENS: Well, you ask the odd leading question, Judith.

PROF SLOAN: All the time.

MR ROSE: Some of what we do is on a purely contestable basis, and much of the research and development corporation funded research, and some of the research that's funded by AFFA and by ISR and other government departments is purely contestable, and we win that because we can offer the service - generally, we can offer a better service rather than - at a reasonable price, because we carry a few government overheads which, I mean, that we're not very often price competitive, or occasionally because some of the databases that we have, which are individual to ABARE, offer us an advantage because we've already done a mass of work with those, and I'm not talking - - -

PROF SLOAN: Is that fair?

MR ROSE: No, I'm not talking - - -

MRS OWENS: Is this the confidential database?

MR ROSE: Yes. Because we have the expertise in-house to handle it, there are times when it's advantageous for us to do that.

MRS OWENS: If you were a private sector competitor, you might feel a bit miffed by that. There are taxpayers that have allowed you to collect this data which then gives you a competitive advantage, because you're being the gatekeeper of the data.

MR ROSE: I'm not talking about the data giving us an advantage. I'm talking about the fact that in the process of collecting the data, we have expertise in-house and we have systems in-house to handle that, but to pass on that information, to pass on that expertise through a private sector organisation would be at best difficult.

MRS OWENS: Why - because of the confidentiality aspect?

MR ROSE: I'm essentially talking about lessons learned in the process, in using the data. It's not that other people can't do it. It's familiarity with a particular database and with the quirks of the database.

MRS OWENS: But that's a bit like saying the ABS collects all this data so they've

got all this expertise because they have collected this data and really that means that nobody should be out there - there shouldn't be the narrow trades of the world and other organisations which are out there providing a service to clients because there's this body of knowledge within the ABS and it's a bit of a closed shop if you think like that. I would have thought a public sector organisation should be in the business of letting a thousand flowers bloom and let others into the game.

MR ROSE: We are to the extent that we can and I'm not talking about withholding - this is not about withholding expertise and withholding data. It's simply that if you've already collected the information for something and already been through the process of gathering and organising data and you have the contacts with the people who supplied that data, there are some economies if somebody else - at times there are economies if somebody else wants to use other transformations of that data for the organisation that has done that to go ahead and to use it. That's not to say that other people shouldn't be able to or can't use our data, the confidentiality difficulties aside.

MRS OWENS: You don't think that the ABS suffered some considerable collateral damage in terms of its reputation by the policy of cost recovery by accepting private sector money and well, speaking as a member of the economics profession, I think it did because the view is that it undermines the independence of the research and information agency.

MR ROSE: Did being purely government funded undermine our independence before or is it - - -

MRS OWENS: I think it was probably clearer.

MR ROSE: - - - only private sector that - - -

MRS OWENS: I just want you to, you know - I mean, is that not an issue?

MR ROSE: Yes, there is always that risk. There's certainly the risk of the perception.

MRS OWENS: And is there not a management issue at least.

MR ROSE: And there was a serious management issue. I didn't mean to dismiss that. It exists with government, with our primary funding organisations as well.

MRS OWENS: Yes, I agree with that.

MR ROSE: We're acutely aware of that in all of our dealings with all our funding organisations. We have to maintain the intellectual independence and we have to maintain as best we can the appearance of that as well. We're not always as successful as we would like to be in the latter. I think we're pretty successful in maintaining the intellectual independence.

MRS OWENS: No, it just seems to be an issue that might be an implementation issue.

MR ROSE: It's inevitable that it's going to be an issue, yes, and so we - - -

DR STEWARDSON: I was going to say, trying to come back to solving the problem of ABARE and our guidelines, I mean, basically it doesn't seem to me it would be terribly difficult to deal with the DISR and the research development corporation as well as AFFA being the lines by which you get taxpayer funded in terms of our diagrams here and equally at the other extreme there doesn't seem to be all that much problem about fitting conceptually things that you do outside as sort of totally commercial things that are one-off. The problems seems to me to be to defining some of the things that you get on an ad hoc basis if you like. It may be ad hoc in the sense that it might be something that runs for a year or even two years and I presume you would still call it purchaser provided split.

But for example if the Department of Foreign Affairs wants you to do something or the Department of Environment or something, over which there seems to me to be a problem of defining whether that is just sort of yet another government agency being sort of for a while a "master agency" or whether this is an outside organisation for which you are doing some commercial work or building on your existing core of information because how you define those things really in terms of our structure leads to whether it should be taxpayer funded or whether it should be being charged at incremental cost or at commercial prices. That seems to me to be the key problem of fitting ABARE and to an extent also the ABS into - - -

MR SMITH: I think we are in a slightly different situation. If I can just put a little bit of context. Both ABARE and BRS are funded by AFFA. We don't have separate appropriations. So when AFFA gets its budget in negotiation with the secretary and the other program managers, we negotiate what our share of that core - let's use the word "core" at this stage - budget is. As Roger said, we have to vary, depending upon what the priorities of our AFFA program managers are - we have to vary our work to meet what their needs are within that particular budget. I think where we're slightly different from ABARE is that 35 per cent of our workforce is not ongoing so that if a particular project finishes, we then terminate those contracts and if we say for example we're moving into the area of salinity, which we are now doing, we then go and employ people on non-ongoing contracts on salinity.

So we have the flexibility, as our work needs change, to vary our workforce to meet whatever the priority might be at the particular time and as Roger said, we also go into negotiations with people like the Murray-Darling Basin Commission, the state government departments and others when a big project is coming up, to see how we can pool all the funds together to maximise what the returns might be. But we just ask - I think ourselves and AQIS are probably the two areas of the department that have this flexibility of non-ongoing staff which doesn't lock us into the stage of if we actually have a water sign just over here and then we have to go into fisheries for example we can't move from one area to the other. So we're a little bit more flexible I think than probably what our colleagues in ABARE are in that regard.

I just wanted to make the point when you were talking before about direct and indirect costs, that our direct costs are really determined by AFFA and that's what we have to live with and that's why we don't charge them indirect costs because it's the budget just being moved internally around the organisation.

MRS OWENS: Can we change the subject and talk a little bit about AQIS. You might enjoy that.

MR SMITH: Yes, we would, thank you. Judith has been smiling up there.

MR JONES: Just before you move on, if I may go back to a topic we were on earlier, whether AFFA charges for its products to the extent that it has used inputs from various - or ABARE. For a policy area, one of the core functions is providing evidence based advice and information so that the evidence base is the science and economic advice so it's implicit that the policy advice has this underpinning of sound science and economics so you therefore wouldn't be charging just because you happen to have used a particular input from one of these research organisations for a particular piece of advice.

MRS OWENS: Yes, I think that makes sense to me. I'm glad you actually said that because basically you're there doing mainly policy work.

MR JONES: It's a shame that we've got this evidence based advice.

MRS OWENS: I was going to just move on to a couple of issues that you raised up-front in relation to AQIS. One was that - - -

PROF SLOAN: The importer said very nice things about you.

MRS OWENS: That's what I was going to say. We got some very good feedback from - - -

PROF SLOAN: Quite unusual, I'd like to tell you, from user groups.

MRS OWENS: - - - the Industry Cargo Consultative Committee. We were talking about consultation and I think you mentioned the word "model" before and it may not be an appropriate model for elsewhere but we actually thought it sounds like a model that is working extremely well in that particular area and you seemed to have consultation at quite a number of different levels and I think the impression we got was that you do listen to what industry has to say and adjust accordingly and there's a lot of information that goes to industry about the financial arrangements and cost recovery and so on. So I thought in terms of having a reasonably happy client group I think you've done extremely well.

The other point I'd like to make is that you have some reservations about using a cost recovery impact statement and it sounded like you had misunderstood what we were trying to do there. We're basically saying that the regulatory impact statement

arrangements that are in place now don't necessarily fully absorb the cost recovery issues that we are looking at now and if there is going to be cost recovery guidelines we need to make it explicit in that process that those guidelines be used and that in some instances the regulatory impact statement process is just not applicable so that it applies to regulatory impact when there's companies involved but not if there's individuals involved and it doesn't apply obviously for information agencies.

So we felt that we needed to fill this gap with something and we're certainly not trying to imply that there should be duplication processes or we're not trying to bring in something that's going to make things more complex. We're just making sure that these arrangements do appropriately acknowledge the cost recovery aspects and we're also starting to think that in that context there should be more emphasis on consultation during the application of a cost recovery impact statement or regulatory impact statement - consultation with industry.

MR CARLTON: It was that risk of duplication that we were concerned about. We thought perhaps if the regulatory impact statement could be expanded to take in those concerns rather than having two separate processes.

PROF SLOAN: That was the intention.

MRS OWENS: Yes, I think it was just not written as clearly as it could have been so we will take that on board.

DR STEWARDSON: In terms of the regulatory agencies, if we're looking at them, I'd like to ask - and I'm not sure whether you want to answer it centrally from AFFA or from AQIS, but in the executive summary and again in the text where you're talking about cost recovery by regulatory agencies, AFFA is recommending an approach which has an agreed sharing of costs between industry and government based on outcomes of a consultation and a contribution from government which reflects its responsibility for policy development et cetera. Just for clarification, are you proposing at that point that there would be a contribution from government for policy development and that sort of thing and then for the rest of the costs there would be an agreed sharing between industry and government, which is how I read it; or is the government share the policy bit? It's up on the top of page 3.

MR CARLTON: This isn't a specific issue that AQIS raised. I'm not sure which part of the department had raised this for it to be included in this but I guess from an AQIS perspective a lot of this work was done back in 1988 or 89 when the government first made the decision that we would go into 100 per cent cost recovery and there was a memorandum of understanding developed between the Department of Finance representing the government and AQIS on what costs we would recover from industry and which costs that the government would continue to fund and that identified areas such as policy, areas such as the compliance with any investigations and legislation review, those type of things which I think you have picked up in your report as identifying as really supporting the government rather than industry. So from an AQIS perspective I think we've sort of done that in the background to where we are now but perhaps this has come from an area of the department that's looking

at what they were doing in the future.

MR JONES: It is currently an amalgam of views from different areas of the department but the intention I think is that those components would be sort of fair game to the government to pick up and in the agreement with industry you would expect those things to be there. There may be other aspects that are also fair for the government to pick up. In other words, that list is not exclusive.

PROF SLOAN: So it's not saying 100 per cent cost recovery minus the costs of policy development blah, blah, blah. It's actually saying we excise those things and then what the sharing is with the rest of the plot is the bit up for grabs.

DR STEWARDSON: That's what I'm trying to establish, whether that's what the suggestion is.

MR JONES: That would be my interpretation.

MR INGHAM: The sentence before which outlines a flexible approach sort of indicates that it should be the result of a consultation and as a minimum the contribution from government should recover those or pay for those components there - parliamentary requirements, policy developments and international obligations but they may be on top of that depending on consultations and results of those.

MRS OWENS: We found that when we spoke to people at the workshops that this issue of policy development can be a little bit ambiguous because some have said some policy development is really relating to our activities as regulatory agencies and that should be charged back to industry and then there's broader policy developments so even within that there seems to be a little bit of ambiguity. I don't know whether anybody wants to comment but some have said like standard setting, if you're setting standards, that is really setting standards in the context of undertaking regulatory activities. Some say that's something that should be charged to industry and others say standard setting is a policy; it's really undertaking a policy function.

PROF SLOAN: What would the AQIS view be on that? You would regard standard setting as part of the 100 per cent to be cost recovered, wouldn't you?

MR CARLTON: I think it depends that there's an element of policy in standard setting in the operational part of AQIS which is then recovered from industry but the negotiation of international standards and so forth is all in a policy arm which is 100 per cent funded by the government. Like it's big "P," policy is government funded, little "p" policy which is involving most operational areas anyway is seen as being a cost that industry should support.

PROF SLOAN: On the page before that page, I mean, my guess is that it was just sloppy drafting because - I don't know whether I do like the term "user pays" because if you're being compulsorily regulated do you really think of yourself as a user? It's

not exactly like walking into a Myer department store, is it?

MRS OWENS: I suppose they don't think of themselves as beneficiaries either.

PROF SLOAN: But you've got this sentence, "especially in situations where the beneficiary of the activity is uncertain." If the beneficiary of the activity is uncertain the conclusion I draw from it is cease the activity immediately or do you actually mean is hard to identify?

MR CARLTON: I think the definition of a beneficiary depends on where you sit. From my point of view a beneficiary - if we provide services to a meat processor would be the operator or owner of that establishment because without our services they can't commercially do business. So they're the beneficiary. That establishment owner may - is sort of saying, "The beneficiary is really the people who eat my meat and therefore there should be a government contribution," and I think that we have always used the term "user pays" so whoever is using our services would pay for them rather than sort of trying to define who is the beneficiary of the service.

PROF SLOAN: I think we probably part ways on that. We would say that it's best, you know, to define the beneficiary. It's then an issue of cost-effectiveness and feasibility in terms of where you charge in the production chain. But I mean, it seems to me if you can't identify the beneficiary you shouldn't be doing the thing in the first place really.

MR CARLTON: I think we would say we can identify the beneficiary. The person or organisation we have identified as to the beneficiary may not agree that they were the 100 per cent beneficiary of the service. So it's more an interpretation of who is the beneficiary.

MRS OWENS: Although when we talked to your friends yesterday they did seem to acknowledge that the costs recovery was appropriate and in some ways they were benefiting from your activities and I think were quite agreeable to doing that. So I think you come back to this idea of consultation and being able to discuss these issues. I think you do make an important point that sometimes it is complicated and it needs to be considered quite carefully, but I think you can't just leave it as the user pays and just say that's appropriate, because I think what we are trying to do is establish the principles to improve economic efficiency.

PROF SLOAN: The Red Meat Council people weren't quite so kind about you I would like to point out.

MRS OWENS: No, so don't get too excited.

PROF SLOAN: I think if you are talking about exporting meat and meat inspection for export, obviously those exporters cannot enter other markets unless they have gone through this process, because often it's a requirement at the other end that they have gone through that. So they are really the beneficiaries of your services. They are the ones that benefit, because otherwise their meat wouldn't be able to leave the

country. They wouldn't be able to export it.

MR CARLTON: Absolutely, I quite agree with that definition, yes.

PROF SLOAN: So not only are they the users of your services and hence you would charge them as users, but they are also in our terminology the beneficiaries of your services and should be charged. So that one in my mind is reasonably straightforward. They might not agree with me.

But you do say here that the cost recovery arrangements for AFFA regulatory agencies, this is also on page 2 just under that Cost Recovery by Regulatory Agency heading, you say "broadly consistent with the PC's guidelines, recommend it in the draft report". They may be, I mean at the moment you have NRA that has 100 per cent cost recovery target. There is one agency where it may not be broadly consistent, because we are saying there should not be cost recovery targets at all on an agency basis. We are basically arguing that cost recovery should apply to individual activities, rather than to an agency.

MR JONES: We don't have our NRA people to take that question specifically, but in the back of the submission there is a little discussion of the various regulatory agencies and the sense in which they are consistent or not and so we are saying broadly consistent.

PROF SLOAN: I think that's reassuring for us.

MR JONES: You may have pointed to an area where it's not fully consistent.

MRS OWENS: I think that's always a problem when you actually do an executive summary, that you tend to sweep up things that maybe shouldn't be swept up when you are doing it. We have this problem as well. It's often the problem with generalisation.

MR JONES: The general thought was that AFFA was broadly supportive of where you are coming out and in our fold we are roughly consistent with what you are proposing, therefore we are not sort of aghast at it and we are not taking great umbrage that the comments you have in the report about in some cases the system is poorly designed, so we are not taking that as direct criticism of our agencies, we are reasonably comfortable, but it's not to say that we are 100 per cent compliant with your guidelines in every case.

DR STEWARDSON: On page 10 of your submission you talk about our distinction between beneficiary pays and regulated pays. In other words, in our terminology where we are looking at the beneficiary being the consumer of the product that is being approved, or the regulated pays where there is regulation in order to avoid negative spill-over effects from the product and you take the case of the NRA there, which I think is a good example to discuss. But you end up by concluding that paragraph by saying, "It's therefore unclear whether the NRA cost recovery arrangements are to be viewed as regulated pays or beneficiary pays."

We think, we hope that the answer to that question is determined by looking at the aim of the act. What is the act that sets up the NRA trying to do? We think in that case that it's to protect the community from harmful chemicals. But it's quite an important point for our guidelines that one can determine that sort of question. Do you think from your experience that in fact one can answer those questions by looking at the aim of the act and finding a reasonably clear answer?

MR READ: I think the whole proposition of whether you are talking user pay or prime beneficiary pay or beneficiaries pay and in relation to what you have just raised in regulated pays or its contrast as well is a difficult proposition in itself. I mean ultimately I would imagine, particularly in relation to for example red meat exports, that the processing establishments which you would say may well be - if you use the language prime beneficiary and sort of the flow through implications of that cost built into that sort of pricing structure and the ultimate users at the end of the day and the fact that they may or may not be the payers, particularly when in a lot of these intervention processors in the supply chain and the development of product, those costs I think can flow quite easily both ways.

It may well be easy to see that the beneficiary at the end of the day may well be the user, but the costs borne may well be the producer, because by applying a price impost across a particular user group such as processors purchasing cattle for example, as soon as you apply a cost structure or levy, then the resources available for the competition of those cattle reduces and the price subsequently follows on. In other circumstances again and depending on elasticity and inelastic-type product, then it is going to go to the other way. At the end of the day, depending on the type of service provided, it is the definition of who pays that particular price and where that is captured and I guess I'm only reflecting on the export side and clearly that first port of call is a reasonable point to apply that charge.

Whether in fact ultimately they are the beneficiary, that is a definitional issue in my mind to some extent and who wears that cost ultimately is another issue that you could sort of debate through, depending on the commodity and the markets that you are entering with that commodity, whether it is actually the end user or the producer.

MRS OWENS: I mean it could be the end user, but it is going to be very hard for the payer, which would probably be the firm back in Australia to pass that on to the extent you are in a market where it is going to be very hard to pass those costs on. But you could also look at it more broadly and say it's all about developing a reputation of our beef industry and we are not in the situation that they are in Europe and that has regional implications back in Australia and the Australian community benefits maybe. I mean you could - - -

MR READ: I think that's something that is being explored with industry particularly at the moment, in how you deliver the particularly regulatory service and that is something that is continually evolving within AQIS with its client group. I mean, you can always have the sort of cast iron approach of inspectors on plants and

there are costs that go with that, or the third party regulatory evolved model and build your producers into a QA system that flows through the whole chain and the amount of intervention by government to certify that product meets particular sets of requirements in the market becomes significantly less and that intervention cost significantly less. I mean, that would be viewed a number of ways by various participants in the producing and processing industries and that applies to all commodities I suspect.

PROF SLOAN: One of the questions we have asked the user groups is that in the absence of regulation would they engage in some form of self-regulation themselves. Now, the reason to ask that question is that it kind of elicits whether there are private benefits to the producer from some cooperative effort and I think when they say yes, like in fact the red meat producers, they say they would engage in forms of self-regulation, which of course they would have to pay for. So you have a little test going there. But it does worry me a bit that we can be a little disingenuous by saying, "It will float up and down the supply chain, depending on the elasticity, so we will just lump it on the producers," and don't forget that was really the genesis of this inquiry, that the producers got fed up with basically that point of view, that there needs to be some more critical thinking about who are the beneficiaries of regulation before you start necessarily jumping to the conclusion that your users should pay.

MR READ: That's exactly why AQIS has developed over the years this very important consultation process which is - I attended one yesterday that actually was represented by producers and processors and all participants sort of within that supply chain arrangement and all acutely aware of their cost structures and how those have been managed and we are in an ongoing way looking at improving those efficiencies in the delivery of those services.

PROF SLOAN: We seem to have got very sadly ambiguous results and in the case of AQIS it seems that one of the tremendous benefits of the consultation has been to drive greater efficiencies in AQIS and some real industry involvement in the model, in terms of how it's done, the cost and everything. Sadly, we have had instances where that doesn't seem to work at all and there are general dissatisfaction of the efficiency levels of the agencies concerned. So it would be nice to think we could eventually draw some lessons because it seems to me there might be another advantage of charging the producers is that the producers are going to take an interest in the efficiency of the regulator where if you put a five-cent per kilogram levy on rump steak down at the butcher shop people wouldn't even know let alone take any interest in the efficiency of a quarantine service.

MR READ: I think also what should be appreciated is producers at the moment are starting to become more acutely aware of the cost structures of that supply chain, whether it be in the processing area or whether it be government intervention of state and commonwealth and other regulatory sort of overloads in that process and all appreciate that generally it's going up or down and it's rarely sitting with some of the participants in the middle and that they clearly are very motivated to control those costs and where we can work in partnership to produce them. That's clearly a partnership goal that we share at this time.

MR JONES: In that section on page 10 discussing the distinction between regulator pays and beneficiary pays, that's very neat conceptually and there will be cases where it is clear-cut, you know, there's a clear negative externality and this is obviously the way to go; other cases where it's very clear-cut, the beneficiary is obvious and you can charge that person and it's cost efficient to do so and it's very clear-cut, but mostly you'll be in grey areas so the thought here is that over time the traditional user pays system has been used to develop systems. In some cases they're working reasonably well so you're asked the question, "If it ain't broke should we be trying to fix it?" - by moving to different concepts which in practice may not necessarily give better results. The thought with NRA was they have a system of standing back and looking at it. It's not obvious, if you're trying to reverse engineer, to say where the system came from, which track you would have come down.

MRS OWENS: You know, some areas are working reasonably well and others aren't and it's our responsibility to try and get some consistency across agencies.

MR JONES: Yes, we clearly don't know the answer to that question but we're posing it as something that we knew you were looking at and just thought it might bear a bit more looking at.

MRS OWENS: I think that's useful and I think we do acknowledge there is this enormous grey area somewhere in the middle that is not going to be easy to deal with I think operationally, and what we're trying to do is get guidelines which make it easier than it was before for some. Some agencies haven't really thought of it this way at all. They have just imposed charges to get money and we don't think that revenue raising is a sufficient justification. So I think what may be unfortunate about our process is that there are agencies that are working quite well and have done quite well thinking through the issues and they may feel that this is an unnecessary imposition to go through cost recovery impact statements and all the rest of it but we've found a sufficient number of problems out there to say that it is warranted. I think my colleagues - have you finished, Judith?

PROF SLOAN: We're thrilled with the submission. For a department it's - - -

MRS OWENS: Yes, I thought it was a very good submission and I think that the one - we've got a number of issues we still have to think through but as I said before, one of the important issues that we still haven't really pinned down is this intragovernmental charging and we may like to come back, if you don't mind, to ABARE and maybe the BRS on this issue.

MR SMITH: We'd be happy to offer any assistance that you think it will involve.

MRS OWENS: Thank you. Thanks very much for that. Is there anything else that anybody else would like to say or any other input? Thank you everybody for coming. We will now break and we will be resuming at 3 o'clock.

PROF SLOAN: The final participant today is the Department of Finance and Administration. Welcome and thank you for coming. I would like you each to give your name and your positions with DOFA for the transcript.

MR KERWIN: Jim Kerwin, branch manager.

MR JOICE: Vernon Joice, budget officer.

PROF SLOAN: Good, thanks very much. I understand Jim at least wants to make just a few opening remarks and will open it up for discussion.

MR KERWIN: Thank you very much. Just a couple of opening remarks. The first comment would be that Finance supports the proposed cost recovery guidelines. Just as a very quick comment in relation to those however, Finance is of a view that the guidelines ought not to be too prescriptive, but have sufficient information in them for chief executive officers of agencies under their accountabilities which arise out of the FMA Act and the CAC Act, which is the Commonwealth Authorities and Companies Act, in order to be able to have them as a framework within which to operate.

Finance is not of a view that it sees itself as providing the guidelines itself on cost recovery, or the interpretation of those, particularly as time goes by, but that is a matter for chief executive officers to do within their agencies. Finance very deliberately with the formulation of the FMA Act and the CAC Act stepped out of any sort of role in which it may appear to be a micro-manager of these agencies or any agency. However, it does have an interest in ensuring or observing if in fact efficient, effective and ethical behaviour does occur within these particular businesses.

In relation to the cost recovery impact statement, Finance agrees and is of a view that it should be an integral part of the guidelines. Finance's view is that the Office of Regulation Review should assess a CRIS process. In regard to a separate question about quality assurance of things, Finance is of a view that where these proposals incorporate a cost recovery process, it would also be subject to a QA process. This is policy-type questions coming before Finance. As part of the QA process, Finance would include tests for efficiency effectiveness and significant benefits being provided reasonably immediately.

As a final point and this is more to the question of cost recovery being seen as a price and different to the pricing reviews that Finance has an interest in, pricing reviews at their conceptual centre involve examining whether the government is getting value for money in terms of the price that it pays for outputs. Finance would be quite comfortable with pricing review methodology and approach, also incorporating cost recovery, to see whether external parties who are paying prices on the basis of cost recovery are also getting value for money and we can perhaps talk a little bit more about generally.

MRS OWENS: Thank you. I think there are a number of issues that I would like to

explore with you and I think there is the issue of the guidelines themselves. There are some broader issues that we have come across over the last week or so of hearings and some concerns that were raised at the workshops that you attended, at least part of the time, and maybe we could start with the guidelines. That seems a good place to start. You said you would like to ensure that they are not prescriptive and I think quite a few others have said that they would like to see guidelines which act as guidelines and are not prescriptive, but at the same time there is a fine line between that and ensuring that you have guidelines which are sufficiently stringent to ensure that there is a degree of consistency of approach across agencies.

So there is a fine line there and some have actually said that we should be more prescriptive and more definitive about issues like how do you undertake costing and providing guidance on costings. So that was one point. I know in our report we suggested perhaps the ongoing responsibility for improving and refining the guidelines should rest with your department, but I think you have some reluctance in actually having that sort of role. If DOFA doesn't do it, who should bear that responsibility?

MR JOICE: I consider that this is something that could rest quite comfortably with the Office of Regulation Review. Cost recovery guidelines I think in many respects would be similar to the regulatory impact arrangements that currently exist, particularly as this is something that impacts on the private sector. It is not government users, it is third party users of services. They have established processes in place, they are highly experienced in this area and I think they would be seen as being not only in a position to undertake the assessment of processes, but as being possibly more independent.

Finance, in doing its QA process of proposals which incorporate the cost recovery process, is actually I suppose voicing an opinion. If it is voicing an opinion, but is also seen to be I suppose the arbiter of the rules, there could be seen to be some conflicts. It is worth noting that with the pricing review process, that there has been greater responsibility placed on agencies for the conduct of those processes as well. So I think the Office of Regulatory Review is certainly well placed to both do the assessments and distribute the guidelines.

MRS OWENS: I suppose there are a couple of problems I can think of. One is it's an office of regulative review relating to regulation and our guidelines are meant to also cover information agencies. So it's sort of going beyond where the Office of Regulation Review is currently sitting. So it would have to change its face and its responsibilities would have to be changed to incorporate this. I wonder about whether given DOFA's responsibilities in relation to quality assuring policy proposals and pricing reviews, whether this doesn't fit neatly with those other responsibilities that you have. I guess it raises in my mind what is the responsibility of a Department of Finance and Administration in our administrative structure.

MR JOICE: If I answer the first component first about the difference between, say, information agencies and regulatory agencies, while if we are taking a strict interpretation with this on is regulation and that one is information, there may be

differences. But we are looking at the impact for the purchasers of their services, whether it is a regulatory agency without naming anywhere, you are saying, "You have to do this process and here is the fee for it", or if we have someone, for example ABS, where they are providing information. That still has a similar impact on the private sector users. Particularly with ABS quite often there isn't any alternative sources of that information. I am seeing that the role of the Office of Regulatory Review has been the impact of regulation and taking regulation with a broad interpretation of government activity on the private sector.

MR KERWIN: Can I just follow this through in a bit of a practical sense about how the whole system might work. A scenario that could develop would be that the Office of Regulatory Review would be the first point of review in relation to a cost recovery matter. Where Finance comes to have a role in this would be in relation to that cost recovery being reviewed and probably once every three years in regard to whether it was still an appropriate price to be paid by an external party for services provided by government.

In assessing whether it's an appropriate price, the guidelines would be quite relevant in relation to that. The type of review that Finance would hope to become involved in would be in conjunction with the agency and with the agency driving the matter particularly, Finance would form a view whether on the one hand the prices being paid by government were appropriate in the sense that they were somewhat near benchmarked prices or costs. In relation to where third parties were paying for things provided by government, either under regulation or in relation to information, the process of price review would also pull those in. But the framework which would be used by Finance and the agency within this review would be the framework of the guidelines. I would suspect if the guidelines needed to be altered, then the office of regulatory review would do that.

So I would think in the first instance initially the Office of Regulatory Review would look at the proposal and say yes or no or pass some comment on them. The matter to be charged then to the community, either under a regulation or because it was a provision of information for instance, would then proceed and then Finance by virtue of probably once in every three years looking at the major agencies would be most likely to pick up certainly the significant cost recovery of the matters.

MRS OWENS: I can see you have been involved in what we have called the ongoing monitoring part of the process.

MR KERWIN: Yes, we would be.

MRS OWENS: There is the issue of what I think Vernon said before, that the Office of Regulation Review looks at the impact on the private sector. What we haven't got in the guidelines at the moment is appropriate coverage of intragovernmental cost recovery. We haven't picked that up yet, but we intend to do so for the final report. How does that fit into your framework?

MR KERWIN: I think that would certainly still fit in within the framework of a

reviewer of these things.

MRS OWENS: That would be within pricing reviews?

MR KERWIN: Yes, it would. I mean the pricing reviews would take on the particular tone of looking at what government pays and then separately looking at what is being asked for others to pay. So there would be the budget-funded side looked at and then there would be the non-budget-funded side looked at. You are right, some of those revenue streams on those cost recoveries could come from within government.

MRS OWENS: We actually had quite a few tasks for Finance which you may not want to pick up, but another one was the suggestion we had that within five years all the existing cost recovery arrangements would be reviewed and we had suggested in our implementation chapter that perhaps your department would develop a timetable and prioritise these reviews. Do you have a view about that, whether you want to do that?

MR KERWIN: In a practical sense we will probably get around the major agencies once every three years. What we would look to do within that framework would be to target in some instances where we saw strategic advantage to the Commonwealth. So if there was a necessity for us or we had a belief that it would be useful for the Commonwealth to look at some particular portfolio, then we would do that. So in a sense there is a time-driven process going on here, but it is also event driven as well. There could be events which would emerge that would change our thinking.

MRS OWENS: But I think in the context of these initial reviews we are actually saying let's apply this cost recovery impact statement and this is actually bigger than just looking at the prices; it is actually looking at the underlying rationale for doing it and so on. Does that quite fit with that, or maybe we are talking about doing something a bit different early on.

MR KERWIN: If I can just reflect back what I believe is being asked. There would be quite a lot of cost recovery occurring from within the public service at the moment. An initial step would be to do an assessment of those within the guidelines and whether Finance would be involved in those or not. The initial reaction to that would be that it doesn't particularly fall within Finance's brief to do that. It probably goes with the office of regulation once again but I don't particularly have an answer about how that might work quite effectively.

MRS OWENS: So possibly those initial reviews and existing arrangements would be with the Office of Regulation and Review because that's basically - they will have the same sort of role as looking at new cost recovery arrangements which you're saying should rest with the Office of Regulation and Review but then you would have the ongoing responsibility as part of your pricing reviews to ensure that the pricing arrangements are consistent with the guidelines on an ongoing - so there's a one-off thing that has to be done and then there's an ongoing process that we need to think about. I'm just trying to clarify that in my head.

MR KERWIN: If we looked at it as a process that might happen over a period of say three years, we probably would be doing our initial - and just the Office of Regulation and Review were not part of starting the process. Just say that the use of that particular body was to do new cost recovery arrangements. In order to pick up on the ones that currently already exist, the pricing review process will do that but it will probably take three years for it to actually get to an end. The driver for doing a review is particularly a driver which looks at whether government is getting value for money from the price of outputs.

If there was however a particular instance where there was evidence that the community was being significantly affected by seeing appropriate cost recovery methodologies, I suspect there would be nothing to stop Finance having a look at that, but as a general rule I think we would proceed on our course in relation to cost recovery of our major agencies - sorry, the pricing review of our major agencies but with the flexibility to have a look at a particular area if that was considered to be necessary. So if there are adverse findings in the report, maybe that's something we could have a look at.

DR STEWARDSON: I got a bit confused at some stage in this discussion. In terms of providing the guidelines on cost recovery, in a very broad sense basically that's our job. What we saw as needing to be done when we, for better or worse, had finished, was some greater degree of specificity and, for example, but only as one example, things like guidance to agencies on how they should value fixed assets for depreciation purposes for cost recovery and a whole lot of fairly specific things like that and we were suggesting that that sort of specific guidance for implementation of the broad guidelines would come from DOFA. I understood in what you said initially, Jim, that you were saying that was something not for DOFA but for the CEOs of each agency but then I understood what you said Bernard, that you were suggesting that it was a matter for the ORR. So I'm a little confused by the responses.

MR KERWIN: If I can just respond to that. Finance has an obligation to people who read Finance and other APS business financial reports to ensure that there is some level of consistency across the APS. So in relation to say asset valuation, Finance will definitely be issuing guidance outside of the professional standards if it's required in order to cover doubt where doubt may arise and we are in fact in the process of starting to formulate almost monthly or quarterly type accounting framework type guidance for agencies in order to do that. So I suspect we will naturally cover that because of our role around - making sure that when we do a set of consolidated statements for the Commonwealth we are in fact adding up similar sorts of figures, figures on similar conceptual foundations. So I suspect we will cover that.

The thought that I had in my mind when I made the comment was that Finance in terms of operating within a framework where CEOs really are accountable for efficient, effective and ethical behaviour of their businesses - Finance has to be very careful that it doesn't take on a role that it probably did have a few years ago and that

was a role which in a sense micro-managed some of these agencies. As a central finance function, Finance is interested in having accountabilities exercised by people who should be exercising them and transparency around the exercise of those accountabilities. So at the end of the day when financial reports are issued, when people appear before senate estimates and other sorts of scrutiny that happen of APS businesses, Finance is quite comfortable that these sorts of mechanisms for transparency and scrutiny will get to the nub of quality of management and other issues like that rather than Finance as it did some years ago, being the recipient basically of all government transactions and doing separate analysis of particular agencies.

So when it comes to the question of guidelines then, Finance is quite comfortable with guidelines existing but there would be an expectation that CEOs with proper will would be looking to implement those guidelines into their organisations and they would be the ones who would be making the judgments about interpretation, rather than Finance being asked, probably on a repeated basis, to interpret what the guidelines might mean. So it takes out levels of bureaucracy and probably reinforces the notion of accountability.

DR STEWARDSON: Apart from the financial definitions, how would we get consistency of interpretation of the guidelines at a detailed level?

MR KERWIN: You probably could never guarantee that under either model. One of the things that happens I think in regard to business and human behaviour is when you look to do that you get increasing levels of questioning and increasing levels of refinement until you probably get a system that is not greatly working. So I would suspect the guidelines will provide sufficient information to affect behaviour and guidelines which are interpreted and deployed by CEOs with proper will, will also deliver the sort of behaviour that the commission might be looking for.

MRS OWENS: I presume if you do these rolling reviews every three years and the pricing reviews, some of that issue about judging the interpretation of the guidelines would pop up under those pricing reviews. Would that be correct?

MR KERWIN: It would do for sure and if we follow the logic of that through, the process Finance would ideally look to be involved in would be sitting down with senior members, executive members of these particular APS businesses and through a staged, through a disciplined process, reviewing those sorts of matters. There would be a report that would come out of that and the report would identify, just say there was abhorrent type behaviour for instance. In the event that that report came out that way, there would be a report then to the expenditure review committee annually. This occurs annually as part of the budget process and it would say for instance in a worst case scenario that there was evidence within this particular organisation of cost recovery being done outside the guidelines with the particular consequences that that might mean, like overcharging, for instance.

MRS OWENS: So you do the reports now to the expenditure review committee on the outcomes of your pricing reviews?

MR KERWIN: Yes, we do.

MRS OWENS: Do you have any consultation with industry or with other users of agency services when you're doing these reviews?

MR KERWIN: We have done. One of the agencies who have had a pricing review in the last expenditure review committee was the ACCC and on that occasion we did go back to industry and we did have levels of consultation and I think generally we took away from that probably a principle that it's very useful to continue to do this.

MRS OWENS: This is one of the things I think that we have picked up very strongly in these hearings, that industry is saying that they want these processes to be transparent and that they want to be consulted where it's appropriate. I think in our final report we will be saying more about involving industry - at least when cost recovery impact statement process is going on but possibly in this context as well.

MR KERWIN: You could also do it at the pricing review stage as well I would think.

MRS OWENS: Yes. So you would be quite happy to see that happen?

MR KERWIN: Yes, we would.

MRS OWENS: Okay. But what we're really saying is, it's really a fairly significant change in the way you're conducting your pricing reviews now, isn't it? We're actually saying the process may have to change a bit to embrace more consultation and that the subject matter of those reviews may have to change a wee bit as well. Are we still going to call these pricing reviews or are they going to be called something else?

MR KERWIN: No, I think we would continue to call them pricing reviews because on the one hand we'll be dealing with prices paid by government and that's where they have got their name from to date but on the other hand we would be dealing with prices paid by parties who could be other than government or could be other than government agencies. In terms of the additional work, I don't see a lot of additional work in relation to how we are structuring the pricing reviews nowadays. We're putting quite a lot of onus back onto the particular businesses to conduct them. Finance is no longer part of any lower level participation but is part of the higher level review of the evidence that comes forward about the prices. In regard to the question on third parties and levels of independence that you might need in terms of the information being able to come back from them, we would look to make sure that when this steering committee or whatever it is looking at the pricing reviews receive that information that there was evidence that it was able to be given without any sort of suspicion of duress.

DR STEWARDSON: So the cost recovery review process really can be subsumed if you like within the pricing review process without any sort of significant problem?

MR KERWIN: I would think so. I mean, one of the benefits that would come out of this would be that it would bring the cost recovery policy of the agency to the attention of its executive if it isn't already there and ultimately to the sign-off by the chief executive officer.

DR STEWARDSON: The intermediate point in your draft, in your comment, "quality assuring new policy proposals", and you've suggested that where new policy proposals incorporate a cost recovery process, then as part of the quality assuring of the new policy proposals that cost recovery would be subject to quality assuring. I'm not quite clear what that means in your terminology. Can you explain that to me please and how it relates to or differs from the CRIS process for a new - - -

MRS OWENS: I'll just add to that. To me it just looks like if you keep the CRIS process back in say the Office of Regulation Review with a broader remit, isn't there some sort of overlap there with your quality assurance process.

MR KERWIN: Okay. If I might just make a comment, Vernon, on the quality assurance process generally - and Vernon might make a comment on the Office of Regulation Review. When a new policy item comes to finance one of the obligations on behalf of government, it has to review what it calls the costings. That means looking at what an agency believes this overall thing is going to cost, looking at the assumptions that have gone into that, whether they're realistic, whether they're whatever they happen to be. The other part of the process that Finance also looks at is to raise questions - and for the benefit of the Finance Minister - about whether this particular proposal fits genuinely with the notion of sustainable government finances, which is the question that finance needs to consider. An agency may be coming forward with something which will have a social impact. Finance will review it from the point of view of whether its financial impacts to the government's bottom line are appropriate given the other results that are expected from them.

So if in fact a policy came along that had questions about how immediate the effects were going to be, if the effects of the investment of $100 million might be 10 years out and if the effects were going to be insignificant, if it's a very clear case, Finance, regardless of social consequences or possible social consequences would probably advise against it. So hypothetically that's what Finance does and can do from time to time. Incorporating the review for cost recovery type things into this, I might just let Vernon make a comment on that.

MRS OWENS: Just before we get on to Vernon, this raises a really interesting question about our whole report and having a set of guidelines and whether you would look at this whole document as part of this QA process and look at the implications that this would have for sustainable finances and the social impact. By applying these guidelines you could go either way, but it potentially could mean that some of these agencies would be actually collecting less revenue from outside sources and so it could have an impact back onto government finances.

MR KERWIN: Could be.

MRS OWENS: Some of the agencies have actually said that to us, because in trying to run through our guidelines they've said, "If we did this, this could actually mean that we will have less revenue," and I don't think we're going to get that from the Department of Finance. But would you go through this sort of QA process when you got this final report?

MR KERWIN: What the report may do for us is to give us a framework that could assist. The questions before Finance at the moment, or the questions that could be before Finance in relation to cost recovery, is the question of whether the discretion to cost recover has been one properly made, in the sense that if the motivation was to go outside of pressures that were coming from budget funding - meaning that, whatever is occurring within the APS, if there were less resources being made available by the government of the day to do some particular thing, maybe it's inappropriate then to have cost recovery on that particular thing to make sure it continues to get done. So that sort of scrutiny would certainly come from Finance. That would be part of the policy considerations. So if the cost recovery was a mechanism to have policy outside of what might be considered appropriate, we would certainly be making a comment on that.

MRS OWENS: Sorry, I interrupted. You were going to hand over to Vernon.

MR JOICE: Two issues: the first one on the role of the Office of Regulatory Review. Currently when we get a new policy proposal, that new policy in most instances will include a RIS anyway, and in doing our QA that's one of the things that we look at. It spells out the impact and quite often the cost to third parties. So in making our assessment of the costings provided by an agency the RIS is taken into account. In instances where we may disagree for some reasons, we will go back to the agency and try and resolve that inconsistency. Generally for proposals to go forward they're required to have agreed costings; in other words, we and the agency agree on how the costings are made.

DR STEWARDSON: So the RIS which we are suggesting should always talk about the cost recovery program associated with the new policy, which as I understand a RIS should do anyway, but it seems to be more honoured in the breach than the observance.

MR JOICE: We would see the CRIS as forming part of it. It's providing, if you go through the steps, why, how, so on and so forth. That to us would be subject to that QA process.

DR STEWARDSON: So what else would the QA process involve other than examining a RIS, including the cost recovery things, as it properly should do?

MR JOICE: The QA process also involves us then providing advice to the minister and to the government, as Jim said before, on the sustainable finances and the impact on the bottom line, and as to whether it is appropriate policy or not.

DR STEWARDSON: So the ORR really checks that they've done their RIS properly and then you take it and draw out the implications for the whole of government of the RIS and advise the minister accordingly. Is that about the size of it?

MR JOICE: I think that's quite a reasonable comment on it.

MR KERWIN: Can I just make a comment on pricing reviews just to put them into some sort of context. Pricing reviews don't always mean a reduction in the revenue being made available to an agency to conduct their business. Pricing reviews are an opportunity to do a whole range of things, and bearing in mind that the APS has only come into an accrual-based measurement framework within the last two years or three years, the cash base world has brought with it a legacy of a number of things. Asset maintenance, for instance, has not had the benefit of appropriate signals through a balance sheet or through an operating statement that maybe you would get out of an accrual based system.

So pricing reviews have a capacity to get to things within the nature of the organisation that may need addressing. They also get to the question of whether additional or the same or lesser quantities of things are really being requested by government and, as a result of that, the end result of a pricing review is not predetermined. The end result of a pricing review is, after it gets through the expenditure review committee, that the government as part of its budgetary process agrees to do or not to do certain things.

So when we come to the question of if the guidelines actually reduce the level of revenue that's coming from another source, there is nothing wrong with the pricing review to highlight that, because at the end of the day the government of the day wants to make sure that the impact back on the community is not unreasonable, and if in fact the government of the day wants to proceed down a particular path, then it may come to the party with additional resourcing to do that. So once again we'd look for transparency to draw these things out.

MRS OWENS: I think if any of the issues has caused the most heat, this one probably has. There is a nervousness out there among some agencies that, if they did follow the guidelines, it may show that they should actually be not cost recovering for particular activities. They're concerned that they'll lose that revenue. So you could actually set up a barrier for the successful implementation of these guidelines, and there's an assumption that they'll automatically lose the revenue and they'll be worse off and they then will be in a position where they can't do as much as they were doing before. So they paint the worst case scenario, if you like, but what you're saying is that that's not really an automatic thing that's going to happen.

MR KERWIN: It's not an automatic thing, no, but it will, however, before a decision is made get scrutiny from a number of quarters, so people participating in it will need to still come forward and maybe really very uncomfortable within a framework of this type of scrutiny, but there isn't a knee-jerk reaction from Finance which basically says, "You will not get the additional resourcing."

MRS OWENS: There's the short-term issue about budget funding. There's the bigger issue about trying to get the cost recovery arrangements working in a way which improved economic efficiency, in which case it may in the longer term mean that it's not going to have additional pull on the resources, if indeed that was the way it was to go, if you can get the incentives in place so that economic efficiency is improved.

DR STEWARDSON: One of the things that a number of agencies, departments, have said to us - you may have said it yourself; I don't remember - is that we haven't adequately addressed intergovernment payments, payments to an agency by other government agencies or other government departments. I think that's a fair criticism, and we want to address it in general terms, and in fairly specific terms it's a most important issue for ABARE, which has, as it were, about three parent departments. It's located within AFFA but it gets a lot of government funding via at least two other government departments, and also on a more ad hoc basis from other departments from time to time. Do you have any comments or advice for us about how we should be handling these intergovernment payments, in general and/or specifically in the case of an agency like ABARE?

MR KERWIN: I'll just make a general comment. If there's anything going on here by way of a deliberate dynamic, I think it's very much to do with one department having some level of control about the quantity of service that's being demanded. The process then follows that the party which is demanding the product has the budget and then pays a price an then you get a transfer of revenue over to the other party so it can pay its way. So I think there's a model which is being used here which is fairly deliberate, with the intention of having some level of assurance that the demand from one area in fact regulates the quantities that are being provided by the other area, and I'm not too sure how effectively that works because I just don't have the information. But I suspect that it would be more effective than the alternative, which is to put the budget into the agency doing the work and producing the outputs and then having those provided to whichever department needed them.

I think there has been over time evidence, not only in the federal public service but in others, that that sort of arrangement leads to the party providing being the determinant of what is and what ought to be demanded rather than the agency or the business which has the demand for the products or services. So I think that's sort of process or that sort of model is in operation.

DR STEWARDSON: Okay. But then, for example, how do we cope with - and let's go away from ABARE - say the ABS gets a certain budget allocation to do a certain quantum of output which presumably at least in its pricing review it stipulates what that is and it may be every budget submission or it may be a more general thing in the annual budget submission and then another government department or a government department decides that it really does need to have something extra and it is prepared to pay for it, something which maybe given time would be incorporated within the ABS's own budget, but isn't at the moment, someone has just thought of it. How do we handle that sort of issue? What sort of payment is that payment from the

other government department? Is it part of the core as we define it, is it the public good, or is it more by way of a commercial payment like anybody might go onto the ABS?

MR KERWIN: I'm not too sure of the answer to that, because I am not too sure of core and non-core. But once again what in reality could be happening here is that a particular department has a need for a service that the ABS can provide. The assumption is that the ABS is not resourced by government to provide that service and therefore the ABS either directly or as a broker to bring in resources from outside - that can also happen - provides the service and provides it on a cost recovery basis, or acts in a consultancy-type arrangement.

At a point in time - and if we reflect back to the earlier submission we made, this is a question of the section 31-type revenue streams that come along and section 31 probably has an underlying conceptual basis that says there is a type of work involved in a particular agency and there are revenue streams that come from government to provide that. If you get revenue streams outside of that and if you get them up to some particular amount, well, that remains available to you as a department. If you have them outside of that particular amount, then a question arises and a threshold is reached within Finance where a question can be raised about whether it ought to continue and whether it ought to continue as being a core part of that business.

Because cost recovery-type arrangements at a particular level can have the potential to change or to increase or to alter at the margin the type of work that an agency might do. That is a question for government to answer and not a question for a CEO to answer. So in terms of the practicalities of observing and managing that, scrutiny doesn't happen as soon as some of that behaviour exhibits itself. Scrutiny happens when the behaviour gets to a particular level. So that's probably the fundamental question there.

MRS OWENS: We were a bit concerned I think and it is recognised in your report that there are different levels of scrutiny, depending on whether there are section 31 arrangements in place or not. I think when we met with you earlier, a few weeks ago, you said that you agreed that all agencies should be subject to the same degree of scrutiny. I think that was one of our recommendations. Do you still maintain that's appropriate? There is this feeling with agencies earning the money that they keep some of that money and even if they hand it over to you it reduces the amount of scrutiny that you have of that agency. It may be the wrong impression that we have got.

MR KERWIN: The scrutiny that Finance would hope to apply to the financial conduct of agencies can be driven by time constraints or by time drivers, something like pricing reviews and we would hope to get around to the major agencies once every three years, which is our present plan. However, we are quite happy to intervene in that timetable if in fact there are events that would in a practical sense or just in a result for effort-type sense, cause us to go somewhere else. So the level of scrutiny - scrutiny will occur at a particular level, which is not at too low a level. It

ought to occur at a level where there is some question about whether at the margin the nature of the business is changing or going in a direction that government hasn't yet approved and the section 31 arrangements allow us to do that. I don't have a particular answer for your question, because it probably represents behaviour or examples at too low a level for us to even pick up. I mean, we are talking in millions of dollars here when we say the revenue streams.

MRS OWENS: Another issue that we faced when we were doing this inquiry was the difficulty we had in actually getting information of that cost recovery revenue and cost recovery arrangements, both through annual reports and budget papers and so on and we made I think a fairly strong plea for that to be rectified. Have you got any concerns with that recommendation?

MR KERWIN: I don't think so. I think what we would need to put our minds to, once again with not an enormous amount of detail coming into it, but with sufficient information coming out of our financial systems to be helpful for scrutiny and review and transparency would be looking at the chart of accounts. The chart of accounts at the moment provides some level of information, but it may be useful to have additional lines in the chart in relation to cost recovery-type revenue or section 31-type revenues, so it is easier to see where these are coming from and that would not cost too much at all. It would be a matter of increasing the number of lines in the chart and then having agencies putting information in there, so that wouldn't be a problem.

MRS OWENS: Presumably the agency should be able to supply this information, particularly if they are having to justify what they are doing to you or through the CRIS process or whatever, they are going to have to monitor it. It is a matter of putting that information into the public domain in a useable form.

MR KERWIN: If we bring the sort of dynamics into play that we are talking about and that is the initial necessity to get it through the Office of Regulation Review and then the periodic review by Finance within those guidelines within the pricing review framework, then that sort of information just necessarily has to be there.

DR STEWARDSON: Given that our inquiry has highlighted the fact that the information doesn't exist in that way at the moment, is this not something that you would be resolving to do anyway as an outcome of that realisation?

MR KERWIN: I think it would be, yes.

MRS OWENS: Thank you very much for that. I think we all did very well and I thought it was an interesting discussion. Is there anything else, Vernon or Jim, you would like to raise with us before we finish today.

MR JOICE: The only thing I would like to raise is it was mentioned that there isn't a lot of information there at times. I think this is the very reason why we need this framework, so that these cost recovery processes are open to scrutiny and with that greater scrutiny I think we will have greater consistency of the arrangements. It

tends to bring everyone into line.

MRS OWENS: Good. Thank you very much. I think we will now close today's proceedings and this round of hearings and I don't think there is anybody else in the audience that may want to say something, so I now close the hearings and we will be presented a final report to government in mid-August. Thank you.

AT 3.55 PM THE INQUIRY WAS ADJOURNED ACCORDINGLY

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