# Stage 2 Cost Recovery Impact Statement

## Package of cost recovery changes, 2023

# 1 EXECUTIVE SUMMARY

This cost recovery impact statement (CRIS) explores options to address financial deficits under Establishment fees, and to address seven minor 'design' issues. Options are identified using, and assessed against, the Ministry for Primary Industries's cost recovery principles of Transparency, Justifiability, Efficiency and Equity.

## 1.1 Establishment fees

Establishment fees pay for a range of food safety, biosecurity and animal welfare verification services to enable overseas market access for the red meat sector.

### 1.1.1 The problem

The current Establishment fees were set in 2015.

The majority of verification services' costs are veterinarian personnel costs. Since 2015, veterinarian costs have increased significantly and further increases are forecast. Total costs are projected to increased from $31.9 million in 2021/22 to $35.3 million by 2025/26.

While cost pressures have been broadly managed to date, total accumulated under-recovery is forecast to be $10.81 million by the end of 2025/26. A total of $0.85 million would be written-off by 2025/26 with the rest ultimately written-off over future years.

### 1.1.2 The preferred option

The forecast cost increase and flat revenue means a rate increase is required to fully recover costs and the existing memorandum account deficit. The proposed fee increases are:

- $70.30 to $79.80 for veterinanrian establishment fees
- $75.10 to $88.10 for supervising veterinanrian establishment fees
- $41.04 to $51.40 for the programme charge.

The preferred option – Option (2) – increases total fees by around 11%. This is equivalent to 1.3% increases per annum since 2015, and much lower than inflation in consumer prices of 2.8% per annum and in vet services surveyed by Statistics New Zealand of 3.8% per annum.

The preferred option avoids all but a forecast $0.63 million (which is unavoidable) of the $10.81 million under-recovery being written-off.

### 1.1.3 Impacts

The preferred option is expected to have a negligible impact on the industry as a whole. The overall impact is equivalent to a 0.04% increase in export prices. The impact will vary for different meat types, with bovine least impacted and smaller-volume meats like deer, pig, and goat more impacted though still to a small degree.

By fully recovering recoverable costs, Option (2) best meets the Efficiency principle, satisfies the Transparency and Justifiability principles, and no reasons under the Equity principle have been identified for why Option (2) should not be preferred.

The Meat Industry Association supports Option (2), which is also a requirement under legislation for making a change part-way through a financial year.

## 1.2 Design issues

Design changes are relatively small and uncontroversial. The seven changes in this year's package received support from submitters.

### 1.2.1 Limited exemptions from animal products risk management programmes

The preferred option introduces a $135 hourly fee to process exemptions to risk management programmes. Exemptions can be required from time-to-time, for example, if a shipment is delivered to a location that is not covered by the risk management programme. Exemptions are time-limited and can only be granted by MPI if there is a negligible risk to human or animal health.

The $135 hourly fee is the same hourly rate for similar services. The cost to producers would be between $405 and $2,025 per exemption request.

### 1.2.2 Infant formula auditing

The proposal introduces a $295 hourly charge for MPI to carry out on-site audits of infant formula manufacturing facilities on behalf of China's State Administration for Market Regulation (SAMR). The audits ensure infant formula can be sold in China.

China's SAMR normally conducts the audits with New Zealand businesses responsible paying for them. MPI undertook the audits on China's SAMR's behalf when travel between New Zealand and China was paused due to COVID-19. Establishing a fee for MPI's audits future-proofs the service in case travel between New Zealand and China is interrupted in future.

The $295 hourly charge is higher than MPI's standard hourly rate for other services due to the need to quickly scale up the capacity on an as-needed basis rather than having a more expensive permanent capacity. Costs to infant formula manufacturers could increase by around $46,000 per audit, and by around $370,000 in total per annum for the industry as a whole in years when travel is interrupted.

### 1.2.3 A tidier fee structure for approval of premises for export requirements

The preferred option makes fees easier to understand and reduces administration costs for businesses. There is no change in the level of fees.

### 1.2.4 On-call charges for vets doing biosecurity and animal welfare work

The preferred option introduces a $45 charge for vets being on-call when doing biosecurity and animal welfare work. This charge already exists for animal products work and compensates staff for the inconvenience of being on-call outside of normal work hours.

### 1.2.5 Call-out charges for vets doing live animal international trade work

The preferred option introduces a three-hour minimum charge for vets being called-out for live animal and germplasm exports, animal welfare, and biosecurity work outside of normal hours. This charge already exists for some animal products work and compensates staff for the inconvenience of being called-out outside of normal work hours. The preferred option will increase costs to industry by around $370 per call out and $58,500 in total per annum.

### 1.2.6 Veterinary rate at transitional and containment facilities

The preferred option corrects an inconsistency between the hourly fee for veterinary inspectors under the biosecurity cost regulations and other cost regulations. Biosecurity cost regulations have a fee of $102.27 per hour while other regulations have $186.30 per hour. The preferred option increases the $102.27 fee to $186.30 rate which reflects the cost of vet salaries plus overheads. Total costs across industry would increase by around $15,600 to $28,200 per annum.

### 1.2.7 Penal rates for animal product veterinary services

The preferred option corrects inconsistencies between regulations and collective agreements. The preferred option does not increase costs as MPI is already charging businesses according to the collective agreements, but if the proposal does not proceed, costs to public funding would increase by around $450,000 per annum.

# 2 AGENCY DISCLOSURE STATEMENT

This CRIS has been prepared by MPI.

There have been no significant or unusual constraints in the preparation of this analysis.

## 2.1 Data

The analysis around the Establishment fees uses a lot of data.

Historical financial data is not available before 2017/18. Ideally, data would be available back to the last time fees were reset in 2015/16. This has not been a significant constraint on analysis, however, as the data is sufficient to identify the causes of the financial deficits with high confidence.

Future financial data is based on forecasts with the usual uncertainty that comes with that. MPI makes best endeavours with forecasts, but forecasts routinely carry a lot of uncertainty due to the wide range of factors that can impact revenue and costs.

In assessing whether MPI's Establishments expenditure has been reasonable, the analysis compares MPI expenditure and cost inflation with the latest comparable public data including data published by Statistics New Zealand around inflation in consumer prices and in prices charged by veterinary services, and forecast inflation in consumer prices by the Reserve Bank of New Zealand. At the time this analysis was done, historical data on consumer prices was available up to March 2023, while veterinary services were available up to December 2022.

The analysis also includes a summary of how the affected sector has performed using a long time-series of trade data up to March 2023. Forecast data is used to describe how the sector might perform over the next couple of years. The forecasts appear to be reasonable as they have, so far, closely matched published data.

## 2.2 Cost recovery principles and preferred options

Options have been developed and assessed in accordance with MPI's cost recovery principles.

MPI is confident in the factual analysis in this CRIS, though whether the principles have been sufficiently met involves a level of judgement. MPI considers that the Transparency, Justifiability and Efficiency principles have been sufficiently met for each preferred option.

Additional judgement is required around the Equity principle. Equity involves consideration of fairness and, therefore, value judgements. As such, views about what is fair can differ and it is ultimately up to the Government (and Parliament) to decide what is fair. Nevertheless, all the preferred options in this CRIS were supported, or no objection was raised, by affected parties.

## 2.3 Impact analysis

Estimates of the immediate financial impact of options on the market and at the business-level are presented. However, as the options are minor relative to the size of the industry, the CRIS does not contain a full analysis of the market impacts or of demand for MPI services over the longer term.

B. Arnold.

Bruce Arnold, Director Cost Recovery

14 June 2023

# 3 Quality Assurance

The Ministry for Primary Industries Regulatory Assessment Panel has reviewed the Regulatory Impact Statement prepared by the Ministry of Primary Industries Cost Recovery Team and associated supporting material, and considers this CRIS partially meets the Quality Assurance criteria.

This CRIS partially meets the criteria as it only partially meets the complete, clear and concise criteria.

# 4 Common Terms

A list of common terms is provided in the table below:

| Term | Description |
| --- | --- |
| Memorandum account | These accounts are where all the funds recovered go into and are used by MPI to fund the services it provides. The rule with memo accounts is that they must always track to zero. |
| Risk Management Programme (RMP) | As defined in the Animal Products Act 1999. A RMP is used to identify, mitigate and manage hazards. Anyone who processes animal materials or produces animal products must register and operate under a risk management programme. |
| Verification | The application of methods, procedures, tests, and other checks to confirm:<br>• compliance with a risk based measure (such as a risk management programme or regulated control scheme), including<br>  ○ the applicability of the programme or scheme to the operations of the relevant animal product business; and<br>  ○ the effectiveness of the programme or scheme:<br>• whether the animal material or animal products have been produced or processed in a way that meets the requirements for the official assurance<br>• whether a regulated person has complied with a requirement imposed by or under legislation |
| Verifier | A recognised person whose specified functions and activities include carrying out verification functions and activities. |
| Establishment Verification | Any place or premises where the verification functions are performed by Ministry verifiers who are permanently or semi-permanently based at the place or premises. Involves staff being based at a premise (i.e. an establishment) due to the large amount of work. |
| Circuit Verification | Where the verification or advice functions are performed by Ministry staff who are not permanently or semi-permanently based at the place or premises.<br>Circuits involves MPI staff visiting businesses on a temporary, as-needed basis (‘circuit’ referring to an MPI verifier completing a circuit of leaving an MPI base and travelling to several premises before returning to base). |
| Supervising Veternarian | A veterinary verifier who has prime responsibility for the verification functions at a place or premises. |

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# 5 BACKGROUND ON COST RECOVERY

## 5.1 COST RECOVERY IN GENERAL

MPI provides a range of services across the Biosecurity, Food, Fisheries, Forestry and Animal Welfare systems. These services help protect New Zealand from biosecurity risks, ensure that food is safe to eat, and manage the sustainability of our natural resources. The exclusion of pests and diseases, a safety assurance, also improves trading partners willingness to accept New Zealand products. The improved market access enables the primary sector to grow the value of its production, including exports. Services include:

- biosecurity inspections to prevent pests entering the country
- developing and maintaining domestic and overseas standards for food and other products
- monitoring and testing products to ensure consumer safety
- gaining market access and providing assurances to overseas customers.

Cost recovery helps ensure the provision of these services. About 30% of MPI's departmental funding typically comes from cost recovered revenue.

## 5.2 WHICH SYSTEMS ARE THE SUBJECT OF THIS CRIS?

This CRIS covers a number of issues affecting the Food, Biosecurity and Animal Welfare systems.

## 5.3 HOW ARE COST RECOVERY CHARGES REGULATED?

Legislation allows MPI to recover costs, with regulations setting out specific charges. The specific legislation is cited later in this CRIS as each issue is considered.

Most of MPI's legislation requires costs to be recovered in accordance with the cost recovery principles of Transparency, Justifiability, Efficiency, and Equity. These principles also appear in MPI's cost recovery guidance[1] and in the Office of the Auditor General's guidance[2].

The principles are discussed further in Chapter 6.

## 5.4 HOW ARE COST RECOVERY REGIMES REVIEWED?

In line with best practice guidance, MPI generally undertakes a review of expenditure and revenue at least once every three years. Fees and levies may be updated outside of the normal three-year review cycle if a material surpluses or deficits arise, such as if:[3]

- accumulated deficit or surplus is more than four months (33%) of annual revenue
- the accumulated deficit or surplus is $1 million or more
- a deficit is due to be written-off (due to time limits in legislation on the recovery of deficits), or a surplus has existed for an equivalent amount of time such that it would be written-off if it was a deficit.

Frequent and timely reviews help ensure that revenue and expenditure are balanced and are preferred by industry as they help avoid large swings in charges.

Reviews of cost recovery settings will also be triggered if 'design' issues are identified. Design issues cover potential faults around:

- who should pay for services
- the scope of expenditure that is cost recovered
- the way in which costs are recovered
- the level of the charge.

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[1] *Ministry for Primary Industries Cost Recovery Policy Guidance*, MPI Information Paper No: 2018/08, https://www.mpi.govt.nz/dmsdocument/30855-Ministry-for-Primary-Industries-Cost-Recovery-Policy-Guidance
[2] *Setting and administering fees and levies for cost recovery: Good practice guide*, https://oag.parliament.nz/2021/fees-and-levies.
[3] Triggers come from MPI's internal operational policy *Managing deficits and surpluses*.

An example of a design issue around the level of a charge would be an inconsistency in the amount charged for the same type of cost between different services.

MPI takes a principles-based approach to reviews, as set out in the 'Cost Recovery Principles and overall approach to cost recovery' chapter, to expenditure and revenue reviews and design issues.

On occasion, 'first principles' reviews are conducted to test whether MPI's cost recovery frameworks and legislation remain fit for purpose.

## 5.5 MPI'S SERVICES, CHARGES, AND THE REGULATORY FRAMEWORK

### 5.5.1 HOW ARE COST RECOVERY CHARGES REGULATED?

Legislation allows MPI to recover costs in accordance with the Cost Recovery Principles of Transparency, Justifiability, Efficiency, and Equity (see Chapter 6).

Regulations under each Act set out specific levies and fees.

### 5.5.2 HOW ARE COST RECOVERY REGIMES REVIEWED?

In line with best practice guidance, MPI generally undertakes a review of expenditure and revenue at least once every three years. Additionally, MPI aims to set fees and levies at levels that ensure memorandum accounts trend towards zero over a three-year period. To achieve this, fees and levies may be updated outside of the normal three-year review cycle if a material surplus or deficit accumulates in a memorandum account.

Reviews of cost recovery settings will also be triggered if 'design' issues are identified. Design issues cover potential faults around:

- who should pay for services
- the scope of expenditure that is cost recovered
- the way in which costs are recovered
- the level of the charge.

An example of a design issue around the level of a charge would be an inconsistency in the amount charged for the same type of cost between different services.

MPI takes a principles-based approach to reviews, as set out in the 'Cost Recovery Principles and overall approach to cost recovery' chapter, to expenditure and revenue reviews and design issues.

On occasion, 'first principles' reviews are conducted to test whether MPI's cost recovery frameworks and legislation remain fit for purpose.

## 5.6 GOODS AND SERVICES TAX (GST)

The fees and levies in this CRIS are GST-exclusive.

# 6 COST RECOVERY PRINCIPLES AND THE OVERALL APPROACH TO COST RECOVERY

This chapter summarises MPI's Cost Recovery Principles, how they relate to each other, and what this means for the overall approach to cost recovery.

## 6.1 MPI'S COST RECOVERY PRINCIPLES

MPI's four Cost Recovery Principles are:

- Transparency – costs are transparent
- Justifiability – costs are reasonable
- Efficiency – net benefits are maximised, and
- Equity – costs are fair.

These principles are set out in MPI's cost recovery guidelines,[4] and most of MPI's legislation[5].

The principles build on each other with Transparency and Justifiability providing a foundation to the consideration of, and sometimes trade-offs between, Efficiency and Equity. Essentially, MPI can only cost recover if it has sufficiently met the Transparency and Justifiability principles.

Once the Transparency and Justifiability principles have been met, the Efficiency and Equity principles state that the beneficiaries of a service should generally pay for that service. That is, beneficiaries pay 100% of costs of a service they use unless there is a strong efficiency or equity reason for why they should not.

A more comprehensive description of the principles and how they relate to each other is set out in Appendix 1.

## 6.2 OVERALL APPROACH TO COST RECOVERY

### 6.2.1 BENEFICIARIES GENERALLY PAY

Beneficiaries (customers and other industry participants) should generally pay for the services they demand and use.

Charging beneficiaries encourages them to demand and use only the quantity and quality of services they value highly enough. If the costs of services are subsidised by others, beneficiaries would demand more and higher quality services without concern for how those services are funded. The higher demand is an inefficiency, as it leads to more resources being used in the provision of services than their beneficiaries actually value or are willing to pay for.

Charging beneficiaries helps ensure that the quality and volumes of MPI services are not higher than is economically efficient.

### 6.2.2 WHEN BENEFICIARIES MIGHT NOT PAY

Beneficiaries might not pay full costs in four situations:

#### 6.2.2.1 TRANSPARENCY AND JUSTIFIABILITY

The first is where MPI has not sufficiently demonstrated that it is doing all it reasonably should to keep costs low (i.e. that it cannot meet the Transparency and Justifiability principles).

If MPI has not sufficiently demonstrated that past expenditure is justified, then write-offs might occur. If MPI has not sufficiently demonstrated that expected future expenditure is justified, then it may be appropriate for MPI to:

- change fees/levies to a level that can be justified for the time being, and
    - cover the remainder of costs, or

[4] *Ministry for Primary Industries Cost Recovery Policy Guidance*, MPI Information Paper No. 2018/08

[5] Including the Agricultural Compounds and Veterinary Medicines Act 1997 and the Animal Products Act 1999 which are relevant to large parts of this CRIS. The Animal Welfare Act 1999 and Biosecurity Act 1993, which are relevant to one design change in this CRIS, name only equity and efficiency.

    - recover the deficit from a future time period after further work has been undertaken
- guarantee that prices will not exceed a certain level over the next period, or
- charge fees at a fixed level, rather than variable with time, to encourage efficient service delivery.

#### 6.2.2.2 ADMINISTRATION COSTS

The second is where the administrative costs of charging (e.g. invoicing, collection) are excessive compared to the revenue raised or the efficiency gain of precisely charging beneficiaries.

#### 6.2.2.3 EXTERNALITIES

The third is where there are externalities. Externalities are positive or negative impacts on third parties that result from the demand and supply of a good or service. MPI primarily deals with negative externalities. An example of a negative externality is consumers demanding, and importers supplying, overseas products, creating a biosecurity risk from pest incursions to domestic farmers. In this example, charging importers for MPI activities around managing negative externalities encourages importers to reduce risk at their end and, therefore, the need for MPI services.[6]

#### 6.2.2.4 EQUITY

The fourth is where the Government determines that there are equity (fairness) reasons why the Government, or some other party, should contribute to costs. Equity involves value judgements. It will normally be considered fair that beneficiaries or exacerbators pay (in line with the Efficiency principle), but there may be reasons why Government might want to make a contribution, e.g. because Government wants to support small businesses or emerging industries, or because parties cannot afford to pay and the Government would rather not see parties stop operating.

[6] Administration costs of charging to account for externalities are also relevant.

# EXPENDITURE AND REVENUE REVIEWS

# 7 ESTABLISHMENTS

## 7.1 SUMMARY

Establishment fees pay for a range of food safety, biosecurity and animal welfare verification services to enable overseas market access for the red meat sector.

Expenditure has and is expected to continue to exceed revenue. Unless addressed this will result in an increasing memo account deficit and ultimately write-offs at taxpayer expense. $0.63 million is already expected to be written-off at a cost to public funding by the end of this financial year, with $1.52 million remaining as a recoverable deficit. Total accumulated under-recovery is forecast to be $10.81 million by the end of 2025/26 with a total of $0.85 million being written-off by 2025/26 with the rest ultimately written-off over future years.

Deficits have arisen due to small increases in input costs including vet salaries that have accumulated over the eight years since the last time fees were reset in 2015.

The preferred option – Option (2) – increases fees by around 11%. This is equivalent to 1.3% increases per annum since 2015, and much lower than inflation in consumer prices of 2.8% per annum and in vet services surveyed by Statistics New Zealand of 3.8% per annum.

The preferred option avoids all but a forecast $0.63 million (which is unavoidable) of the $10.81 million being written-off.

The preferred option is expected to have a negligible impact on the industry as a whole, including around a 0.04% increase in export prices. The impact will be higher and lower than this for different meat types, with bovine least impacted and smaller-volume meats like deer, pig, and goat more impacted though still to a small degree.

By fully recovering recoverable costs, Option (2) best meets the Efficiency principle, satisfies the Transparency and Justifiability principles, and no reasons under the Equity principle have been identified for why Option (2) should not be preferred.

The Meat Industry Association supports Option (2), which is also a requirement under legislation for making a change part-way through a financial year.

## 7.2 INDUSTRY BACKGROUND

### 7.2.1 RECENT RED MEAT SECTOR PERFORMANCE

The red meat sector as a whole has grown in value both before and since COVID-19.

In the five years before COVID-19 to the end of 2019, the value of red meat exports grew by 6.3% (5.1% CPI-adjusted[7]) per annum.[8] This was made up of export volume increases of 1.2% per annum, and price increases of 5.1% (3.9% CPI-adjusted) per annum. Increases in volumes and prices indicates that world demand for New Zealand red meat growing was the main driver.

Since COVID-19, volumes and inflation-adjusted prices have been subdued with[9] the value of red meat exports growing by 4.9% (0.5% CPI-adjusted) per annum. Increases in export prices have been 4.4% (0.0% CPI-adjusted) per annum with export volumes increasing 0.5% per annum.

[7] Consumers price index.
[8] Red meat here includes bovine, sheep, deer, goat, and pig meat and excludes by products, fats, etc. The calculations compare the year to December 2019 with the year to December 2014.
[9] Comparing the year to March 2023 to the year to December 2019.

**Figure 1: Red meat export volume and inflation-adjusted prices[10]**

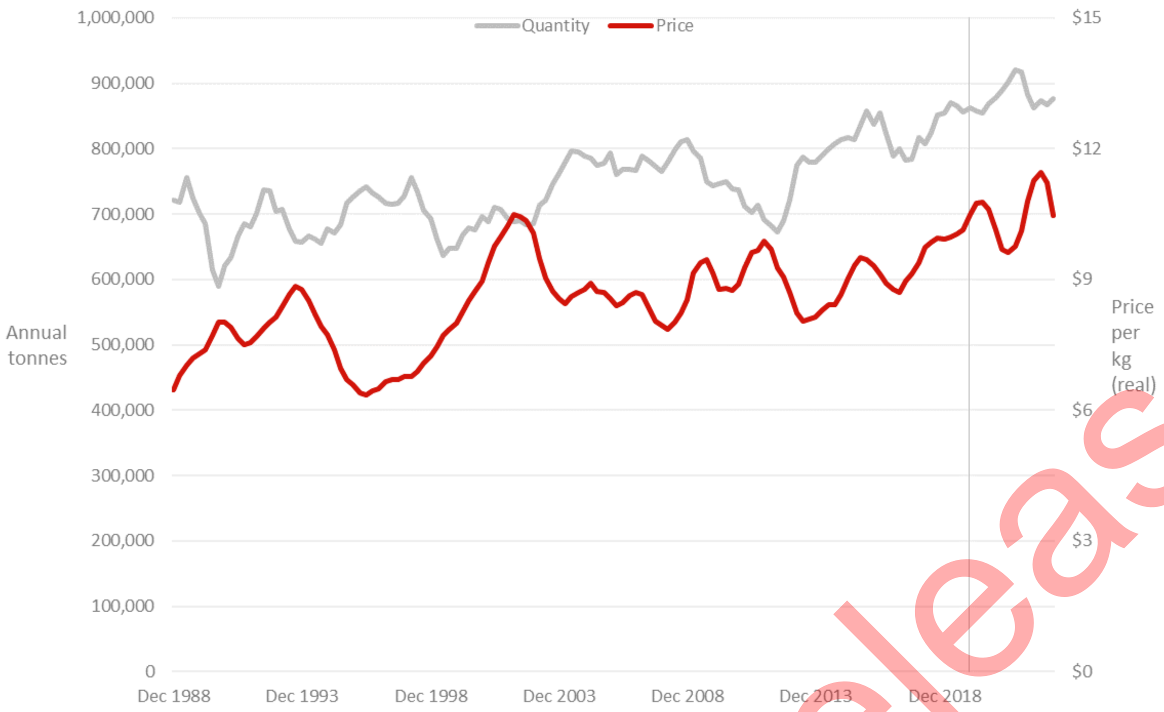


**Figure 2: Red meat export inflation-adjusted value**




### 7.2.2 VARIATION WITHIN THE SECTOR

How exports volumes, values and prices have tracked varies by meat type. For instance, while beef has increased in volume and price consistent with strong increases in demand before and after the emergence of COVID-19, venison is characterised by supply decreases before COVID-19 and supply increases after COVID-19.

[10] Prices are CPI-adjusted to the base of March 2023.
The vertical grey line in figures in this CRIS marks December 2019, separating before and after the emergence of COVID-19.

**Figure 3: Summary of how industry has tracked recently according to price and volume data**

| Meat type | Before the emergence of COVID-19 | | | | After the emergence of COVID-19 | | | |
|---|---|---|---|---|---|---|---|---|
| | Volume | Price | Value | Demand or supply driver | Volume | Price | Value | Demand or supply driver |
| Bovine | ↗ | ↗ | ↗ | Demand increase | ↗ | ↗ | ↗ | Demand increase |
| Sheep | ↘ | ↗ | ↗ | Supply decrease | ↘ | – | ↘ | Demand and supply decrease |
| Deer | ↘ | ↗ | ↘ | Supply decrease | ↗ | ↘ | ↘ | Supply increase |
| Goat | ↗ | ↗ | ↗ | Demand increase | ↘ | ↗ | ↘ | Supply decrease |
| Pig | ↗ | ↘ | ↗ | Supply increase | ↗ | ↗ | ↗ | Demand increase |

### 7.2.3 FORECASTS

MPI's *Situation and Outlook for Primary Industries* report expects a decline in export value across the June 2022/23 and 2023/24 years with global economic weakness reducing prices in 2022/23 and 2023/24 and volumes peaking in 2022/23 and falling in 2023/24. Overall, the report forecasts a 5.9% fall bovine meat export value, a 2.3% fall in sheep meat export value, and a 5.9% increase in deer meat export value.[11]

Based on data to March 2023, the forecast for 2022/23 has so far been on track with some differences such as sheep meat prices being lower than forecast and venison prices being higher than forecast.

**Figure 4: How forecasts are tracking**

| Meat type | 2022 actual | 2023 forecast | 2024 forecast | 2023 actual so far | Notes |
|---|---|---|---|---|---|
| **Beef** | | | | | |
| Tonnes | 482,860 | 484,100 | 460,200 | 350,337 | On track – 72% of forecast volume 75% through the year and quarter 4 is historically relatively high |
| Price per kg | $9.49 | $9.35 | $9.30 | $9.37 | On track – final price might turn out to be a bit lower than forecast |
| Value ($m) | $4,581 | $4,540 | $4,270 | $3,284 | On track |
| **Sheep** | | | | | |
| Tonnes | 364,230 | 377,400 | 372,500 | 278,019 | On track – 74% of forecast volume and quarter 4 is historically relatively high |
| Price per kg | $11.81 | $11.29 | $11.17 | $10.38 | Lower than forecast and likely to end lower still by the end of quarter 4 |
| Value ($m) | $4,303 | $4,260 | $4,160 | $2,887 | Tracking lower than forecast |
| **Deer** | | | | | |
| Tonnes | 13,855 | 13,500 | 13,300 | 9,534 | Tracking a little lower than forecast |
| Price per kg | $12.27 | $12.75 | $13.25 | $14.21 | Higher than forecast |
| Value ($m) | $170 | $170 | $180 | $135 | Tracking higher than forecast |

## 7.3 SERVICE BACKGROUND

### 7.3.1 HIGH-LEVEL SERVICE DESCRIPTION

MPI provides a range of food safety, biosecurity and animal welfare verification services to enable overseas market access. These services are either provided as 'Circuits' or 'Establishments'. Circuits involves MPI staff visiting businesses on a temporary, as-needed basis ('circuit' referring to an MPI verifier completing a circuit of leaving an MPI base and travelling to several premises before returning to base). Establishments involve staff being based at a premise due to the large amount of work.

Fees for Circuits were reset in 2022. This CRIS considers options around Establishment fees.

[11] Goat and pig meat are not forecast separate from other products.

### 7.3.2 HOW HAVE THESE SERVICES PERFORMED?

Since 2018, MPI has published a Red Meat Report which reports annually on the performance of all services for the red meat sector including Establishments. This helps provide transparency to the sector, providing an opportunity to test how efficient MPI is with fee revenue.

These reports are an area of ongoing improvement with the focus of early reports being on financial performance. This means information about performance over time is limited, but the June 2022 report covered a range of outputs and outcomes across the 2021/22 year including:

- 1,200 on-farm audits (an annual requirement for EU market access)
- EU authorities conducted an audit of MPI's on-farm verification programme and raised no concerns
- a successful audit by the United States Department of Agriculture
- delivery of training to all corporate-affiliated red meat establishment plants on the Optimising Operator Ownership programme which shifts verification focus from individual non-compliance with risk management plans to a systems-level focus
- audits of red meat establishments and food production businesses against COVID-19 requirements.

### 7.3.3 WHAT OTHER CONSULTATION AND REPORTING TAKES PLACE WITH INDUSTRY?

MPI undertakes other consultation with industry in addition to the Red Meat Report.

The main is forum is the MIA-MPI Strategic Directions Group with the read meat industry representative organisation, the Meat Industry Association.

The Group acts as an accountability mechanism for MPI and provides an opportunity for industry to help identify cost savings, service improvements and which services are of most value.

### 7.3.4 HOW ARE THESE SERVICES FUNDED?

#### 7.3.4.1 LEVEL OF THE CHARGE

Services may be provided by a vet or a supervising vet. Supervising vets have greater responsibilities and educational requirements and, so, a higher salary which translates to a higher hourly rate. The Establishments fee is higher for a supervising vet.

Fees are made up two components. The first component covers the cost of time vets or supervising vets spend verifying. The second component is a 'programme charge' covering overheads such as IT, HR, and legal costs.

The current fees have been in place since 2015.

**Figure 5: Current fees[12]**

| Fee | Vet | Supervising vet |
|---|---|---|
| Total fee per hour | $111.34 | $116.14 |
| Vet component | $70.30 | $75.10 |
| Programme charge | $41.04 | $41.04 |

The vet component can be charged at time and a half or double time where the vet works outside of normal hours. The programme charge is only applied to normal hours, not overtime hours.

Additional charges exist around miscellaneous costs involved with delivering verification services, including travel costs and meal allowances. The expenditure and revenue from these cost items are included in the financials in this CRIS but are charged for separately and not proposed to change.

#### 7.3.4.2 REGULATIONS

The fees appear in Part 7 of Schedule 1 of the Animal Products (Fees, Charges, and Levies) Regulations 2007 and in Part 7 of the Schedule of the Animal Products (Dairy Industry Fees, Charges and Levies) Regulations 2015.

[12] This figure presents the fee for normal time. Time and a half and double time is charged on the vet component when applicable.

Normally, changes take place at the start of the financial year on 1 July. The timing of this year's package of cost recovery changes means that changes won't be implemented by 1 July 2023. In this situation, the Animal Products Act 1999 requires[13] that the Minister be satisfied that affected parties 'agree or substantially agree' with the changes.

#### 7.3.4.3 WHY IS A FEE APPROPRIATE?

Verification services are a 'private good'[14].

A fee is charged to businesses to recover costs. If industry as a whole benefitted rather than particular businesses, then a levy across industry would be appropriate. Crown funding would be appropriate if benefits accrued to wider society rather than particular businesses or industry as a whole.

## 7.4 PROBLEM

### 7.4.1 HOW HAS REVENUE AND EXPENDITURE TRACKED OVER TIME?

Figure 6 sets out revenue and expenditure as far back as is available, drawing on data in the annual Red Meat Reports.

**Figure 6: Total revenue and expenditure 2017/18 to 2025/26 ($m) under current fees**

| | Actual | | | | | Forecast | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2017/18 | 2018/19 | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 | 2024/25 | 2025/26 |
| Revenue | 32.08 | 31.59 | 30.90 | 30.82 | 32.21 | 31.66 | 31.66 | 31.66 | 31.66 |
| Expenditure | 31.47 | 32.51 | 31.11 | 30.83 | 31.93 | 32.96 | 33.78 | 34.56 | 35.30 |
| One-off changes | | -1.19 | | | | 0.63 | 0.21 | 0.01 | |
| Surplus/deficit | 0.61 | -0.92 | -0.20 | -0.01 | 0.28 | -1.30 | -2.12 | -2.90 | -3.64 |
| End balance | 1.19 | -0.92 | -1.12 | -1.13 | -0.85 | -1.52 | -3.43 | -6.32 | -9.96 |

Figure 6 shows that by the end of 2017/18 revenue had been greater than expenditure for at least two years such that a surplus of $1.19 million had arisen. This was refunded in 2018/19.

2018/19 saw a modest reduction in revenue (which persisted through to 2020/21) and a modest increase in expenditure (which did not persist). This resulted in, at the same time as the surplus was refunded, and almost equal-sized deficit arising of $0.92 million. $0.63 million of the 2018/19 deficit is expected to be written off in the 2022/23 year at a cost to public funding. Further amounts would be written off in 2023/24 and 2024/25 under current Establishment fees.

From 2019/20 to 2021/22, revenue and expenditure were essentially in balance despite cost inflation during this time. The decline in revenue was offset by MPI not filling vacancies.[15]

The forecast period is made up of a forecast of constant revenue at 2021/22 levels (minus a one-off adjustment that only occurs in 2021/22) and forecast expenditure of about 2.5% per annum[16].

### 7.4.2 WHAT IS THE NATURE OF THE PROBLEM?

The deficit that has arisen under the fees is an efficiency problem – it could be due either the fee to fees being kept too low for a desired level of service, or expenditure is too high, or a combination of both.

[13] Section 115(2)(b).

[14] A private good is one where a person/business can be excluded (e.g. don't receive the service if they don't pay), and where the benefits accrue to the person/business (the benefits are 'non-rival') rather than to the whole industry or to society.
Verification services are a private good because they are only provided by MPI when paid for and the benefits accrue to the business that receives the service. For example, individual businesses receive benefits of higher revenue from being able to export when ve rified. Industry or society as a whole does not benefit from any individual business exporting.

[15] The decline in staffing means more services are provided through overtime charged at overtime rates to businesses. This maintains the level of service and revenue. Cost savings arise because not all hours spent by verifiers are billable (e.g. training, annual leave). The savings on non-billable hours more than offsets the higher overtime charges.
While overtime is sustainable for staff on a temporary basis, the impact on staff welfare means this is not a long-term solution.

[16] 3.2% in 2022/23, 2.5% in 2023/24, 2.3% in 2024/25, and 2.1% in 2025/26.

If expenditure is reasonable, eliminating a deficit with public funds may also be considered as inequitable by parts of society.

Deficits, therefore, cause the Efficiency and, potentially, Equity principles to not be met.A deficit has arisen under the fees. Deficits are an efficiency problem – either the fee is too low for a desired level of service, or expenditure is too high, or a combination of both.

### 7.4.3 WHAT IS THE SIZE OF THE PROBLEM?

MPI is forecasting that expenses will have exceeded revenue by a total of $2.15 million by the end of 2022/23 with $0.63 million of that having to be written-off at a cost to public funding[17] whether fees change or not.

These deficits are forecast to rise to a total of $10.81 million by the end of 2025/26 with a total of $0.85 million being written-off by 2025/26 with the rest ultimately written-off over future years.[18]

If MPI is meeting the cost recovery principles[19], under-recovery of costs is effectively a subsidy from public funds to industry, encouraging more use of services than is efficient.

In addition, covering written-off costs from public funding carries a deadweight loss. Deadweight loss is how much higher taxes to provide the public funding distorts taxpayer decisions to work, invest and spend. The deadweight loss associated with the expected, unavoidable, write-off of $0.63 million is $0.13 million, with an additional, avoidable, deadweight loss of $0.04 million by 2025/26 (associated with the $0.22 million write-off), and a further $1.99 million of deadweight loss over further years[20].[21]

A subsidy from public funds to industry may also be considered as inequitable by parts of society.

### 7.4.4 WHAT IS THE CAUSE OF THE PROBLEM?

Setting aside the $0.63 million which must be written off, the cause of current and future deficits is small increases in the costs of inputs, including vet time, which have accumulated over the eight years since the last time the fees were reset.

The duration since the last fee reset is not in itself a problem. New Zealand Food Safety has operated in the intervening eight years without incurring significant operating deficits that would have triggered a rate reset or write offs. The cumulative and forecast cost increases since 2015 have however now created an environment where further cost increases cannot be offset.

Demonstration of the cause of the problem appears in Chapter 7.5.1.3.2.

## 7.5 OPTIONS

### 7.5.1 IDENTIFYING OPTIONS

#### 7.5.1.1 Introduction to the process of identifying options

Conceptually, there are infinite possible options for setting fees as fees can be increased or decreased to any value. As such, we need a way to reduce the full range of feasible fees to a smaller range of fees.

MPI uses the Cost Recovery Principles, including stakeholder views, to identify a range of options that are plausible consistent with the Cost Recovery Principles. Chapter 6.2.2.1 identified options that may be considered if the Transparency and Justifiability principles have not been sufficiently met, for example.

Typically this process results in a few options (sometimes up to a dozen depending on how many cost recovery features are changing). The 'Assessment against the Cost Recovery Principles' chapter (Chapter 7.7) would then analyse the plausible options and identify a preferred option or options.

Other options may be considered during the policy development process, and ultimately discarded as not plausibly consistent with the Cost Recovery Principles.

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[17] Under legislation, deficits are written-off if not recovered within three years. This helps ensure costs are not unreasonably recovered, e.g. because so much time has passed that fee payers now might be very different from fee payers then and, so, too many costs would fall on parties that didn't contribute to the cost.
[18] Figure 6 records an end balance in 2025/26 of $9.96 million being the total deficits of $10.81 million minus total write-offs of $0.85 million.
[19] The degree to which the cost recovery principles are being met is discussed in Chapters 7.5.1.3 and 7.7.
[20] The $2.0 million is just from expenditure up to 2025/26 – years beyond this would have their own deficits which would be eventually written off.
[21] Deadweight loss is estimated at 20% of public funding, consistent with Treasury's cost benefit analysis guidelines.

#### 7.5.1.2 Summary

Overall, MPI and industry as represented by the Meat Industry Association considers that MPI's consultation means MPI has sufficiently met the Transparency and Justifiability principles.

The Efficiency principle then says that costs should be recovered from beneficiaries, being the red meat sector. The Meat Industry Association agrees with this.

The Equity principle then asks whether there are fairness reasons to depart from this approach. With the Meat Industry Association expressing support for the 'beneficiary pays' approach in feedback, MPI has identified no reasons to depart from this approach. Ultimately, it is up to the Government to decide what is fair and it may identify equity concerns and pursue other options.

#### 7.5.1.3 Detail

As above, beneficiary pays is efficient and, unless the Government identifies equity concerns, will be deemed equitable. This section, then, focusses on the Transparency and Justifiability principles.

##### 7.5.1.3.1 Transparency

Public consultation was open for about five weeks. The consultation document included the final options considered in this CRIS and one other option that is discarded in this CRIS. The consultation document provided some limited financial data and justification for the options.

Additionally, as noted in in Chapters 7.3.2 and 7.3.3, other consultation takes place around financial and service performance and service levels through other forums.

The Meat Industry Association sought more information which MPI provided and is covered in Chapters 7.4.1 above and 7.5.1.3.2 immediately below. The information included a longer time-series of financial data and a deeper explanation of whether past and forecast expenditure is reasonable.

The Meat Industry Association was satisfied with this information. As a result, MPI is confident it has met the Transparency principle.

##### 7.5.1.3.2 Justifiability

Expenditure under Establishment services is made three broad groups:

- vet time
- miscellaneous direct costs such as travel cost, meal allowances
- overhead/indirect costs such as IT, HR, and legal costs.

This chapter looks at whether the change in costs by group seem reasonable. The Meat Industry Association was satisfied with this information. MPI is confident that it has sufficiently met the Justifiability principle.

###### 7.5.1.3.2.1 Vet time

In summary, the expenditure on vets appears to be reasonable with a risk that it is on the low side. Expenditure increases (and the fees needed to pay them of between 1.6% and 2.0% annualised increases) are significantly lower than past inflation including of vet services surveyed by Statistics New Zealand, where inflation in the cost of services has been 3.8% per annum.

The increase in vet hourly rates needed to cover vet salaries is 13.5% from $70.30 to $79.80 for vets and 17.3% from $75.10 to $88.10 for supervising vets.

These fees were last reset in July 2015. The 13.5% and 17.3% increases in hourly rates are equivalent to annual increases of 1.6% and 2.0% respectively for the eight years between 2015 and 2023.

The vet hourly rates are set at levels that are expected to bring the account into balance by 2025/26, including recovering the accumulated deficit. Similarly, the rates set in 2015 were what was expected to bring the account into balance likely including any accumulated deficit at the time.

As such, the proposed increase in fees will not perfectly match other data and information that will help indicate whether the increases are reasonable, but we should expect them to be fairly close.

Relevant other data and information that can help judge whether the proposed increases are reasonable include:

- The salary MPI pays vets has increased by an annualised average of 1.6% per annum between 2016 and 2022 (the period over which data has been able to be retrieved), while the salary MPI pays supervising vets has increased by an annualised average of 1.2% per annum.

- The 1.6% per annum for vets is close to the 1.6% proposed in fees. The 1.2% for supervising vets is a little lower than the 2.0% proposed in fees, however the 2.0% may be considered reasonable as it implies a possible addressing of the low past 1.2% increases.
- MPI's current salaries are $106,674 for a vet and $128,665 for a supervising vet. This is similar to the average salary reported by Seek of between $100,000 and $110,000.
- The proposed increase in fees is lower than past inflation and forecast inflation in consumer prices (the consumers price index, CPI). Actual consumer price inflation has averaged 2.9% between June 2015 and March 2023, with forecast inflation after than expected to higher at around 5.5% for the 2023/24 year and 4.3% for the 2024/25 year .
- The proposed increase is lower than past inflation in the cost of veterinary services surveyed by Statistics New Zealand. Actual inflation in the price of veterinary services has averaged 3.8% between June 2015 and December 2022.
- MPI is still carrying vacancies[22] which is not sustainable long term. Higher salaries need to be offered to recruit vets.

#### 7.5.1.3.2.2 Miscellaneous direct costs and overhead/indirect costs

These two groups are considered together as data limitations mean it is not possible to separate overheads and miscellaneous expenditure for years prior to 2021/22.

In summary, the increase in expenditure is much less than inflation and volume growth would otherwise result in. This suggests efficiency gains have occurred. Overall expenditure is expected to increase by about 1.0% per annum. This is much less than inflation of between 2.7% and 4.5% depending on the cost index and time frame preferred. The 1.0% is also estimated to be more than half caused by increased volume, meaning a true price increase is about 0.4% per annum.

For the forecast period, overheads and miscellaneous expenditure is forecast to total around $11.0 million per year, made up $10.1 million on overheads and $0.8 million from miscellaneous expenditure. This is up 5.0% on the $10.4 million average between 2017/18 and 2020/21[23].

Identifying precisely how much of this expenditure increase is due to volume changes, cost inflation, and efficiencies is not possible with available data but expenditure increases are less than inflation suggesting that there have been efficiencies:

The 5.0% increase in expenditure is equivalent to an annual average growth of 1.0% between the midpoints of the 2017/18 to 2020/21 and 2022/23 to 2025/26 periods.

Assuming, for now, that volumes are expected to be approximately the same, the 1.0% is much less than various inflation comparisons including:

- actual inflation since June 2017 of 3.5% per annum in consumer prices and of 2.7% per annum in an MPI index[24] of costs
- actual inflation since June 2019 (the midpoint of the actual period) of 4.5% per annum in consumer prices and of 2.9% in the MPI index
- actual and forecast[25] inflation of 4.5% per annum in consumer prices from June 2019 to June 2024.

The proposed change to the programme component of Establishment charges which covers overhead costs would increase revenue by only 2.0% from $9.9 million to $10.1 million.[26] MPI's forecast for is for no change in miscellaneous expenditure which are funded by direct charges separate from the Establishment charges.

Overall, overhead and miscellaneous revenue and expenditure is forecast to increase by only 1.8%. The 1.8% is much less than the 5.0% increase in overheads and miscellaneous expenditure meaning that increased volumes

[22] See Chapter 7.4.1 and footnote 15.
Under cost recovery settings rate increases are triggered when deficits become unsustainable rather than when costs increase. This is appropriate as cost increases are often offset by decreases in other costs or through operating changes or efficiency savings. In this case, the cost savings from vacancies temporarily offset cost increases from salaries. An unsustainable deficit is defined under MPI policy as occurring where a surplus or deficit is greater than four months revenue (a third of annual revenue).
[23] 2021/22 has been excluded because the numbers are still being validated.
[24] An index made up of the *Labour cost index - Central Government Administration, Defence and Public Safety* and *Producers price index (inputs) - Central Government Administration, Defence and Public Safety* weighted by MPI's total spending on personnel and other inputs.
[25] Reserve Bank of New Zealand, February 2023 Monetary Policy Statement, https://www.rbnz.govt.nz/hub/-/media/project/sites/rbnz/files/publications/monetary-policy-statements/2023/mpsfeb23-data.xlsx
[26] While the programme charge is proposed to increase by 25.2% from $41.04 to $51.40, the increase in revenue is only 2.0%. The reason for this is that the programme charge has previously been charged on budgeted rather than actual hours. Budgeted hours are higher than actual hours.

should explain the remaining 3.0% increase in expenditure.[27] If this is correct, the true price component is about 0.4% per annum compared to inflation of between 2.7% and 4.5% above.

## 7.5.2 FINAL OPTIONS AND KEY FEATURES

### 7.5.2.1 Fees

As a result of sufficiently meeting the Transparency and Justifiability principles[28], the only option considered, other than the status quo, is that which fully recovers costs:

- Option (1) – The status quo. The fees are unchanged and the deficits are written-off over time.
- Option (2) – Full cost recovery. The fees are increased to recover the accumulated deficit and forecast expenditure through to 2025/26.

**Figure 7: Options**

| Fee | Option (1) – status quo | | Option (2) – full cost recovery | | Percent increase since 2015 | |
|---|---|---|---|---|---|---|
| | Vet | Supervising vet | Vet | Supervising vet | Vet | Supervising vet |
| Total fee per hour | $111.34 | $116.14 | $131.20 | $139.50 | 8% | 12% |
| Vet component | $70.30 | $75.10 | $79.80 | $88.10 | 14% | 17% |
| Programme charge | $41.04 | $41.04 | $51.40 | $51.40 | 2% | 2% |

Note that the percentage increases in Figure 7 for the programme charge and the total fee are not a straight comparison of the before and after fees.

For instance, the increase in the programme fee appears to be a 25% increase from $41.04 to $51.40, but the actual increase is only 2.0% because the basis for the fee is changing from budget hours to actual hours. Actual hours are lower than budgeted hours so the fee needs to be higher on paper to recover the same revenue increase of 2.0%.

As the programme charge is one component of the total fee, the actual increase in the total fee is less than it appears.

### 7.5.2.2 Expenditure and revenue

Expenditure and revenue under Option (1) is in Figure 6 in Chapter 7.4.1.

Figure 8 sets out the new revenue, surplus/deficit and balance lines under Option (2).

The increase in fees is expected to increase revenue by $9.61 million in total between 2023/24 to 2025/26. This avoids forecast write-offs in 2023/24 and 2024/25, recovers the accumulated deficit at the end of 2022/23, and sees the account reaching near balance in 2025/26.

**Figure 8: Total revenue and expenditure 2017/18 to 2025/26 ($m) under Option (2)**

| | Actual | | | | | Forecast | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2017/18 | 2018/19 | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 | 2024/25 | 2025/26 |
| Revenue | 32.08 | 31.59 | 30.90 | 30.82 | 32.21 | 31.66 | 35.05 | 35.05 | 35.05 |
| Expenditure | 31.47 | 32.51 | 31.11 | 30.83 | 31.93 | 32.96 | 33.78 | 34.56 | 35.30 |
| One-off changes | | -1.19 | | | | 0.63 | | | |
| Surplus/deficit | 0.61 | -0.92 | -0.20 | -0.01 | 0.28 | -1.30 | 1.27 | 0.49 | -0.25 |
| End balance | 1.19 | -0.92 | -1.12 | -1.13 | -0.85 | -1.52 | -0.25 | 0.24 | -0.01 |

## 7.5.3 DISCARDED OPTIONS

Some options that are feasible were discarded as not plausibly consistent with the Cost Recovery Principles.

[27] Higher volumes result in a greater share of overheads.
[28] As discussed in Chapter 5.5.1.2.

#### 7.5.3.1 NOT RECOVERING MOST HISTORICAL DEFICITS

This option was considered at consultation stage but has since been discarded. The option focussed on recovering forecast deficits, though also recovering enough further revenue to avoid the $0.22 million in write-offs. This option would have seen fees increase revenue by 9.3% compared to Option (2)'s 10.7%.

The discussion document was not clear why this option was included but an option that recovers future costs only may be appropriate where future costs have been justified but historical costs have not. The discussion document did not analyse historical costs so this may be why it was included.

Recovering the additional amount to avoid the write-offs may have been justifiable if MPI was confident it would, in future, justify historical costs and, thus, needed to avoid short-term risks that public funding would subsidise industry.

In any case, historical data has now been obtained going back almost to when the fees were last reset and, as in Chapter 7.5.1.3.2, MPI is now confident that both forecast and historical expenditure is justified. As such, this option could not plausibly meet the Cost Recovery Principles.

#### 7.5.3.2 GRADUATED COST RECOVERY

During previous cost recovery consultations[29], some industry participants in other sectors have suggested graduated changes to charges. Graduated changes would see lower fees (though still higher than the status quo) in year one and higher charges in year three to lessen the immediate impact on businesses. These suggestions were made in situations of heavy financial pressure on industry due to COVID-19.

The suggestion falls under the Equity principle: that it is considered fair by those proposing this approach that businesses doing better in the future subsidise businesses under pressure in the early years, and that this outweighs the efficiency costs of the subsidy and the administration costs for businesses and MPI of multiple changes in a three-year period.

While the red meat sector is forecast to decline in value[30] by around 13.9% in real terms (accounting for CPI inflation) between the two years between 2021/2022 and 2023/24, much of the drop should be temporary for the period of the economic downturn and is less than the 38.7% increase in real value in the five years to June 2022.

Additionally, while this option was not raised in consultation, it was not suggested by the Meat Industry Association.

This option has been discarded on the basis of there being no strong Equity-based desire to consider this option.

## 7.6 ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

### 7.6.1 INTRODUCTION

This section sets out the immediate financial impact of options at the industry and business-level, and then considers how the financial impact feeds through to changes in prices and volumes over the medium- to long-term.

### 7.6.2 IMMEDIATE INDUSTRY-LEVEL IMPACTS

Option (2) is forecast to increase revenue by 10.7% in the 2023/24 to 2025/26 period from $31.66 million per annum to $35.05 million per annum.

[29] Consultation in early 2021 on changes to germplasm, poultry, bee, and dairy levies.
[30] Due to weakening world demand. See Chapter 5.2.3.

### 7.6.3 IMMEDIATE BUSINESS-LEVEL IMPACTS

On average, individual businesses will face a 10.7% increase in the cost of Establishment services.

The precise impact on individual businesses will depend on how many hours they use that are normal hours versus overtime hours and how close budgeted hours were to actual hours. This is because the programme charge only applies to normal hours and not overtime hours and as the programme charge is moving from being based on budget hours to being based on actual hours.

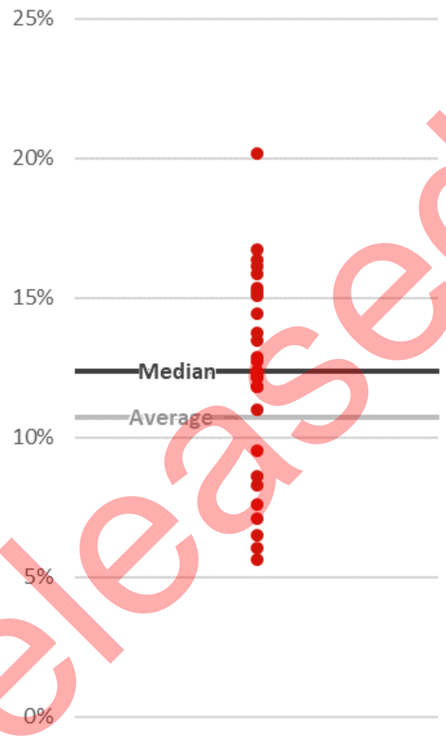
In 2021/22, 28 businesses across 58 sites paid Establishment fees.

Using the 2021/22 business-level data, the increase in cost could range from between 5.6% and 20.2%. At 12.4%, the median increase in cost is higher than the average.

As the charge is a fee for hours worked and not a levy on production, there is little information about how the cost increases varies by size of business. Additionally, the small number of businesses means that analysis could result in commercial sensitivities and breach the purpose for which information is supplied.

MPI can say that there is a slight positive, though very weak, relationship between businesses with more premises and the average cost they pay per premise. This perhaps suggests that businesses with more revenue use face more cost, though this potential conclusion has low confidence.

**Figure 9: Increase in cost by business**




There appears to be a stronger relationship (with moderate confidence) between the value of exports by meat type[31] and the average total cost paid by businesses. That is, that businesses processing meat types with high volumes have much lower average costs from Establishments. This is consistent with economies of scale – businesses with larger volumes are able to spread costs that don't vary hugely by volume across those larger volumes, reducing the impact of cost increases.

### 7.6.4 MEDIUM- TO LONG-TERM MARKET-LEVEL IMPACTS

Changes in fees are changes in business costs. Increased fees feed through to reduced profits and, over the medium- to longer-term, higher market prices and lower volumes until normal profitability is restored.

At an industry-wide level, the total costs of Establishments are forecast to be $35.05 million, of which $3.39 million per annum is due to the increase in fees.

This compares to total export value of $9.0 billion in the year to March 2023 (though this is expected to fall slightly during the forecast period). Establishment services, therefore, are expected to equal 0.4% of export value, with the increase in cost being 0.04%. Overall, if the cost increase was fully passed on, it would result in around a 0.04% increase in price and a similar-sized reduction in volumes.

MPI data is not detailed enough to estimate the impact by meat type with any level of confidence. However, using the crudely estimated economies of scale referred to in Chapter 7.6.3, the impact for bovine could be around half of the 0.04% at 0.02% and for smaller volume meat types, four or more times the 0.04% at 0.16%. These estimates are very rough – while we have high confidence in their direction relative to the 0.04%, there is low confidence in the level.

## 7.7 ASSESSMENT AGAINST THE COST RECOVERY PRINCIPLES

This section assesses the options using MPI's Cost Recovery Principles and approach as described Chapter 6. As the Cost Recovery Principles and industry views were used to identify plausible options and this resulted in only one option other the status quo, this section effectively only summarises and refers to earlier analysis.

[31] Data used in Chapter 7.2.

### 7.7.1 TRANSPARENCY AND JUSTIFIABILITY

#### 7.7.1.1 TRANSPARENCY

Between the on-going consultation MPI has with industry, the information in the consultation document, and the further consultation with the Meat Industry Association where information contained in this CRIS was provided – including revenue and expenditure over time and an analysis of the causes of changes – we consider, and the Meat Industry Association effectively agrees, that the Transparency principle has been met.

#### 7.7.1.2 JUSTIFIABILITY

Justifiability requires that costs be reasonable.

From the analysis in Chapter 7.5.1.3.2, we consider, and the Meat Industry Association effectively agrees, that the Justifiability principle has been met.

### 7.7.2 EFFICIENCY AND EQUITY

#### 7.7.2.1 EFFICIENCY

Option (2) maximises efficiency by fully recovering costs that are still recoverable (that is, excluding the $0.63 expected to be written-off in the 2022/23 year).

Fully recovering costs encourages businesses to use services only when the value exceeds their cost. Fully recovering costs avoids write-offs at a cost to public funding and the associated deadweight loss of $0.04 million by 2025/26, and a further $1.99 million of deadweight loss over further years (see Chapter 7.4.3).

Conversely, Option (1) does not fully recover costs, encouraging greater use of services than is efficient and resulting in deadweight loss of about $0.04 million by 2025/26, and a further $1.99 million of deadweight loss over further years

Overall, Option (2) best achieves the Efficiency principle.

#### 7.7.2.2 EQUITY

The Equity principle asks whether there are fairness reasons to depart from the most Efficient approach. With the Meat Industry Association expressing support for the 'beneficiary pays' approach in feedback, MPI has identified no reasons to depart from this approach. Ultimately, it is up to the Government to decide what is fair and it may identify equity concerns and pursue other options.

Overall, MPI's application of the Equity principle has not identified any reason to depart from Option (2) as the preferred option.

## 7.8 INDUSTRY FEEDBACK

MPI released a consultation document for public feedback over about five weeks. The consultation document included the final options considered in this CRIS and one other option that is discarded in this CRIS. The consultation document provided some limited financial data and justification for the options.

Additionally, as noted in in Chapters 5.3.2 and 5.3.3, other consultation takes place around financial and service performance and service levels through other forums.

The Meat Industry Association sought more information which MPI provided and is covered in Chapters 5.4.1 above and 5.5.1.3.2 immediately below. The information included a longer time-series of financial data and a deeper explanation of whether past and forecast expenditure is reasonable.

The Meat Industry Association was satisfied with this information and supports Option (2). MPI considers that the Minister can be satisfied that affected parties agree with the change for the purposes of making a change part way through a financial year (see Chapter 7.3.4.2).

## 7.9 CONCLUSION

The current fees will continue to raise less revenue than is needed. This is expected to result in under-recovery of $10.81 million by the end of 2025/26 with a total of $0.85 million being written-off by 2025/26 with the rest ultimately written-off over future years at a cost to public funding.

Option (2) avoids all but $0.63 million of the $10.81 million being written-off.

Option (2) best meets the Efficiency principle, satisfies the Transparency and Justifiability principles, and no reasons under the Equity principle have been identified for Option (2) not to be preferred. The Meat Industry Association also supports Option (2).

## 7.10 Implementation

Changes to give effect to the increased fees will require amendments to the Animal Products (Fees, Charges, and Levies) Regulations 2007 and the Animal Products (Dairy Industry Fees, Charges and Levies) Regulations 2015.

The changes will come into force at least 28 days after Cabinet makes decisions and these decisions are Gazetted. MPI will notify fee and levy payers of the outcome of Cabinet decisions including, if applicable, new rates. MPI will also update service application forms and webpages to include any changed fees.

The changes are to update existing fees. Enforcement risks are low as the regulatory frameworks are already in place and services are only provided where paid for.

While the 28 day period provides industry with sufficient time to update their internal financial systems, primary sector producers have contracts with suppliers and customers that last longer than that. Submissions on other past cost recovery changes have mentioned contracts of six months, for example. This creates a risk for processors that they would pay higher fees for a period of time before contracts can be updated.

While MPI endeavours to consult with industry, and have final policy decisions notified, as early as some amount of risk is inevitable, for example, due to the timing of MPI's financial data availability.

Some processors may mitigate this risk by budgeting for anticipated increases after the publication of the consultation document in March, or from financial information from past Red Meat Reports. Others may temporarily bear higher debt or lower profits until contracts are renegotiated.

## 7.11 MONITORING AND REVIEW

MPI monitors all accounts on an ongoing basis in order to minimise financial surprises to fee and levy payers and to MPI.

MPI will continue to monitor Establishments revenue and expenditure on an ongoing basis and review settings if a deficit or surplus accumulates. Monitoring and review is guided by an internal MPI policy which says that charges will be reviewed when any of the following conditions are met:

- accumulated deficit or surplus is more than four months (33%) of annual revenue[32]
- the accumulated deficit or surplus is $1 million or more
- a deficit is due to be written-off, or a surplus has existed for an equivalent amount of time such that it would be written-off if it was a deficit[33].

In the case of the changes in this CRIS, for instance, the second and third conditions were met.

[32] Annual revenue is average annual revenue over the most recent three years.
[33] Typically, after four years.

# DESIGN CHANGES

# 8 Limited exemptions from animal products risk management programmes

## 8.1 BACKGROUND AND SERVICE DESCRIPTION

Anyone who processes animal materials or produces animal products (called ‘producers’ for this chapter) must register a risk management programme (RMP), according to the Animal Products Act 1999. An RMP is used to identify, mitigate, and manage hazards when working with animal materials. RMPs help ensure the product is fit for purpose for the consumer.

Producers that do not register or comply with an RMP cannot get an official assurance from MPI inspectors. An official assurance informs foreign governments that animal products shipped to their country meet their import requirements.

Sometimes situations arise which breaches a producer’s RMP, meaning they’re ineligible for an official assurance (for example, if a person delivers a shipment to a location that is not covered by the RMP). When this happens, a producer may ask MPI to issue a notice exempting the producer from operating under the RMP for a set period, under certain conditions.[34] The exemption makes the producer eligible for official assurance again.

MPI may only grant an exemption notice if there is a negligible risk to human or animal health. The notice only covers specific shipments and is not a blanket exemption.

## 8.2 STATUS QUO AND PROBLEM

After receiving an exemption request, MPI staff must draft decision and exemption documents, seek a peer review, and coordinate approvals from legal and management. It takes around nine hours on average for MPI staff to process an exemption request.

This service cannot currently be cost recovered under the Animal Product (Fees, Charges, and Levies) Regulations 2007 and the Animal Products (Dairy Industry Fees, Charges, and Levies) Regulations 2015.

Costs are currently paid for from public funding, effectively subsidising producers. This has efficiency costs of potentially overusing the service by producers as they do not face full costs and potentially under-providing the service by MPI, and from the deadweight loss[35] of public funding.

It may also be considered inequitable for public funds to pay the cost of processing exemption requests rather than those who directly benefit from the service (i.e. producers).

## 8.3 OPTIONS

We have identified the following options:

- Option (1) – The status quo. Exemptions continue to be paid for from public funds.
- Option (2) – Introduce a fee of $135 per application plus $33.75 per quarter hour beyond the first hour for exemption requests. [36] This would require amending the Animal Product (Fees, Charges, and Levies) Regulations 2007 and the Animal Products (Dairy Industry Fees, Charges, and Levies) Regulations 2015.

## 8.4 ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

It can take between three and 15 hours to process an exemption request. Option (2) would, therefore, increase cost to producers by about between $405 and $2,025 per exemption request. MPI data shows that there are few repeat applicants, so most producers who seek exemptions would only have to pay these costs once in a single year.

The average annual number of applications submitted is 27.5. At an average of nine hours, the total cost to industry would be around $33,400 per annum..

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[34] MPI’s authority to issue exemption notices comes from section 14 of the Animal Products Act 1999.
[35] Deadweight loss is how much higher taxes to provide the public funding distorts taxpayer decisions to work, invest and spend.
[36] That is, time spent is charged to a minimum of one hour.

## 8.5 ASSESSMENT AGAINST THE COST RECOVERY PRINCIPLES

We consider that Option (2) sufficiently meets the Transparency and Justifiability principles, best meets the Efficiency principle, and is consistent with the Equity principle.

On Transparency, the options and analysis in this chapter were consulted on publicly.

On Justifiability, the hourly rate under Option (2) is the same used for similar services and MPI's normal performance management processes will help ensure that time spent on applications is reasonable.

Option (2) best meets the Efficiency principle because charging producers ensures that producers only request exemptions when the benefits to them exceed the cost of MPI's time. The recovered costs also mean public funding is not required, avoiding deadweight loss.

Under the Equity principle, we have not identified any reasons why beneficiaries (producers) should not pay.

## 8.6 CONSULTATION

Fonterra and the Dairy Companies Association of New Zealand submitted in favour of Option (2), with Fonterra approving of beneficiaries paying for the service rather than public funds.

Federated Farmers also made a general statement in favour of all the design change proposals so long as historical deficits are not recovered (they are not).

## 8.7 CONCLUSION

MPI's preferred option is Option (2) – to introduce a charge for exemptions to RMPs. Option (2) best achieves the cost recovery principles.

## 8.8 MONITORING AND REVIEW

Option (2) is a small charge with the hourly fee derived from overall staff and overhead costs for services of this type under the overall memorandum account. As such, this fee will be tracked as part of general expenditure in this memorandum account rather than tracked and reported individually. Future reviews of this fee would be expected to take place as part of reviews of the base hourly rate that the fee is set to.

# 9 Infant formula auditing

## 9.1 BACKGROUND AND SERVICE DESCRIPTION

New Zealand infant formula products must be registered with China's State Administration for Market Regulation (SAMR) before they can be sold in China. Due to COVID-19 travel restrictions, MPI and SAMR agreed that MPI would carry out on-site audits of infant formula producing facilities where required to continue the registration process.

If SAMR says an infant formula production facility must be audited before it will register the products, then the facility's operator must ask MPI to carry out the audit.[37] The operator can only request the audit once the infant formula has passed a technical assessment and SAMR has said the facility can be audited. The audits ensure the products meet China's product requirements.

Audits are detailed and are carried out by verifiers who have specialist technical expertise. A full audit involves pre-audit preparation and meetings, observation of production, sample testing, and report writing.

## 9.2 STATUS QUO AND PROBLEM

Travel is currently open with China, but MPI-assisted audits may be needed if the travel restrictions for travel to and from China re-emerge.

Currently there is no explicit regulation allowing MPI to charge infant formula manufacturers for the costs involved in auditing facilities on SAMR's behalf.

Instead, as SAMR audits are similar to verifications so MPI has the option to charge for auditing using the fee for circuit verifiers (and used this previously). At $198.96 per hour, the circuit verification fee[38] only partially recovered the true cost which was $295.00 per hour. The cost of under-recovering is covered by public funding which may be considered inequitable and comes with a deadweight loss.

## 9.3 OPTIONS

We have identified the following options:

- Option (1) – The status quo. Use the circuit verification fee of $198.96 per hour.
- Option (2) – Introduce a fee of $295.00 per hour for on-site audits on SAMR's behalf. This would require amending the Animal Product (Fees, Charges, and Levies) Regulations 2007 and the Animal Products (Dairy Industry Fees, Charges, and Levies) Regulations 2015.

## 9.4 ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

The following estimates are based on assumptions at the time the consultation document was prepared. They have not been updated but would be for any future review of charges (see Chapter 9.8).

Audits take around 120 hours each per infant formula, ranging from 80 to 160 hours. Between four and ten businesses may need audits with around four formulas each.

Figure 10 sets out estimated costs under Option (1) and Option (2). Option (2) increases the cost to businesses, in years where travel between New Zealand and China is interrupted, by 48.3% with a total cost across industry of around $370,000.

The costs in Options (1) and (2) would only be incurred in years where travel between New Zealand and China is interrupted.

**Figure 10: Infant formula auditing costs**

| Option | Cost per formula | Cost per business | Total cost |
|---|---|---|---|
| Option (1) - $198.96 per hour | average $23,900<br>range $15,900 to $31,800 | average $95,500<br>range $63,700 to $127,300 | $254,700 to $1,273,300 |

[37] According to the China Overseas Market Access Requirements (OMAR), amendment 10. OMARS are export requirements issued by MPI under section 60 of the Animal Products Act 1999. Access to OMARS is restricted to registered exporters and Risk Management Programme (RMP) operators.
[38] See Part 7 of the Schedule to the Animal Products (Dairy Industry Fees, Charges, and Levies) Regulations 2015 and Schedule 1, Part 7 of the Animal Products (Fees, Charges, and Levies) Regulations 2007.
The $230.50 hourly rate for circuit verifiers is made up of two parts: $198.96 per hour to cover future costs and $31.54 per hour for historical deficits. As SAMR audits did not contribute to the deficits, only the $198.96 is charged with the $31.54 waived.

| | | | |
|---|---|---|---|
| Option (2) - $295.00 per hour | average $35,400<br>range $23,600 to $47,200 | average $141,600<br>range $94,400 to $188,800 | $377,600 to $1,888,000 |

## 9.5 ASSESSMENT AGAINST THE COST RECOVERY PRINCIPLES

We consider that Option (2) sufficiently meets the Transparency and Justifiability principles, best meets the Efficiency principle, and is consistent with the Equity principle.

On Transparency, the options and analysis in this chapter were consulted on publicly and other discussions were held with infant formula producers.

On Justifiability, while the hourly rate is higher than for similar services including circuit verifiers, a higher hourly rate is needed to quickly scale up auditing capacity when needed. This is considered to be more appropriate than having this capacity on call permanently in case it's needed in future.

An additional issue arises as because this service is infrequently charged, there is uncertainty around what level of hourly cost would be required at any point to upscale auditing capacity. The $295 hourly rate is MPI's best estimate based on recent experience, but future costs may be higher or lower than this. MPI has the ability to partially waive fees if the cost turns out to be lower than the $295 hourly rate.

Option (2) best meets the Efficiency principle because charging producers full costs ensures that producers only request audits when the benefits to them exceed the auditing costs. The recovered costs also mean public funding is not required, avoiding deadweight loss. Option (2) also avoids administration costs with staff understanding and processing waivers which occurs under Option (1).

Under the Equity principle, we have not identified any reasons why beneficiaries (producers) should not pay.

## 9.6 CONSULTATION

Fonterra and the Dairy Companies Association of New Zealand submitted in favour of Option (2). Fonterra noted the importance of having auditors available when needed. The Dairy Companies Association of New Zealand asked that costs be transparent to businesses at the time businesses are considering requesting an audit.

Federated Farmers also made a general statement in favour of all the design change proposals so long as historical deficits are not recovered (they are not).

## 9.7 CONCLUSION

MPI's preferred option is Option (2) – to introduce a charge for on-site SAMR audits. Option (2) best achieves the cost recovery principles.

## 9.8 MONITORING AND REVIEW

As this service is infrequently charged, there is uncertainty around what level of hourly cost would be required at any point to upscale auditing capacity.

With regards to the risk of over-recovery, MPI has the ability to partially waive fees if the cost turns out to be lower than the $295 hourly rate.

With regards to the risk of under-recovery, the infrequent use of the service means the opportunity to recover past under-recovery is low – there may not be future years where the service is provided where MPI can add historical deficits to future charges. Additionally, it may not be efficient and equitable to do so given the small number of affected businesses and the risk that different future businesses end up paying deficits of different past businesses. MPI may need to review this rate more frequently than other fees to mitigate the risk of under-recovery.

# 10 Tidier fee structure for approval of premises for export requirements

## 10.1 BACKGROUND AND SERVICE DESCRIPTION

Some countries only allow animal products to be imported if they were produced in premises included on official country lists. For example, China only imports animal products from New Zealand that were produced in an MPI-approved premises.

To be included on the list, producers must apply to MPI to have their premises 'export approved'. This ensures premises meet the requirements for animal products intended for export. New market access requirements for China will increase the need for MPI's premises application processing services.

## 10.2 STATUS QUO AND PROBLEM

Applications can be for dairy premises and non-dairy premises. The problem with existing changes is that they either do not cleanly account for how the service is provided, resulting in a somewhat messy application of fees by MPI where more straight-forward fees would be cleaner and more transparent.

With regards to dairy premises, there is no explicit charge for these applications, so MPI has been using a charge available to it for unspecified services. While the unspecified services charge recovers costs, it is not as transparent as if there was a specific charge.

With regards to non-dairy premises, the existing charge is a fixed fee equal to one hour's work.

One hour is sufficient for processing an application for a single premise for one country list.

One hour is not typically sufficient to process applications for one premise to multiple country lists or for multiple premises to multiple country lists. As such, applicants submit an application for each premises. For multiple sites or multiple countries, or both, MPI would charge the application fee, with a 25% waiver for such premises from the second application by the same company. It takes 45 minutes on average to process every subsequent application hence the 25% waiver to the per application fee. Requiring multiple applications for what is effectively a single application increases compliance costs for businesses.

## 10.3 OPTIONS

We have identified the following options:

- Option (1) – The status quo. Fees of the below with single applications for each premise and destination:
  - dairy premises: $67.50 per application plus $135 per hour for time after the first half hour
  - non-dairy premises: a fixed $135 for each application for non-dairy premises.
- Option (2) – A fee of $135 per application plus $33.75 per quarter hour beyond the first hour. This would require amending the Animal Product (Fees, Charges, and Levies) Regulations 2007 and the Animal Products (Dairy Industry Fees, Charges, and Levies) Regulations 2015.

## 10.4 ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

Applications for a single premise take around an hour to process, with further premises taking around 45 minutes. The base hourly rate under Option (2) remains at $135.

There should be no increase in cost as the examples in Figure 11 show. The total cost from fees to industry will also be unchanged at around $270,000 to $337,5000 per annum, with some reduction in administration costs under Option (2) to industry.

**Figure 11: Application examples**

| Application example | Option (1) | Option (2) |
|---|---|---|
| **Dairy premises** | | |
| Single premises application of 1 hour | Total: $135.00<br>Breakdown: $67.50 application fee + $67.50 for the 0.5 hour beyond the first 0.5 hour | Total: $135.00<br>Breakdown: $135.00 application fee |
| Two premises application of 1 hour 45 minutes | Total: $236.25<br>Breakdown: $67.50 application fee + $168.75 for the 1.25 hours beyond the first 0.5 hour | Total: $236.25 |

| | | |
|---|---|---|
| | | Breakdown: $135.00 application fee + $101.25 for the 0.75 hours beyond the first hour. |
| **Non-dairy premises** | | |
| Single premises application of 1 hour | Total: $135.00<br>Breakdown: $135.00 application fee | Total: $135.00<br>Breakdown: $135.00 application fee |
| Two premises application of 1 hour 45 minutes | Total: $236.25<br>Breakdown: $135.00 application fee for the first premise + $135.00 application fee for the second premise - $33.75 (25% waiver on the second application) | Total: $236.25<br>Breakdown: $135.00 application fee + $101.25 for the 0.75 hours beyond the first hour. |

## 10.5 ASSESSMENT AGAINST THE COST RECOVERY PRINCIPLES

We consider that Option (2) sufficiently meets the Transparency and Justifiability principles, best meets the Efficiency principle, and is consistent with the Equity principle.

While both options meet the Transparency principle as they were consulted on publicly, Option (2) better meets the Transparency principle as the charges businesses face will be clear

On Justifiability, the hourly rate is not proposed to change, but administration costs would be more reasonable under Option (2) than Option (1).

Option (2) best meets the Efficiency principle by reducing administration costs.

There appear to be no factors relevant to the Equity principle.

## 10.6 CONSULTATION

Fonterra, the Dairy Companies Association of New Zealand and Seafood New Zealand submitted in favour of Option (2), with Fonterra and the Dairy Companies Association of New Zealand noting the reduced administration costs.

Federated Farmers also made a general statement in favour of all the design change proposals so long as historical deficits are not recovered (they are not).

## 10.7 CONCLUSION

MPI's preferred option is Option (2) – fee of $135 per application plus $33.75 per quarter hour beyond the first hour. Option (2) best achieves the cost recovery principles.

## 10.8 MONITORING AND REVIEW

Option (2) is a charge to the structure of fees to improve transparency and reduce administration costs. As such, no specific review is proposed. The level of fee itself will be monitored and reviewed as part of MPI's normal monitoring and review practices.

# 11 On-call charges for vets doing biosecurity and animal welfare work

## 11.1 BACKGROUND AND SERVICE DESCRIPTION

MPI employees often work on an on-call basis outside of normal working hours when inspecting live animals that have been imported to or exported from New Zealand. Inspectors must be on-call in case the animal urgently needs emergency care in an MPI-supervised veterinary clinic.

## 11.2 STATUS QUO AND PROBLEM

Payment to staff for being on-call is a normal part of staff remuneration in order to encourage staff to make themselves available and compensate for the inconvenience of being available to undertake short-notice work. MPI pays staff $45 per on-call shift.

MPI is able to recover this cost from vet work under animal products regulations, but not vet work relating to animal welfare and biosecurity as an on-call charge is not specified in the relevant regulations.

Additionally, some specialist services overlap animal products, animal welfare, and biosecurity, so MPI inspectors are uncertain about whether they should charge on-call rates due to this ambiguity.

## 11.3 OPTIONS

We have identified the following options:

- Option (1) – The status quo. On-call costs are only recoverable for services clearly under animal products regulations.
- Option (2) – A fee of $45 for on-call shifts for animal welfare and biosecurity work, as well as animal product work. This would require amending the Animal Welfare (Cost Recovery) Regulations 2015 and the Biosecurity (Costs) Regulations 2010.

## 11.4 ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

Option (2) would increase the costs to users of on-call biosecurity or animal welfare services by $45 per shift. The typical number of on-call shifts per year is between 28 and 56. Based on this, the total annual cost of Option (2) will be in the range of $1,260 to $2,520.

## 11.5 ASSESSMENT AGAINST THE COST RECOVERY PRINCIPLES

We consider that Option (2) sufficiently meets the Transparency and Justifiability principles, best meets the Efficiency principle, and is consistent with the Equity principle.

On Transparency, the options and analysis in this chapter were consulted on publicly.

On Justifiability, the $45 amount is equivalent to approximately a 10% increase on standard pay which is not unreasonable to compensate staff for the inconvenience of being available at short notice (e.g. not being able to plan to attend social events).

Option (2) best meets the Efficiency principle because charging producers ensures that producers only request that services be on-call when the benefits to them exceed the cost. The recovered costs also mean public funding is not required, avoiding deadweight loss.

Under the Equity principle, we have not identified any reasons why beneficiaries (producers) should not pay.

## 11.6 CONSULTATION

Federated Farmers made a general statement in favour of all the design change proposals so long as historical deficits are not recovered (they are not).

## 11.7 CONCLUSION

MPI's preferred option is Option (2) – fee of $45 for on-call shifts across animal product, animal welfare, and biosecurity work. Option (2) best achieves the cost recovery principles.

## 11.8 MONITORING AND REVIEW

Option (2) is a small fix to a gap in charging for on-call shifts. As such, no specific review is proposed. The level of fee itself will be monitored and reviewed as part of MPI's normal monitoring and review practices.

# 12 Call-out charges for vets doing live animal international trade work

## 12.1 BACKGROUND AND SERVICE DESCRIPTION

Veterinarians are often called on to do work outside of normal working hours when inspecting imported and exported live animals, especially horses.

## 12.2 STATUS QUO AND PROBLEM

Minimum payments to staff who are called-out is a normal part of staff remuneration in order to encourage staff to make themselves available and compensate for the inconvenience of undertaking short-notice work. MPI pays staff a minimum of three hours if they are called-out.

MPI is able to recover this costs from vet work under animal products regulations except for work related to live animal or germplasm exports, and not for vet work relating to animal welfare and biosecurity.[39]

## 12.3 OPTIONS

We have identified the following options:

- Option (1) – The status quo. The three-hour minimum is only recoverable for some animal product work.
- Option (2) – The cost recoverable three-hour minimum is extended to live animal and germplasm exports, animal welfare, and biosecurity work. This would require amending the Animal Products (Fees, Charges, and Levies) Regulations 2007, the Animal Welfare (Cost Recovery) Regulations 2015 and the Biosecurity (Costs) Regulations 2010.

## 12.4 ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

There are around 160 call outs a year at an hourly rate of $318.04 (being the double-time rate due to being outside of normal hours). Call outs average 1.85 hours which MPI recovers at a total cost of $94,100 per annum. Increasing the time recovered from 1.85 hours to 3.00 hours will increase costs to industry by around $370 per call out and $58,500 in total per annum.

## 12.5 ASSESSMENT AGAINST THE COST RECOVERY PRINCIPLES

We consider that Option (2) sufficiently meets the Transparency and Justifiability principles, best meets the Efficiency principle, and is consistent with the Equity principle.

On Transparency, the options and analysis in this chapter were consulted on publicly.

On Justifiability, paying staff a minimum amount is a standard feature of contracts in order to encourage them to provide work on-call. The three-hour minimum is a reasonable amount to compensate staff for the inconvenience of providing work at short notice (e.g. cancelling attendance at social events at short notice).

Option (2) best meets the Efficiency principle because charging producers ensures that producers only call-out services when the benefits to them exceed the cost. The recovered costs also mean public funding is not required, avoiding deadweight loss.

Under the Equity principle, we have not identified any reasons why beneficiaries (producers) should not pay.

## 12.6 CONSULTATION

Federated Farmers made a general statement in favour of all the design change proposals so long as historical deficits are not recovered (they are not).

[39] A three-hour minimum is specified under Part 7 of the Animal Products (Fees, Charges, and Levies) Regulations 2007 and the Animal Products (Dairy Industry Fees, Charges, and Levies) Regulations 2015 but not:
- Part 8, Schedule 1 of the Animal Products (Fees, Charges, and Levies) Regulations 2007
- Part 2, sub-part 2 of the Schedule to the Animal Welfare (Cost Recovery) Regulations 2015
- Regulation 1 of the Biosecurity (Costs) Regulations 2010.

## 12.7 CONCLUSION

MPI's preferred option is Option (2) – the cost recoverable three-hour minimum is extended to live animal and germplasm exports, animal welfare, and biosecurity work. Option (2) best achieves the cost recovery principles.

## 12.8 MONITORING AND REVIEW

Option (2) is a small fix to a gap in charging for call-outs. As such, no specific review is proposed. The level of fee itself will be monitored and reviewed as part of MPI's normal monitoring and review practices.

# 13 Vet rate at transitional and containment facilities

## 13.1 BACKGROUND AND SERVICE DESCRIPTION

Goods that may pose a biosecurity risk are sent to transitional and containment facilities to be inspected and treated before they are cleared for entry into New Zealand. The facilities hold organisms that should not become established in the country.[40]

MPI biosecurity inspectors inspect, investigate, and audit transitional and containment facilities and those who operate them. The inspectors also process applications for approval of new facilities.

Some of the compliance activities MPI carries out on these facilities are only allowed to be performed by a veterinary inspector (an MPI veterinarian who is also warranted as a biosecurity inspector). For example, a veterinary inspector would monitor an animal held in a facility to ascertain whether the animal should be cleared, moved from the facility, or continue to be held.

## 13.2 STATUS QUO AND PROBLEM

MPI is authorised to recover the costs of *biosecurity* inspectors' activities from operators under the Biosecurity (Costs) Regulations 2010 at a general rate of $102.27 per hour. Although some inspection activities must be carried out by a *veterinary* inspector, the regulations do not allow MPI to charge the $186.30 per hour cost of a veterinary inspector. There is a financial deficit of $84.03 per hour for veterinary inspectors.

The status quo can also cause administrative confusion for MPI and operators as veterinary inspectors are charged at $102.27 per hour under the biosecurity cost regulations and $186.30 under other regulations.

## 13.3 OPTIONS

We have identified the following options:

- Option (1) – The status quo. A fee of $102.27 per hour for veterinary inspectors doing veterinary work under the biosecurity cost regulations.
- Option (2) – A fee of $186.30 per hour. This would require amending the Biosecurity (Costs) Regulations 2010[41].

## 13.4 ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

Services affected by the 82% increase in fees under Option (2) are provided around 46 times a year. The fees for these services currently range from around $102.27 to around $1,040.40 and would increase to around $186.30 to $1,769.85. Total costs across industry would increase from around $15,600 to $28,200 per annum.

## 13.5 ASSESSMENT AGAINST THE COST RECOVERY PRINCIPLES

We consider that Option (2) sufficiently meets the Transparency and Justifiability principles, best meets the Efficiency principle, and is consistent with the Equity principle.

On Transparency, the options and analysis in this chapter were consulted on publicly.

On Justifiability, the hourly rate under Option (2) is the same used for similar services and MPI's normal performance management processes will help ensure that time spent on applications is reasonable.

Option (2) best meets the Efficiency principle because charging producers ensures that producers only call-out services when the benefits to them exceed the cost. The recovered costs also mean public funding is not required, avoiding deadweight loss.

Under the Equity principle, we have not identified any reasons why beneficiaries (producers) should not pay.



[40] For example, certain laboratories are containment facilities because they import micro-organisms for testing, which are never allowed to be released into New Zealand.

[41] The following items within the regulations:

- Item 18: approval of a transitional or containment facility, or a facility operator
- Item 19: inspection and compliance auditing of a transitional or containment facility under section 39 of the Act
- Item 20: investigation and compliance auditing of a facility operator, or proposed operators under section 40 of the Act.

## 13.6 CONSULTATION

New Zealand Pork supported Option (2) on the basis that users should pay for services of benefit to them.

Federated Farmers also made a general statement in favour of all the design change proposals so long as historical deficits are not recovered (they are not).

## 13.7 CONCLUSION

MPI's preferred option is Option (2) – a fee of $186.30 per hour for veterinary inspectors doing veterinary work under the biosecurity cost regulations. Option (2) best achieves the cost recovery principles.

## 13.8 MONITORING AND REVIEW

Option (2) is a small fix to a gap in the fee for veterinary inspectors. As such, no specific review is proposed. The level of fee itself will be monitored and reviewed as part of MPI's normal monitoring and review practices.

# 14 Animal product penal rates for veterinary services

## 14.1 BACKGROUND AND SERVICE DESCRIPTION

MPI Verification Services veterinarians check that animal products operators (e.g. slaughterhouses) are following required practices.

Verifiers often work unsociable hours such as early shifts (i.e. between 2 a.m. and 6 a.m.) and at the weekend because they are required to be present for certain operational practices. If a verifier works these hours they are paid penal time, which is a premium on top of their normal hourly wages.

The penal rates that can be recovered from users, as set out in the regulations are:

- Penal 0.5: a 50% premium on normal time – equivalent to time and a half
- Penal 1.0: a 100% premium – equivalent to double time
- Penal 2.0: a 200% premium – equivalent to triple time.[42]

## 14.2 STATUS QUO AND PROBLEM

New collective employment agreements (CEA) for veterinarians have recently come into force, resulting in discrepancies between the penal rates that MPI must pay their veterinarians and the rates that MPI can recover from the animal products operators:

- One CEA from 2019 states that if a veterinarian starts work before 6 a.m. then MPI must pay them *Penal 2.0* time for a maximum of 1 hour. The regulations, however, state that only *Penal 1.0* time can be recovered if a veterinarian works an early shift.
- The most recent CEA came into force from the 2021/22 year.

  It states verifiers get overtime (paid at double time) on weekends plus *Penal 1.0* for the first hour (only) worked before 6 am. The *Penal 1.0* corrected a discrepancy where a verifier was paid less for an early start while in overtime compared with an early start within a 40-hour working week. The fix now means they are paid the same.

  The regulations, however, currently state that penal rates and overtime rates cannot be charged in respect of the same hour (the first hour before 6 am).
- The final issue relates to shifts between midnight and 2 am. where the shift started on a weekday. Currently, the regulations refer to 'Monday to Thursday'. The regulations do not cover situations where staff starting a shift on a Thursday or Friday and work through to between 12 am and 2 am the following day.

MPI is charging businesses according to the collective agreement, but without regulatory backing.

## 14.3 OPTIONS

We have identified the following options:

- Option (1) – The status quo penal rates in the animal products regulations.
- Option (2) – Amend the definitions of Panel 0.5, 1.0, and 2.0 in the animal products regulations (2007 and 2015) to align with the rates that MPI pays its verifiers as listed in the CEA:

| Time period | Option (1) | Option (2) – Collective Employee Agreement settings |
|---|---|---|
| Midnight to 2am, Monday to Thursday | Penal 0.5 | If shift started before midnight, Penal 0.5.<br>If shift started after midnight, Penal 2.0 for the first hour, Penal 1.0 thereafter. |
| Weekdays 2am to 6am | Penal 1.0 | If started before midnight, Penal 1.0.<br>If shift start is after midnight, Penal 2.0 for the first hour, Penal 1.0 thereafter. |
| 12am – 12pm Saturday, first 3 hours | Penal 0.5 | |

[42] Penal rates are set out in the following regulations: Schedule 1, Part 7, Clause 3 of the Animal Products (Fees, Charges, and Levies) Regulations 2007, and Schedule, Part 7, Clause 3 of the Animal Products (Dairy Industry Fees, Charges, and Levies) Regulations 2015.

| | | |
|---|---|---|
| 12am Saturday – 12am Monday, other than the first 3 hours between 12am – 12pm Saturday | Penal 1.0 | From 12am – 6am Saturday and Sunday, Penal 2.0 for the first hour, Penal 1.0 thereafter.<br>From 6am Saturday to 12pm Saturday, Penal 0.5, for the first 3 hours.<br>After the first 3 hours in 6am – 12pm Saturday, and from 12pm Saturday to 12am Monday, Penal 1.0 |
| Hours 9 and 10 of a 10-hour shift | Penal 0.5 | Removed as it's not included in the agreement. |
| Hours 9 and 10 of a 10-hour shift, if the hours are between 10pm – 6am | Penal 1.0 | Removed as it's not included in the agreement. |
| Statutory Holiday | Penal 1.0 | Penal 1.0, however an early start may still apply at Penal 2.0 for the first hour before 6am. |
| Every hour of penal time other than those outlined above | Penal 2.0 | Removed as it's not included in the agreement. |
| When starting a shift in overtime before 6am | Not payable | Penal 1.0 for the first hour. |

## 14.4 ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

As MPI is already charging businesses according to the collective agreement, there would be no additional financial cost to businesses. If the regulations are not changed and MPI charges according to the regulations, the financial cost to public funding would be around $450,000 per annum.

## 14.5 ASSESSMENT AGAINST THE COST RECOVERY PRINCIPLES

We consider that Option (2) sufficiently meets the Transparency and Justifiability principles, best meets the Efficiency principle, and is consistent with the Equity principle.

On Transparency, the options and analysis in this chapter were consulted on publicly.

On Justifiability, it is reasonable that staff that staff are paid penal rates for working outside of normal hours. The penal rates were the outcome of a goodfaith negotiation and none were identified as unreasonable in consultation.

Option (2) best meets the Efficiency principle because charging producers ensures that producers only demand services outside of normal hours when the benefits to them exceed the cost. The recovered costs also mean public funding is not required, avoiding deadweight loss.

Under the Equity principle, we have not identified any reasons why beneficiaries (producers) should not pay.

## 14.6 CONSULTATION

Federated Farmers made a general statement in favour of all the design change proposals so long as historical deficits are not recovered (they are not).

## 14.7 CONCLUSION

MPI's preferred option is Option (2) – to align the time periods when the various penal rates apply across the animal products regulations with those listed in the CEA. Option (2) best achieves the cost recovery principles.

## 14.8 MONITORING AND REVIEW

Option (2) fixes inconsistences between the regulations and collective agreements. As such, no specific review is proposed. The level of base hourly rate itself will be monitored and reviewed as part of MPI's normal monitoring and review practices.

# APPENDIX 1: MPI'S COST RECOVERY PRINCIPLES

MPI's four Cost Recovery Principles are:

- Transparency – costs are transparent
- Justifiability – costs are reasonable
- Efficiency – net benefits are maximised
- Equity – costs are fair.

These four principles appear in much of MPI's legislation including the Animal Products Act 1999 which governs Establishment fees.[43]

The legislative definition and interpretations of each principle are set out below.

## Transparency

### Legislation

'Costs should be identified and allocated as closely as practicable in relation to tangible service provision for the recovery period in which the service is provided.'

### Policy interpretation

'Transparency' means providing adequate information to people such that they can understand charges and have an opportunity to input into their calculation and setting.

'Identified and allocated…' means presenting the costs in a way that people can see what services generate what costs and when. 'Allocated' does not mean 'charged'. How costs are charged is a result of consideration of all the principles.

## Justifiability

### Legislation

'Costs should be collected only to meet the reasonable costs (including indirect costs) for the provision or exercise of the relevant function, power, or service.'

### Policy interpretation

'Reasonable costs' are those necessary to deliver the service at the demanded quantity and quality.

## Efficiency

### Legislation

'Costs should generally be allocated and recovered in order to ensure that maximum benefits are delivered at minimum cost.'

### Policy interpretation

Efficiency is made up of several elements:

- Costs should be the lowest necessary to provide the service.[44]
- Costs should be charged to those who benefit from the service and/or those whose behaviour generates the need for the service:

[43] https://www.legislation.govt.nz/act/public/1999/0093/latest/whole.html#DLM35716
https://legislation.govt.nz/act/public/2003/0114/latest/DLM223236.html
[44] A re-emphasis of the Justifiability principle. The concept appears twice to help ensure MPI keeps cost efficiency top of mind.

- Those who benefit from the service – If the customer pays, they have the incentive to demand only those services that provide them benefit compared to other things they might purchase. If parties other than the beneficiary pays, then the beneficiary will demand more services than otherwise.
- Those whose behaviour can reduce the need and cost of the service – Typically both the supplier (MPI) and the participant/applicant will be able to do things to reduce the need and cost of the service. For example, fixed charges with MPI bearing some financial risk can encourage MPI to deliver services more time efficiently, while businesses can reduce cost by providing accurate information in applications (requiring less follow-up by MPI).

  If MPI has transparently justified its costs, it will not normally be appropriate for MPI to contribute to the costs.

- Charges should account for administrative costs – for instance, sometimes it will be administratively prohibitive to charge those that benefit or those that can reduce costs so a simplified approach is warranted.
- Charges should be competitively neutral – MPI should not use any dominant market position to charge inflated prices and make more than a fair economic return.

### Efficiency and the type of costs

All relevant costs are potentially recoverable, including:

- direct costs associated with services, such as staff time, travel costs, systems and equipment used in delivering the specific service, and
- support costs associated with delivery of the service, such as training and development costs for staff, administrative support costs, management costs, project costs and capital costs, and
- a proportion of wider business support or common costs, for example costs associated with corporate functions like finance, human resources management, information technology, and costs of property and utilities.

It is administratively impractical to precisely allocate wider business support or common costs to the wide range of MPI services. Instead, staff hours are used as a proxy on the assumption that the more staff hours are part of a service, the more property, human resources and other wider support and common costs the service will use.

### Efficiency and type of services

If costs are to be recovered from beneficiaries, the appropriate type of charge to use depends on whether the service is a private good or club good.[45]

Fees are used for private goods – services that are of direct benefit to individual businesses. Levies pay for club goods – services that benefit sectors or groups of businesses as a whole.

If costs are to be recovered from exacerbators, the appropriate type of charge is a levy on the activity, or proxy for the activity, that causes the risk.

## Equity

### Legislation

‘Funding for a particular function, power, or service, or a particular class of functions, powers, or services, should generally, and to the extent practicable, be sourced from the users or beneficiaries of the relevant function, power, or service at a level commensurate with their use or benefit from the function, power, or service.’

### Policy interpretation

The Government will usually deem it fair that beneficiaries pay.

On other occasions, the Government will determine that other fairness considerations mean that another party contributes to the costs. For example, sometimes industry will be happy to support parts of its industry. Other times, Governments will want to provide additional support.

[45] There is also a category of merit goods – services which the community as a whole desires more of than would be provided if charged for at full cost.

## Relationship between the Cost Recovery Principles

The principles build on each other with Transparency and Justifiability providing a foundation to the consideration of Efficiency and Equity.

Figure 12 summarises the relationship between the principles.

### Transparency and Justifiability come before considering Efficiency and Equity

The APA says about Justifiability that MPI can only recover reasonable costs.

While the Transparency principle itself doesn't have a similarly strong statement, the very next clause says that costs should not be recovered unless there's been adequate consultation with affected parties including 'sufficient time and information to make an informed contribution'. Adequate consultation can only happen if MPI has been transparent.

With language of 'should not' and 'only', Transparency and Justifiability require[46] some minimum standard to be met. In contrast, Efficiency and Equity are to be achieved 'generally'.

This sequential approach to the principles, rather than considering the principles simultaneously, makes sense. It is not possible to be confident that the efficient way of cost recovering has been identified if costs have not been sufficiently justified, or affected parties have not had a reasonable opportunity to test the costs.

### There will sometimes be trade-offs between Efficiency and Equity

The 'generally' in the Equity principle means that a Government might decide to charge someone other than the beneficiary. The 'generally' in the Efficiency principle means that cost recovery settings will not always maximise benefits and minimise costs.

This also makes sense. If the Government determines that it is more equitable to pay for a service through Crown funding rather charging beneficiaries or those whose behaviour can reduce the need for the service, then the cost recovery setting will not be maximising net benefits.

The two 'generally's allow for trade-offs to be made between Efficiency and Equity.



[46] The Animal Products Act 1999 and Wine Act 2003, however, also say that failure to consult sufficiently does not affect the validity of cost recovery charges.

**Figure 12: Relationship between the Cost Recovery Principles**