



Department of  
**AGRICULTURE  
FISHERIES &  
FORESTRY -  
AUSTRALIA**



Mrs Helen Owens  
Presiding Commissioner  
Productivity Commission  
LB2 Collins Street East  
Melbourne VIC 8003

14 June 2001

Dear Commissioner

Please find attached the submission from the Department of Agriculture, Fisheries and Forestry - Australia (AFFA) to the Productivity Commission's Inquiry into Cost Recovery.

The Department appreciates the opportunity to make a submission to the inquiry. This second submission includes input from AFFA portfolio areas with cost recovered activities, including the Product Integrity and Animal and Plant Health Business Group and the Levies and Revenue Service as well as the following portfolio agencies:

- Australian Bureau of Agricultural and Resource Economics (ABARE);
- Bureau of Rural Sciences (BRS);
- National Registration Authority for Agricultural and Veterinary Chemicals (NRA);
- Australian Quarantine and Inspection Service (AQIS); and
- Plant Breeders Rights Office (PBRO).

We look forward to having the opportunity to attend the hearing on Friday 15 June 2001. I have notified Marie Conti of your office as to who will be attending from this Department.

The contact officer for this Inquiry is David Ingham who can be contacted on (02) 6272 5883.

Yours sincerely



**Centenary of Federation**

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Department of  
**AGRICULTURE  
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Second Submission to the

Productivity Commission

Review of cost recovery

14 June 2001

## **Executive Summary**

This submission to the Productivity Commission includes input from AFFA portfolio areas with cost recovered activities, including the Product Integrity and Animal and Plant Health Business Group and the Levies and Revenue Service as well as the following portfolio agencies:

- Australian Bureau of Agricultural and Resource Economics (ABARE);
- Bureau of Rural Sciences (BRS);
- National Registration Authority for Agricultural and Veterinary Chemicals (NRA);
- Australian Quarantine and Inspection Service (AQIS); and
- Plant Breeders Rights Office (PBRO).

The following is a summary of the main issues raised by AFFA and its agencies in the Submission, including some recommendations on issues the Productivity Commission (PC) might consider in completing its final report on cost recovery.

### **Cost Recovery by Information Agencies**

- The PC recommends that information agencies need to make greater use of public funding to remove distortions created by cost recovery measures. In arguing for a move to public funding, account needs to be taken of the relative distortions created by revenue collection by means other than cost recovery. This should include the possible reductions in distortions that may occur from charging for a service previously provided at no cost.
- The distinction between ‘core’ and ‘non-core’ activities is often not clear. There will be circumstances when partial cost recovery is a reasonable arrangement.
- Accountability for expenditure of public funds is often best achieved through a ‘purchaser-provider’ model, where some agencies are funded through cost recovery from other government agencies for a portion of their core activities. The PC may wish to examine more closely the implications of intra-governmental transfers for the design of cost recovery arrangements.

### **Cost Recovery by Regulatory Agencies**

- AFFA agrees that there is a need to have cost recovery guidelines in place for government agencies, and notes that the cost recovery arrangements for AFFA regulatory agencies are broadly consistent with the PC’s guidelines recommended in the Draft Report.
- As Cabinet mostly makes decisions about cost recovery arrangements, agencies have limited or no flexibility on whether to adopt cost recovery for their activities.
  - In view of this, AFFA believes the effectiveness of the final report as a practical guide for agencies would be enhanced if relatively more emphasis were given to those parts of the PC’s guidelines which covered implementation, monitoring and review of cost recovery arrangements and less to design of the arrangements.
- Regulatory changes are sometimes driven by demands from industry. In these situations, the additional costs associated with implementing such changes should be borne by industry.
- There are often difficulties in distinguishing between those ‘regulated’ and the ‘beneficiaries’ of a regulatory activity, which create practical problems in using the distinction between ‘regulated-pays’ and ‘beneficiary-pays’ as a basis for cost recovery systems. The PC may wish to consider further to what extent user pays (as opposed to the ‘beneficiary/regulated-pays’ distinction) provides an appropriate basis for cost recovery arrangements. In the light of these practical problems (especially in situations where the beneficiary of the activity is uncertain, and/or where the ultimate incidence of the charge is shared between different parties in the production chain), AFFA recommends a more flexible approach to cost recovery involving:

- an agreed sharing of costs between industry and Government, based on the outcomes of effective consultation, and endorsed by industry; and
- a contribution from Government which reflect its responsibility for policy development, Parliamentary requirements, and international obligations.
- In certain circumstances, a temporary over-recovery of costs may be appropriate to smooth fluctuations in the level of fees, on the condition that the funds are eventually returned to industry.
- AFFA disagrees with the proposed Cost Recovery Impact Statement, as it is likely to duplicate other processes, particularly for regulatory agencies which are required to develop a Regulatory Impact Statement for activities that involve cost recovery.

## **Other Issues**

- Industry consultation is very important for AFFA and its agencies, with such consultation considered an important step in the development and review of cost recovery arrangements. The guidelines for consultation need to reflect a requirement for the involvement of industry bodies as those groups will pay the fees and charges.
- AFFA agencies currently undergo a number of rigorous reviews of their activities, including their cost recovered activities. In light of this, AFFA supports the principle of reviewing cost recovery arrangements but has concerns that this should not duplicate reviews that are presently conducted on a regular basis.

## **1. Introduction**

The Department of Agriculture, Fisheries and Forestry – Australia (AFFA) welcomes the Productivity Commission's (PC's) Draft Report on cost recovery in the light of the current lack of a clearly enunciated and consistent policy framework for Commonwealth agencies. AFFA's second submission supplements the comments provided in its first submission sent to the PC in November 2000. Separate submissions were provided at that time to the Productivity Commission by Australian Bureau of Agricultural and Resource Economics (ABARE) and the National Registration Authority for Agricultural and Veterinary Chemicals (NRA).

This second AFFA submission to the PC includes input from AFFA portfolio areas with cost recovered activities, including the Product Integrity and Animal and Plant Health Business Group and the Levies and Revenue Service as well as the following portfolio agencies:

- ABARE
- Bureau of Rural Sciences (BRS)
- NRA
- Australian Quarantine and Inspection Service (AQIS)
- Plant Breeders Rights Office (PBRO).

This Submission is arranged in four sections. Section 2 provides comments addressing the PC's recommendations relating to cost recovery for information agencies. Section 3 provides comments addressing the PC's recommendations relating to cost recovery for regulatory agencies. Section 4 deals with a number of residual cost recovery issues raised by the PC in its Draft Report.

## 2. **Cost Recovery for Information Agencies**

The PC describes information agencies as those whose prime purpose is the collection, compilation and dissemination of information. Under this description, the AFFA agencies **ABARE** and **BRS** would be classified as information agencies. Although some activities of other areas of AFFA, and other AFFA agencies would have activities that fall within this description, these activities would not constitute the “prime purpose” of the agencies that undertook the activities.

### 2.1 *Distortionary effects of cost recovery*

An issue which the PC mentions in its Draft Report (Chapter 2 and page 114), which AFFA believes needs to be given more prominence relates to the distortionary effects of cost recovery. It is important to recognise that in the vast majority of situations, revenue raising will be an important objective of cost recovery arrangements and if cost recovery is not pursued then a substitute source of revenue will be needed. If the activity is funded from the Budget then the distortionary effects of raising revenue through general taxation will need to be assessed against the distortionary effects of the cost recovery activity - that is, the “relative” distortionary effects need to be assessed rather than the “absolute” distortionary effects. When cost recovery is through charges on users of a service, the distortion will often be significantly less than that resulting from a general taxation of non-users. Indeed, charging for a service previously provided for free could be seen as correcting and existing distortion.

AFFA believes that the PC needs to give more prominence in its report to the economy-wide effects of transferring the revenue source from cost recovery to general taxation.

### 2.2 *Core and non-core activities*

The PC recommends that information agencies carefully define core and non-core activities, but recognises the difficulty of defining the boundary. It suggests that core activities should be wholly Budget funded and provided free of charge. The PC justifies this, in part, by indicating that basic statistical data about the economy helps to create an informed and prepared community, and contributes to a well functioning democracy.

AFFA is concerned about the practical difficulties of the core versus non-core dichotomy – which drives the PC’s recommendations on cost recovery for information agencies. Most AFFA agencies would see core activities as being those which are of sufficient importance to be considered as central to the work of the agency. The concept of equity and access to information also needs to be considered in defining core activities. This may or may not be consistent with the PC’s test for ‘core’, which is based on whether the information has the public good characteristics of non-rivalness in consumption and non-excludability. AFFA notes that the fact that cost recovery is possible at all would mean that these activities have at least some excludability and therefore are not pure public goods.

Nevertheless, if the PC’s concept of a core activity is used – then, for example, nearly *all* of BRS’s activities would fall into this category. The exceptions are:

- charging for publications – charges that cover only the cost of printing and disseminating the work further. This is an example of cost recovery according to a user pays ethos because BRS is not specifically funded to widely disseminate its material; and
- conducting work directed towards an Australian Government outcome but funded by other governments through cost recovery arrangements, for example work funded by foreign governments.

AFFA recognises that economic theory would suggest that government provision and funding may be preferred or necessary if the good or service being provided has “public good” characteristics, or spillover effects are associated with its provision. This therefore provides some support for the PC’s test for core activities, and its recommendations that these activities be taxpayer funded. AFFA believes, however, that this classification of activities needs to be varied in some circumstances.

Many of the goods and services provided by AFFA’s information agencies are not pure public goods – having, in many cases, a mix of private and public goods characteristics.

- This is due in part to the substantial processing costs associated with transforming raw data into information products that meet particular user needs.
- In addition, information is increasingly being tailored to meet the specific needs of individual users with respect to timeliness of delivery, presentation, focus and aggregation. Unprocessed information is rarely provided on the basis that ‘one size fits all’ and would often conflict with confidentiality and privacy issues.

For example, in relation to the provision of information on the internet, AFFA would dispute a suggestion that information agencies should make all data available on the internet free, on the basis that once collected, the data is essentially a public good. Processed data cannot be provided on the internet at low cost as data services often require a more complex and complete presentation than raw data. Data processing may also be expensive, with a high likelihood that data would not meet individual users’ needs without some specific tailoring. Furthermore, if all data were to be made available free on the internet there would be a substantial funding shortfall for information agencies such as BRS and ABARE, which would require additional budget funding to cover.

### 2.3 *Intra-governmental transfer funding*

A further concern of AFFA is that ABARE’s and BRS’s cost recovery practices are not easily modelled by the PC’s core/non-core split which appears to assume that agencies are funded centrally, and ignores the sorts of relationships through which ABARE and the BRS are funded. For example, these agencies receive some funding through the Department of Industry, Science and Resources (DISR), the Murray-Darling Basin Commission and the Research and Development Corporations (RDCs). Draft recommendations 6.5 and 6.6 appear to indicate that ABARE should only work on material that is:

- funded through AFFA’s appropriation and not open to any competitive process; and
- of a purely private good nature funded by non government agencies.

That is, it may not be able to use transfers from other government agencies to fund its core activities.

AFFA notes that:

- Information agencies often cost recover for core public policy work from research and development corporations (RDCs), and government departments other than the agencies’ ‘home departments’ (AFFA for ABARE and BRS). In AFFA’s view the PC does not cover intra-governmental transfers of funds which underpin many of ABARE’s and BRS’s current cost recovery relationships adequately in the Draft Report;
- Appropriation monies are being allocated within Departments increasingly on the basis of payment for delivery against set milestones and outputs under purchaser-provider type arrangements. These arrangements have all the characteristics of cost recovered projects, meaning that processes relating to the allocation and management of appropriation and cost recovered monies are very similar; and

- Accountability for expenditure of public funds is often best achieved through a ‘purchaser-provider’ model, where some agencies are funded through cost recovery from other government agencies for a portion of their core activities.

## 2.4 *Other information agency issues*

Other points which AFFA would note on the Draft Report:

- On page 27 the PC appears to acknowledge that ABARE is correct in charging for capital costs and overheads in pricing incremental services. However, the position of the PC is unclear. ABARE’s case for charging was set out in detail in its original submission to the Commission.
- The discussion on page 118 seems to indicate that the Commission believes that ABARE’s cost recovery is currently driven by the earlier 30 per cent target. The target was noted in the ABARE submission as part of the history of cost recovery, not the current rationale.
- On page 119 there is a discussion of data collection by ABARE and other agencies. The BRS *Digital Atlas of Australian Soils* is incorrectly identified as an ABARE data set.

## 3. **Cost Recovery for Regulatory Activities**

The PC describes regulatory agencies as those that include involvement in regulating goods or services to decrease the risk of harm or damage. Typically they are involved in pre-market assessment of products or services and post-market enforcement and compliance. Under this description, the AFFA agencies AQIS, NRA and PBRO would be classified as regulatory agencies.

While AFFA supports the PC outlining a clear set of guidelines on cost recovery as a useful model to inform future discussions on cost recovery policies, this section of the Submission highlights a number of caveats which AFFA believes need to be taken into account when considering cost recovery issues.

### 3.1 *General comments on the PC’s guidelines*

The process proposed by the PC is broadly consistent with current AFFA cost recovery arrangements. It is feasible for the relevant portfolio agencies to assess the need for current and prospective services, and the appropriateness of cost recovery for new proposals as proposed for Stage 1. However AFFA notes that decisions on this stage of the process will mostly be made outside the agency – for example by Cabinet. (This issue is explored further in Section 3.3). In view of the fact that Stage 1 is often effectively outside the control of the cost recovery agencies, AFFA believes the effectiveness of the final report as a practical guide for agencies would be enhanced if relatively more emphasis was given to Stages 2 to 4 and less to Stage 1.

AFFA agrees that, once a cost recovery approach has been chosen, it is appropriate that the cost recovered agency should be responsible for developing the form of charges and the framework for determining costs and prices (Stage 2).

In terms of monitoring (Stage 3), AFFA’s view is that existing mechanisms to which the PC refers, such as benchmarking, ANAO performance audits, internal audit committees and consultative committees, are effective in achieving accountability in cost recovery. In particular, the value of consultative arrangements between industry and cost recovery agencies should be further emphasised. The first AFFA submission noted the importance of consultation with stakeholders, especially for services provided on a monopoly basis. The National Registration Authority for Agricultural and Veterinary Chemicals (NRA) submission also noted that its schedule of charges and fees has been determined in consultation with industry to ensure that the fees are closely

aligned with the service provided. AFFA further supports the principle of wider consultation including the publication of cost recovery arrangements on agency websites – a measure which is already in place for a number of AFFA’s agencies (including AQIS). The importance of consultation is discussed further in Section 4.7 below.

The periodic review process outlined in Stage 4 raises some issues that are of concern to AFFA. These are discussed in Section 4.3.

While AFFA supports the use of guidelines to promote consistency across the public sector in applying cost recovery to their activities there is a need to ensure that the guidelines provide sufficient flexibility to allow responses to urgent situations that may arise (for example the detection of a disease in Australian agricultural produce). There may be circumstances where a decision on a cost recovery arrangement is required immediately and undertaking the necessary steps in the process (such as the preparation of a Cost Recovery Impact Statement) would not be possible. The guidelines proposed should have the flexibility to provide guidance in such circumstances.

### 3.2 *AFFA’s cost recovery practices*

Based on legal advice, agreement with the Department of Finance and Administration, and industry consultation, **AQIS** has issued its own policy on fees and charges, which are broadly consistent with, and raise many of the issues in, the PC’s guidelines.

The **Plant Breeders’ Rights** (PBR) program is aimed at increasing investment (particularly private investment) in plant breeding. The PBR area of AFFA currently recovers its fees for service directly from the beneficiaries of the program. The PBR cost recovery program was established by Cabinet decision and fee for service provisions included in the legislation of the *Plant Breeder’s Rights Act 1994*. These arrangements are in line with the PC recommendations and consistent with the patents examples referred to in the PC’s Draft Report.

This cost recovery strategy is clearly appropriate from a policy point of view as the scheme is voluntary and will only attract participants if it is deemed to be valuable, if participants receive a benefit from the arrangements and if it is considered to represent value for money. The number of applications is broadly indicative of investment in the industry.

AFFA’s **Red Meat Quota Administration** provides a good example of arrangements that closely mirror the PC’s proposed guidelines. AFFA inherited the management of meat export quotas from the Australian Meat and Livestock Corporation in July 1998 following a review of the red meat industry structure. The transition arrangements, developed by both government and industry, provided that the red meat industry would fund the operation of the Quota Administration Unit until a cost recovery regime could be developed and implemented. This was done by regulation in November 2000, with the progressive introduction of a fee applied to exporters for the grant of quota as each new quota fell due during 2000-01.

Both the red meat industry review and an industry review of quota administration supported and recommended the introduction of cost recovery procedures. There is provision for this already in the primary legislation (*Australian Meat and Livestock Industry Act 1997* and the *Australian Meat and Livestock Industry (Quotas) Act 1990*). Given the extensive coverage of the issue, the Office of Regulation Review (ORR) agreed that a Regulatory Impact Statement was unnecessary to support the regulation applying the fee.



In developing the level of fee to be charged, AFFA and Red Meat Advisory Council (RMAC) engaged a consultant to ascertain the costs to be met by exporters and those that may be considered as being met by government.

Comprehensive statistical information of broad interest is displayed on the AFFA website and individual requests for statistical reports are charged at a rate that covers costs. The arrangements have been in place for around seven months and AFFA is monitoring income from fees and other sources against projected costs to confirm our preliminary assessment of the level of fees applied. The arrangements are designed to be revenue neutral for AFFA. A full assessment will be undertaken at the end of 2001. Additionally, in its report of 1999, the RMAC recommended that the quota administration processes, including cost recovery, be reviewed in three years.

In summary, AFFA believes the processes outlined in the proposed guidelines have largely been met for red meat quota administration. Costs have been apportioned between policy costs – which are being met by Government, and other costs – which are being met by the beneficiaries – in this case the industry.

Another recent AFFA example of a cost recovery process is AFFA's Wool and Dairy Branch involvement with the **privatisation of the Australian Wool Research and Promotion Organisation** (AWRAP). This process was a distinct component of work in AFFA's Industry Development business and cost recovery was a specific aspect of the Government decision. The AWRAP privatisation has now been completed.

At the time of the Government's decision to privatise AWRAP, the Government also decided it was appropriate for industry funds to meet the substantial incremental costs of the Department's work on the basis that the industry members were the beneficiaries of the work. Amendments were made to the *AWRAP Act 1993* to allow this. The Minister issued a Direction to AWRAP under Section 6(1D) of the *AWRAP Act 1993*, directing AWRAP to reimburse certain costs of the major parties involved in the privatisation process, including AFFA. This followed the precedent of recovering Commonwealth costs in the privatisation of Wool International in 1999.

The system developed for wool recovered the following costs:

- legal, consultants and industry consultation costs;
- AFFA salaries and salary on-costs (superannuation, leave) (for wool, for 2 employees in the section);
- AFFA travel expenses (airfares, Travel Allowance including accommodation, taxi fares); and
- certain other AFFA expenses (including AFFA in house legal expenses).

The AWRAP paid the charges upon receipt of invoices from AFFA, with AFFA recovering in total, approximately \$180,600. This was a small part of the costs of the conversion, which was of the order of \$5 million. Levies and Revenue Service recovered costs separately for this work towards facilitation the conversion of AWRAP from the new company, Australian Wool Services Limited (AWS), post-conversion, to the order of \$44,000.

Our processes broadly followed the "*process for assessing cost recovery*" included in the proposed guidelines.

Stage 1            An initial policy review was undertaken, however the decision to cost recover was taken by Cabinet rather than AFFA

Stage 2	The system established is based on AFFA reconciling its expenditure and invoicing AWRAP on an ongoing basis for reimbursement, with an interim levy rate introduced to cover the costs of transition.
Stage 3	Independent auditors verified that AFFA involvement was and is accurate and consistent with the Ministerial Direction, and that AFFA has not claimed additional costs beyond the scope of the initiative.
Stage 4	The processes have each been developed for a discrete period of time – until privatisation is finalised.

### 3.3 *PC's initial policy review stage*

AFFA notes the PC's four stage process includes a first stage which involves an *initial policy review* which the PC describes as requiring the relevant portfolio department or information agency to assess:

- Is the regulation or service consistent with the agency's objectives?
- Who should pay?
- Should cost recovery be imposed and, if so, should fees or levies be used?

AFFA is concerned that the PC should take account of the fact that in most instances these decisions are made outside of the agency which will ultimately implement the arrangements – in many cases by Cabinet processes. This has been the case for most of the portfolio's agencies involved in cost recovery including, notably:

- AQIS – for which Cabinet imposed cost recovery targets of initially 50 per cent, rising to 100 per cent by 1 January 1991; and
- ABARE and BRS were required – following Cabinet decisions – to cost recover a percentage of their respective budgets from the early 1990s.

A number of other Departmental activities are also cost recovered as a result of Cabinet decisions. The red meat quota administration and AWRAP privatisation examples outlined previously are recent examples. In the AWRAP example mentioned in the previous section the decision on the cost recovery framework was taken outside AFFA with cost recovery a specific aspect of the Cabinet decision.

### 3.4 *Trend towards fiscal consolidation*

The draft PC Report's guidelines recommend that a number of activities should be taxpayer funded. These include:

- Parliamentary requirements;
- international obligations;
- provision of "core" goods and services;
- regulatory activities for which the benefits accrue to the wider community; and
- policy development activities.

AFFA is concerned that the PC should recognise that in a context of tight fiscal constraints, as in recent years, agencies have little capacity to forego cost recovery in the absence of direct budget funding in its place.

This problem is further exacerbated when agencies are faced with higher costs for purchasing goods or services which, under the PC's framework, should be "taxpayer funded" – such as those associated with food safety functions of the Australia and New Zealand Food Authority, or for the purchase of statistics which the Australian Bureau of Statistics (ABS) previously provided for free. A further problem in this regard is the fact that the ABS has dropped data collection that used to be

core business. Agencies interested in maintaining some of this data have had to pay, but without supplementation of the resources required to do so.

### 3.5 *Interpreting policy development flexibility*

Major initiatives to develop policy in response to industry calls are sometimes onerous and resource intensive. The guidelines should allow flexibility for Departments and agencies to consider cost recovery for major policy initiatives instigated at industry's request, especially if outside consultants are required and substantial legal expenses are incurred.

### 3.6 *Distinguishing between “beneficiary pays” and “regulated pays”*

The PC's guidelines make a distinction between situations in which it is appropriate to adopt a “beneficiary-pays” and a “regulated-pays” approach. AFFA believes that in some cases this distinction may be impractical. Many of AFFA's cost recovery arrangements were originally developed under an ethos of ‘user pays’ and attempt to apportion the costs of government services equitably to those that use them. The PC might consider further to what extent ‘user-pays’ (as opposed to the ‘beneficiary/regulated-pays’ distinction) provides an appropriate basis for cost recovery arrangements.

In most cases there will not be a single beneficiary and/or the beneficiary will be the party being regulated. For example, AQIS's inspection and certification of exported livestock will be beneficial for the meat processor, the ultimate consumer of meat (often overseas residents), the livestock producer, and even the general population who benefit from increased Australian exports. If the “beneficiary-pays” approach is adopted all these parties would share the cost of the services.

Similarly, in relation to Agricultural and Veterinary Chemicals regulation, AFFA notes the PC position that in regulating chemicals, where the policy objective is to reduce the risks of harmful spillovers (including enforcing safety and quality standards) that would affect the broader community, firms/individuals responsible for the regulated activity (presumably manufacturers/suppliers of chemicals) should pay. This is a ‘regulated pays’ approach and generally is the basis of the cost recovery arrangements of the NRA. However, these manufacturers/suppliers could also be seen as the major financial beneficiaries of chemical registration in that only registered products can be offered for sale. These beneficiaries then pay through the annual sales levy. It is therefore unclear whether the NRA cost recovery arrangements are to be viewed as ‘regulated pays’ or ‘beneficiary pays’.

Chemical users (such as primary producers) benefit through labelling of chemical products with respect to health and safety issues. The PC argues that, in these cases, the consumers of the regulated product should pay for regulation. Chemical users pay for the benefits they receive if chemical manufacturers incorporate allowance for registration costs and the levy in the price of their products. At the same time, consumers of agricultural produce, the production of which has required the use of chemicals in accordance with labelled withholding periods etc, benefit in terms of having safe products. The degree to which costs can be passed forward or back is an issue noted by the PC, but the application of the PC's cost recovery principles in situations such as these is unclear.

Under these circumstances AFFA believes that any guidelines developed which are based on an assessment as to whether the regulated party or the beneficiary should pay will sometimes be too simplistic and other considerations will need to be taken account of in these situations. One of these factors is the ease and cost of collection – it is often easier and less costly administratively to recover costs from industry rather than directly from customers.

### 3.7 *Importance of industry consultation*

In AFFA's view one of the most important factors which requires consideration to arrive at the balance between the "beneficiary-pays" and a "regulated-pays" approaches is the outcome of industry consultations.

As outlined in AFFA's initial submission to the Cost Recovery Inquiry, consultation with stakeholders is considered a very important step in the initiation and ongoing review of cost recovery arrangements within AFFA. AFFA is an agency that deals with a wide range of industries and groups. As a result, industry consultation is extremely important to the corporate ethos of AFFA and its associated organisations. In AFFA's view, cost recovery arrangements that are slightly sub-optimal from an economic efficiency perspective, but have industry support, may be preferable to economically efficient arrangements that do not enjoy the support of industry groups.

Industry stakeholders are consulted generally through representative bodies or advisory committees in the cases of the cost recovery arrangements of AQIS, NRS and AFFA's Levies and Revenue Services area (LRS). The consultative mechanisms are important in enabling clients to raise any issues they have with the cost and provision of the service. AQIS, for example, also reports directly to the various Industry Consultative Committees on the cost-recovery performance of each of its programs.

SMS Consulting conducted a review of AQIS's consultative mechanisms in April 2000. This review concluded that the AQIS/Industry consultation model is highly effective and "a model for other government bodies to follow". It is a unique process that does not copy other Australian or international models for government/industry consultation. The process is well advanced, evolutionary and provides for ongoing growth, change and continuous improvement.

In relation to Plant Breeders' Rights, fees are reviewed regularly and subjected to the scrutiny of stakeholders, including industry representatives on the Plant Breeders' Rights Advisory Committee (PBRAC). Accordingly fees may move up or down, however, the trend has been towards a decrease overall (in real terms) since the inception of the program in 1987.

AFFA recommends that the guidelines on consultation (page 191) need to reflect the necessary requirement of regular consultation with the applicable industry bodies who have to pay the fees and charges.

In situations where the beneficiary of the activity is uncertain, and/or where the ultimate incidence of the charge is shared between different parties in the production chain, AFFA recommends a more flexible approach to cost recovery involving:

- agreement between industry and Government on the most effective mechanisms for implementing cost recovery, based on the outcomes of effective consultation, and endorsed by industry; and
- a contribution from Government which reflects its responsibility for policy development, Parliamentary requirements, and international obligations.

## 4. Other Cost Recovery Issues

### 4.1 Cross subsidisation and over-recovered funds

Two other issues that are important in designing viable and practised cost recovery arrangements relate to cross-subsidisation (and the level of activities at which cost recovery charges are assessed) and over-recovered funds.

AQIS recovers its costs via a mix of cost-recovery and a small amount of community service obligation funding. The Memorandum of Understanding with the then Department of Finance stipulates that AQIS must fully recover its costs on a program basis rather than across AQIS as a whole. This is designed to avoid **cross-subsidisation** occurring between programs.

The Draft Report states that the Commission received evidence of several instances of cross subsidisation. AQIS policy – which is currently achieved – is to prevent cross-subsidisation occurring between programs. It is not AQIS policy to necessarily prevent cross-subsidisation between different locations or specific services within programs. The *AQIS Fees and Charging Policy 2001* specifically addresses the issue of cross subsidisation and states:

It is AQIS policy to prevent ...cross-subsidisation between user groups [or programs] by setting fees and charges that are designed to achieve full cost-recovery for each group....The *Canadian Airlines* case suggests that there can be cross-subsidisation within user groups, provided that there is a rational basis for discrimination between users in that group...AQIS seeks to operate on a system of nationally uniform fees and charges. Therefore, fees and charges set should be consistent between locations. User groups must ensure that processes for allocating costs across programs are reviewed and updated on a regular basis to ensure there is no cross-subsidisation.

The Australian National Audit Office (ANAO) found that AQIS has been "successful in managing its programs in recent years to avoid direct cross-subsidisation". (ANAO 2000, *AQIS Cost-recovery Systems* p.85). Though the ANAO reported that there are some cross-subsidies between some AQIS services within some programs, it found that the extent "was not readily quantifiable".

In relation to **over-recovered funds**, in its *AQIS Cost-Recovery Systems report*, the ANAO found that AQIS had retained over-recovered funds to the value of \$5 million and had not yet returned to industry in the form of discounts and rebates. AQIS' policy is for programs to endeavor to fully recover their costs in the year they are incurred. However, full cost recovery in one year is weighed against the necessity for price stability and, in practice, it is not possible to achieve full cost recovery every year without frequently amending charges. AQIS reaches agreement with the appropriate Industry Consultative Committees on how to return over-recovered funds to clients. It may take a considerable amount of time to reach a decision on the best method to return funds, and this occurs in consultation with industry.

AQIS uses three types of accounts to administer over-recoveries. An income equalisation account is used when the over-recovery is less than ten percent of the overall budget. The principal purpose of the income equalisation account is to enable AQIS and industry to overcome unforeseen downturns in the recovery of expenditure within each industry over a period of years. The account is designed to reduce the need for constant changes to fee/charging levels to accommodate unforeseen and often uncontrollable circumstances. IER accounts are established with the agreement of industry through the program consultative committees.

Over recoveries above 10 per cent may be placed in a revenue rebate account. The funds placed in this account are used to temporarily reduce the level of fees or charges applied for services

performed by the recoverable program, as agreed by industry. The actual method and timeframe for returning these funds is a matter for the relevant consultative committee.

Over recoveries above 10 per cent may be placed in an industry initiative account and are to be used in consultation with industry for projects of benefit to industry, such as research and development.

Of the approximately \$5 million currently sitting in over-recovery accounts, approximately \$1.5 million are over-recovered funds belonging to the Export Meat Industry. This represents three per cent of the overall budget for AQIS' Meat Inspection Program. Approximately \$1.3 million are over-recovered funds in the Import Clearance Program, representing nearly four per cent of total budget. AQIS recognises that the over-recovered reserves are industry funds and are therefore an AQIS liability. The distribution of the over-recovered funds is undertaken, as far as possible, in a timely manner and on a basis that is as equitable as possible to those groups and individuals within the industry who contributed to the surplus position. Any decisions regarding the use of the over-recovered fund are made in full consultation and agreement with the appropriate Industry Consultative Committee.

Similarly, in relation to plant breeders' rights, over recovery of funds is minimal though the Plant Breeders' Rights Advisory Committee (PBRAC) recommends a contingency/development fund to a maximum of 10% of the PBR scheme.

AFFA therefore believes that in designing cost recovery arrangements account needs to be taken to ensure arrangements are practical with, for example, the level of activities at which cost recovery charges are assessed chosen appropriately and measures to ensure that reasonable levels of over-recovered funds can be collected to buffer fluctuations in collections and ensure that the important goal of price stability over time is achieved.

#### *4.2 Cost Recovery Impact Statements*

AFFA opposes the Cost Recovery Impact Statements (CRISs), as it would likely duplicate other processes, particularly for regulatory agencies which are currently required to prepare a Regulatory Impact Statement when planning new activities that may include cost recovery. Further, Departments are variously required to prepare Regional Impact Statements and Business Impact Statements in some instances.

If a CRIS were required, it should be confined to the activities of information agencies, and incorporated to the extent possible within existing processes. Indeed, it is our strong view that the existing Regulatory Impact Statement and Business Impact Statement should be rolled into one, without creating the need for further templates and the detailed reporting this inevitably seems to require. If the Office of Regulation Review were to be given responsibility for the CRIS then it could ensure that any extra requirements were included in Regulatory Impact Statement process. If this extra process were to be required it would come at a cost – which, we believe would appropriately be regarded as a policy development activity and be the funding responsibility of Government.

#### *4.3 Reviews of cost recovery arrangements*

AFFA agrees with the PC recommendation that all cost recovery arrangements be subject to the same budgetary and parliamentary oversight as budget funded activities and also involve a performance based efficiency audit approach based on stakeholder consultation. However, AFFA notes that some AFFA agencies and areas of AFFA involved in cost recovery have already

undergone recent rigorous reviews – as well as undergoing Parliamentary scrutiny through appearing before Senate Estimates Committees.

For example, AQIS's cost recovered programs were recently comprehensively reviewed by the Australian National Audit Office ((ANAO 2000, *AQIS Cost-recovery Systems*). AQIS also undergoes extensive financial/budgetary scrutiny by its Industry Consultative Committees. Generally, Industry Consultative Committees meet quarterly to discuss, among other things, the financial position of, and budget forecast for, each program. Any changes in fees and charges are also discussed with the Committee before any decisions are made to change current imposts.

The NRA has also recently reviewed its cost recovery arrangements (including an activity based costing exercise) in response to an ANAO audit and a National Competition Policy review process.

AFFA would agree that reviewing cost recovery arrangements over the next five years should be a minimum goal for agencies in light of the findings of the PC. However, AFFA would question whether further reviews within the five year timeframe proposed by the PC are necessary where rigorous reviews have been undertaken recently, or are a regular feature of an agency's operations.

#### *4.4 Legal authority for cost recovery activities*

The PC recommends that all cost recovery arrangements should have clear legal authority. AFFA provides the following information in response to this recommendation.

All cost recovered activities within **ABARE** and **BRS** are in line with terms negotiated with DOFA under the current Section 31 Agreement of the FMA Act between the AFFA Minister and the Minister for Finance and Administration. They are also mentioned in the annual Appropriation Act.

**AQIS'** cost recovery is based on a mix of fee-for-service and taxation imposts. The legal bases for the imposts are contained in a number of principal and subordinate legislation.

##### Fee for service legislation

###### *Quarantine Act 1908*

- fees contained in the Quarantine Determination

###### *Export Control Act 1982*

- fees contained in the Export Control (Fees) Orders

###### *Imported Food Control Act 1992*

- fees contained in the Imported Food Control Regulations

##### Taxing legislation

###### *Export Inspection and Meat Charges Collection Act 1985 (the Collection Act)*

###### *Export Inspection (Establishment Registration Charges) Act 1985*

- charges contained in Export Inspection and Meat (Establishment Registration Charges) Regulations

###### *Export Inspection (Quantity Charge) Act 1985*

- charges contained in Export Inspection (Quantity Charge) Regulations

###### *Export Inspection (Service Charge) Act 1985*

- charges contained in Export Inspection (Service Charge) Regulations

The **National Registration Authority** imposes application fees and renewal fees under the Agricultural and Veterinary Chemicals Code (scheduled to the *Agricultural and Veterinary Chemicals Code Act 1994*).

The NRA imposes levies on disposals of registered agricultural and veterinary chemical products through three Acts: *Agricultural and Veterinary Chemical Products Levy Imposition (General) Act 1994*, *Agricultural and Veterinary Chemical Products Levy Imposition (Excise) Act 1994*, and *Agricultural and Veterinary Chemical Products Levy Imposition (Customs) Act 1994*.

The levy is collected under a separate piece of legislation for that specific purpose (Agricultural and Veterinary Chemical Products (Collection of Levy) Regulations). The Act's Regulations prescribe the levy rates, which are based on a product's disposals for each calendar year.

The **Plant Breeders Rights** Office's cost recovery program was established by Cabinet decision and fee for service provisions are included in the legislation of the *Plant Breeder's Rights Act 1994*.