

Mr Paul Belin  
Assistant Commissioner  
Productivity Commission  
Locked Bag 2  
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MELBOURNE VIC 8003

Dear Mr Belin

**SCREENSOUND AUSTRALIA SUBMISSION  
ON COST RECOVERY DRAFT REPORT**

Attached please find a very hastily put together submission on the Draft Cost Recovery Report. I apologise for both the late timing and hastily put together nature of this submission. I hope it is still of value.

Because of the complexity of the issues behind this Cost Recovery Report and the limited capacity that an agency such as ScreenSound Australia has for analysis of complex economic issues I have undertaken most of the work on our two submissions and the seminar presentation myself. This has unfortunately meant that it has received less time than it deserved. Should you wish me to provide a more thoughtful and thorough submission I can do this but it will take a week or two.

In the meantime I hope you can make sense of the submission as it is. I would also like to emphasise that although the submission has focused on matters of concern in the Report my overall view remains that it is an excellent and thorough document that advances significantly consideration of the important next step, a broadly agreed Government policy on cost recovery (or perhaps two policies, one for information agencies and one for regulatory agencies).

Kind regards

RI Brent  
Director

12 June 2001

# Cost Recovery - Draft Report

## Comments by ScreenSound Australia, the National Screen and Sound Archive

The following comments on the above Report are a brief commentary on the key concerns we have with the Report. It is not a comprehensive review of the document. It is biased to comments that are critical. It is therefore important to emphasise at the outset that I found the Draft Report to be a thorough, considered and valuable assessment that assists in considering the application, in both theory and practice, of cost recovery in Commonwealth agencies.

2. The issues of particular concern to ScreenSound Australia have, in large part been covered by the presentation I have already made to the Commission on the draft guidelines. I will not repeat all I said in that presentation but will try and list the key issues here. At the same time I will seek to keep my comments as brief as possible on the basis that I will be available to clarify them when I appear before the Commission, and am also willing to provide more detailed written material should you wish.

3. I repeated the contents of my earlier submission.

4. The comments below are organised according to the chapter headings in the Report, but are preceded with an overview.

### Overview

5. The Draft Report rightly identifies a need for a clear statement of policy from the government on the principles it wishes applied to cost recovery. I support the thrust of the report that uncontrolled use of cost recovery is a potentially dangerous tool that can lead to a range of problems, from direct inequities to economic distortions.

6. At the same time I am concerned that the intermingling of regulatory agencies with information agencies has lead to some overstatement of the issues for information agencies. I do not believe the extent of increased transparency and rigidities in policy proposed by the draft report reflect concerns that exist in fields such as that occupied by ScreenSound Australia. While there have been cases of concern expressed about our charges they have not been taken to forums outside the organisation. I believe this reflects our success in being responsive to our customers and stakeholders and in being open and sensible about our fees.

7. I would **not** like to see a new layer of Cost Recovery Impact Statements (CRIS), increased reporting, application of general rules about the calculation of fees or systems for the categorisation of fees. These would either inhibit the effectiveness of our current fee structures or limit the capacity of ScreenSound Australia to be responsive to market and other forces that affect our pricing.

8. Of particular concern is the application of the CRIS requirements on our very diverse set of prices, the application of strict rules for pricing formulas and new monitoring, review and process rules that will throw substantial additional cost onto this small agency.

9. Turning now to the specifics of the Draft Report:

### **Key Messages**

10. I query the extent to which the second dot point (dissatisfied users and, in particular, concerns about regulatory creep, gold plating and cost padding) apply to information agencies or at least to agencies such as ScreenSound Australia.

11. Despite the absence of a clear set of Government endorsed policies on cost recovery I consider that the third dot point overstates the absence of the attributes of good policy, particularly when applied to ‘information agencies’. In the case of ScreenSound Australia there is a significant degree of transparency in much of our cost recovery infrastructure (through published price lists, clear policies forming the basis of most prices, and publicly available data on our revenues and expenditures). We are fully accountable for our cost recovery arrangements (through our Council, our Department, our Minister, Parliament, Output Pricing Reviews, market research, internal reviews, and published reports). Finally there is no issue of the legality of the charges.

12. I would support the rest of the key messages.

### **Economics of Cost Recovery**

13. I am concerned about two aspects of the conclusion to this chapter, as stated on page 30:

- The degree and value of private benefit from a service is also relevant to the level and type of cost recovery, regardless (to some degree) of the broader public benefit reflected in the concept of ‘core’ and ‘non-core activities’. Where an individual receives substantial private benefit from a serviced or information then it may be efficient and non-distorting to charge for that service regardless of its contribution to the broader public good.
- There are some activities that may not be captured in the concept of ‘outside core activities and subject to competitive neutrality considerations’. Such activities could be outside core activities, but not commercially available. This is the case for some ScreenSound Australia activities that are provided commercially, may be well outside core activities, may even contribute to broader public good, but are not available from other sources. An example would include repair of film or video not treatable commercially, of some possible heritage value, but not of sufficient value to justify its inclusion in our collection. There should be provision for considering cost recovery in such cases.

### **Legal and Fiscal Framework**

14. As part of the Commonwealth, ScreenSound Australia’s revenues must be paid into the Consolidated Revenue Account, and are then appropriated to ScreenSound Australia. In these circumstances the appropriation is fully within the scrutiny of Parliament, our Minister, our Department, and the Australian National Audit Office.

15. The Cost Recovery Impact Statements are a source of serious concern, subject to clarification of ‘significant cost recovery proposals’ to which they would apply. Since no

particular area of cost recovery in our operations recovers more than about \$400,000 it may be that none of our activities would be covered. If, on the other hand, a narrower definition is applied I can foresee a compliance nightmare. Here is a list of the range of services for which ScreenSound Australia has at one time or another charged fees:

- Storage of film, video or audio materials;
- film repair, copying, or assessment;
- audio repair, copying restoration or assessment;
- video repair, restoration, copying, editing or assessment;
- video or audio studio hire;
- access to film, video and audio material that can include any of the above services as a prerequisite;
- research, both technical and collection content;
- delivery of access copies for private or professional/commercial use in domestic and/or broadcast quality, and with or without copyright clearance;
- film screenings at our premises or touring, alone or in collaboration with private sector or public sector partners;
- exhibitions at our premises or touring, alone or in collaboration with private sector or public sector partners;
- presentations to primary, secondary or tertiary student groups, adult groups, the general public and teachers;
- venue hire, training within Australia and overseas, to national institutions, state institutions, companies, private organisations and individuals; products including video, audio and books; retail shop sales; cafe sales; and
- speakers in various forums.

16. I would be interested in learning more of overseas experience with CRIS's (or their equivalents) in the discussion on page 60.

### **Current Cost Recovery Arrangements**

17. Table 4.2 on page 66 should include 'demand management' and 'equity distribution issues' as rationales cited by ScreenSound Australia. If not clearly stated in our previous submission they were certainly intended to be covered. In addition, having now seen the list, I would consider that we also use the 'economic efficiency' and 'competitive neutrality' rationales as well.

18. The table 4.4 on page 73 shows our cost recovery percentage as 3.6. It is in fact much higher if the Capital Use Charge is excluded from our appropriation. The application of this charge to costings for ScreenSound Australia is a very complex matter. It does not reflect a cost of holding/using capital because the overwhelming bulk of the 'capital' it covers is our collection. The valuation is not based on resale value as the collection would have a very low resale worth, and nor does it reflect acquisition cost as the overwhelming bulk of it has been donated. It is valued on replacement cost. Whether this Capital Use Charge is a legitimate cost to attribute to ScreenSound Australia's cost equation in the context of cost recovery is thus debatable. This issue intersects with a number of other costing issues that could be discussed under various chapters but which I will cover here.

19. I also query to what extent the table includes intra-Commonwealth charges, which are arguably outside the scope of the more general discussion on cost recovery, on the basis that they should be considered on an entirely different set of criteria, perhaps limited to how effective they are in more accurately ascribing costs to the appropriate part of government.

20. In looking at the cost recovery calculations covered in the analysis of costing models in appendix H there are difficulties that affect ScreenSound Australia specifically and all information generally:

- When looking at full cost attribution models the issue of how to value the information source is critical. In our case do we value the collection or not and if so how (see above)?
- I also query how direct costs for the collection should be ascribed? On one argument what we must provide is a comprehensive collection, such that if users only use one item they nevertheless required that we keep a much wider collection to ensure that we would have that one item but which had not previously been identified.
- Alternatively perhaps we need only ascribe the one item to them but are they required to pay for its full cost of storage from first collection? (This may parallel the 'first mover disadvantage' but they may in fact be the 'only movers' for that item.)
- If we are restricted to marginal or long run net avoidable costs (LRNAC) for cost recovery limits, how do we value our access facilities? The cost of these facilities is a LRNAC given that they will be closed if we close access services, but we cannot close them without denying our charter.
- How do we cost the repair of a piece of nitrate film, copying to modern film stock, conversion to video, preparation of video master, preparation of a video duplicating master, and preparation of an access video - for the first (and possibly only) user of some heritage film?
- And most importantly, how do we establish the marginal cost of information resources generally, when the entire cost is often in the first creation with an almost zero marginal cost after that? For example in the list of steps above, from nitrate film to video access copy, once the access video exists the marginal cost of allowing a customer to view it is almost zero. If we are to be restricted to recovering incremental cost (as per recommendation 6.7) commercial users of our collection (albeit for 'public good' activities such as broadcast in cultural programs on television) would be entitled to free access to our collection distorting the use of a scarce resource against alternatives for which our collection may be substitutable but not normally in direct competition.

## Effect on Agencies

21. I am concerned that the undesirable effects on agencies outlined in box 5.1 are not in fact issues that relate to cost recovery but rather general issues that go to good/bad administration. Putting aside the notion of 'regulatory creep' (as my concern is with information agencies) the possibility of 'gold plating' and 'cost padding' are not in fact related to cost recovery. Regardless of the power to impose charges it is possible for agencies to over service (and charge it to the taxpayer or the customer) and possible to 'cost pad' (and charge it to the taxpayer or the customer). In the case of cost recovery operations the only difference is that the padding or over servicing is more likely to both be apparent to the customer and of sufficient concern to the customer that it will be raised as a matter of complaint.

22. In the end it is important not to confuse issues of poor administration that result in bad service of one kind or another with the separate issue of how it is paid for. There is no logic in the suggestion that extra service at extra cost is more likely if the bill is being paid by a user rather than the taxpayer.

23. The same point applies to the issue of failure to introduce technological innovation to reduced costs. It is asserted on page 111 that this failure is more likely to occur if there is a user who has to pay for the more expensive delivery rather than if the extra cost is paid by the taxpayer. Not only is this not logical but indeed all the examples that follow point to the exact opposite outcome.

24. Jumping back to page 92 I am concerned that there is a similar break in logic in the suggestion that agencies will focus on cost recovery operations because they will be encouraged by the revenues available. Given that agencies are fully answerable to Parliament, Ministers, ANAO, departmental supervision (from line departments and central agencies such as the Departments of Finance and of Prime Minister and Cabinet), and to customers, I consider it unlikely that agency heads would see benefit in boosting revenues, and costs in low priority areas at the expense of core responsibilities. The comment from AGSO that is cited to support the contention refers to the impact of cost recovery **targets**, not the impact of cost recovery *per se*.

25. This leads to the broader concern about lack of scrutiny for cost recovery operations. I am not sure of the basis of this point. Parliament is not limited to scrutiny of agencies on the basis of the source of their revenue. While Estimates Committees are arguably so limited this is not how they operate in practice. Furthermore the need for agencies such as mine to have revenues paid to the Consolidated Revenue Fund and then appropriated (see above) overcomes this theoretical limitation in any case. In addition there are many other avenues of Parliamentary scrutiny (ranging from other committees to Parliamentary Questions) and scrutiny from the many other agencies mentioned in the paragraph above, that are in no way limited by the source of an agency's revenue!

26. I am very concerned at the suggestion (on page 95) that the efficiency dividend be applied to cost recovery operations. This is a blunt enough instrument when applied across the board (punishing the most efficient agencies as they have the least room for easy wins in improved efficiency). It is particularly problematic to apply it in a context where most efficiency gains should properly be reflected in price reductions (especially given the report's bias to cost based determination of appropriate pricing).

## Economic Effects

27. Many of the comments above have been focussed on arguing against undue restriction on cost recovery. This is based on a view that freedom from rigid rules that restrict the nature of charging is more likely to lead to fair and effective use of this funding and policy tool. Accordingly it should not come as a surprise that I therefore support recommendations 6.2 and 6.3 particularly strongly.

28. On the other hand, as discussed at length in the seminar on the draft guidelines, I have considerable problems with the concept of 'core' and 'non-core' activities. Not only is it very difficult to make any such distinction in the case of ScreenSound Australia, it is also a distinction that overlooks the demand side of the supply/demand equation. While there may be some activities that are more central to our charter and some that are less, some of the clearly core activities are those for which it is most logical to charge in view of issues such as a clear private benefit of economic value to the customer, clear capacity to pay, need for control of demand (noting the potential inconsistency between the last two points), potential economic distortions if no charge is levied, and indeed most of the other rationales listed on page 66.

29. I am also not clear on the reasons for the choice of marginal cost for recommendation 6.7 on page 122. LRNAC seems to me to be equally justifiable, but I would go further. Given the full range of reasons for charging fees covered earlier in the report it seems to me that there may be many other legitimate formulas for pricing services. There are many supply **and demand** factors that should be considered.

30. Differential pricing practices come in for criticism on the basis of the example of cheaper services for academics given because of the broader good that such access delivers. In theory it may make sense to suggest that academics should be properly funded for such value added uses and therefore be able to pay full price. In practice I cannot conceive a model that would actually deliver this outcome even given dramatic increases to the current levels of funding for education generally and tertiary institutions in particular. There would be no sensible way of quarantining the funding to the specified purpose. Thus, while the theory makes sense, in practice agencies such as mine and the ABS will continue face the issue of denying service to users who will produce outcomes of high public value unless we provide fee concessions. In the case of ScreenSound Australia there are further issues relating to the longer term gains that can flow from promoting the use of our collection (including purchase of product) through support for certain users.

## Improving Administrative Arrangements

31. I am concerned at the assumption that cross subsidy through fee structures is necessarily undesirable. The analysis does not seem to consider whether the cross subsidy necessarily involves any market distortions. The example used on page 188 possibly does involve distortion but this is not always going to be the case. Again it is necessary to consider the price in relation to the market and demand. Where an agency supplies services to a market where price is not the principal regulator of demand, price variations will not affect consumption decisions, and the use of price variations (cross subsidy) may be both appropriate and effective. This outcome is indeed more likely in the cost driven pricing approach suggested in the report as it is quite possible the price will be well below the demand curve at a demand level determined by other factors.

32. In relation to the question of consultation on cost recovery I wish to continue the theme I have expressed above in response to the proposals for external scrutiny of cost recovery. There are many existing forums of consultation with 'stakeholders' that could be used for consultations on cost recovery. In the case of ScreenSound Australia we already use our market research, stakeholder consultation (both formal, i.e. focus groups, etc., and informal), direct feedback, usage data and anecdotal evidence from our customer service staff to monitor, assess and review charges. We utilise published policies, consultation on review of those policies, our service charter, our annual report, our web page and published information on charges to provide some degree of transparency to our charges.

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(Director)