

Stage 2 Cost Recovery Impact Statement

Recognising variability in charging for animal products and wine approvals

AGENCY DISCLOSURE STATEMENT

This Cost Recovery Impact Statement (CRIS) has been prepared by the Ministry for Primary Industries.

It provides a brief analysis of options to address problems of fees that do not reflect the length of time it typically takes to provide the service. Options are identified using, and analysed against, the cost recovery principles of Transparency, Justifiability, Efficiency and Equity that appear in the relevant legislation and MPI's cost recovery guidance. This CRIS does not conduct a value-for-money review of the services.

The analysis is brief as the size of the problems and the impact of the options are small. While the proposed increase in revenue is proportionately large (at about 80%), the total amount of extra revenue is estimated at less than \$0.1 million per annum spread across a wide range of industries and businesses. The impact on businesses and markets is expected to be negligible. As such, no further analysis has been undertaken at a business or market level.

Analysis of the problem and options is constrained by a lack of data that limits the degree to which the Transparency principle can be achieved. These limits have been accounted for in the choice of preferred option.

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EXECUTIVE SUMMARY

MPI proposes to change a number of fees based on fixed amounts of time under the Animal Products Act 1999 and the Wine Act from July 2021. These changes involve:

- adjusting some fees/times up and adjusting some down
- introducing an hour threshold beyond which time-variable charges apply.

The overall impact of these changes is an 80% increase in time cost recovered.

Industry submissions supported the introduction of a threshold and generally supported the proposed fees. One area of disagreement was New Zealand Winegrowers and The New Zealand Food & Grocery Council preferring that increases for wine charges be deferred until June 2022.

Level of charges

The fees covered are set at a fixed amount, calculated by multiplying a fixed time for providing the service by the regulated hourly rate of \$135.

The fixed fees do not always reflect the length of time it typically takes to provide the service. This means customers who request more complex services are not paying the full cost of the service, while

others with less complex services are sometimes paying too much. MPI proposes increasing the time for those services that take longer than currently regulated, and decreasing others.

The cost increase for businesses with Risk Management Programmes, for instance, is about \$40 per business per annum.

Structure of charges

Natural variability in the time it takes MPI to provide services means that charging the exact time spent on each service cannot be fully justified. Additionally, imperfect time recording means that any amended fees should put some financial incentive on MPI to keep processing times low.

MPI's preferred option to balance the principle of 'beneficiary pays' with incentivising MPI to keep costs low and justified is to:

- change the fees in the regulation to match what MPI understands to be the typical costs of providing the service; and
- only charge more if the time required to deliver the service is more than an hour higher than the typical time.

MPI's analysis suggests that an hour is likely to reasonably separate more complex services from services that take longer due to natural variability in the time it takes MPI to provide services (e.g. because some staff can be quicker at some tasks than others).

Covid and the timing of changes

While agriculture production volumes are largely unaffected by Covid, MPI does not have timely information about the value of production and exports or of costs. It is highly likely that profit margins are temporarily lower due to Covid in the form of higher costs and, possibly, lower prices due to recessions overseas and, for the wine industry, from lower tourism.

The Government has so far preferred to deal with the impacts on businesses through central supports such as the wage subsidy and through supports to banks (to then support bank customers). This, combined with the general approach to Equity of beneficiaries rather than taxpayers paying, means that MPI's preferred option is to implement the above option from July 2021 rather than delay a year.

The Government may, however, determine that further weight should be given to business concerns. In this case, deferring the above option by a year might be preferred (at a cost to the Crown of less than \$0.1 million).

STATUS QUO

New Zealand's food system¹ is world leading and is based on international best practice science and risk assessment. In general terms the current legislative framework makes businesses responsible for the safety and suitability of their products, with MPI responsible for ensuring that this happens.

This system is critical for protecting and supporting the health of New Zealanders and to support New Zealand's exports. With around 80% of food produced in New Zealand being exported, there are domestic and international customers who expect food products to be safe to consume.

Covid-19 and the primary sector

Primary industry export revenue reached \$48 billion in the year ended June 2020, up 3.6 percent from the previous year, despite the emergence of COVID-19 in late January 2020. This was aided by a strong start to the year prior to the pandemic, a large kiwifruit and apple harvest in March/April, and a weaker New Zealand dollar.

¹ The food system includes the Food Act 2014, the Animal Products Act 1999, the Agricultural Compounds and Veterinary Medicines Act 1997, and the Wine Act 2003.

However, COVID-19 and New Zealand's March/April lockdown created unprecedented challenges. Over the next few years, the global recession is forecast to result in weaker consumer demand and lower product prices in New Zealand and overseas. Agriculture production and trade volumes have been largely unaffected in aggregate and we expect this trend to continue. The impacts will be uneven across the primary industries, however, as the specific circumstances of each sector will influence their performance. The timing and magnitude of these impacts remains uncertain, as the pandemic has yet to run its course.

While volumes are largely unaffected, MPI does not have timely information about the value of production, exports and costs. Submissions highlighted accumulating cost pressures from various sources. These included factors ranging from Covid (while submissions did not explicitly mention freight costs, this is one which has been reported in media) and, in the case of wine, loss of revenue from tourism. It is highly likely that profit margins are temporarily lower due to Covid increasing costs of production while recessions decrease the prices paid by overseas customers.

MPI's services, charges, and the regulatory framework

Cost recovery in general

Cost recovery funds the services that protect New Zealand from biological risks, ensure our food is safe to consume and export, and that help ensure the sustainability of our natural resources. These outcomes allow our primary sector to grow the value of its exports, which currently generate over \$48 billion per annum (2019/20). Typically, approximately 30% of MPI's departmental funding comes from cost recovered revenue. With the emergence of COVID-19, this is expected to be approximately 20% (\$150 million) in 2020/21, largely due to the drop in revenue for border biosecurity levies on arriving travellers.

In line with best practice guidance, MPI generally undertakes a thorough review of each cost recovery regime 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 also be updated outside this normal three-year review cycle if a material surplus or deficit accumulates in a memorandum account.

MPI takes a principles-based approach, as set out in the 'Cost Recovery Principles and overall approach to cost recovery' section, to both its thorough reviews and its out-of-cycle reviews.

What regulated services are covered by this CRIS?

MPI provides a range of regulatory services under the Animal Products Act 1999 and the Wine Act 2003 aimed at ensuring the food New Zealand produces is suitable and safe for consumption and export. MPI provides a wide range of services in the food system, such as verifying that businesses across the whole supply chain are following their food safety measures, providing official assurances that New Zealand's exporters meet overseas market access requirements, and undertaking research, audits and food testing.

The services covered by this CRIS are in the following areas:

- Registration of a Risk Management Programme (RMP)
- Registration of an amendment to an RMP
- Minor updates to an RMP
- Recognition of a person, agency or laboratory (Animal Products and Wine)
- Approval or recognition of a non-dairy or dairy maintenance compound
- Registration of a Wine Standards Management Plan (WSMP)
- Significant amendments to a WSMP
- Application for a dairy product disposition

- Provision of technical advice

The services are private goods

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.

The services listed above are only provided by MPI upon payment of a fee and the benefits accrue to the business that receives the service. For example, the benefits of an RMP accrue to the business that implements that plan in the form of reduced food safety risks and continued customer demand.

To encourage businesses to only demand or use services that they value highly enough it is economically efficient to, wherever possible, recover the costs of providing private goods from those who benefit from the services.

How are the fees regulated?

In general

The Acts allow MPI to recover costs in accordance with the principles of Transparency, Justifiability, Efficiency and Equity (see the 'Cost Recovery Principles and overall approach to cost recovery' section of this CRIS).

Regulations under the Acts set out the fee levels. In the case of the listed fees, these regulations are the Animal Products (Dairy Industry Fees, Charges and Levies) Regulations 2015, the Animal Products (Fees, Charges, and Levies) Regulations 2007, and the Wine Regulations 2006.

Additional requirements for changes made part-way through a financial year

Any changes to the charges in 2021 will be made part-way through the financial year (1 July 2021 to 30 June 2022). In this situation:

- the Animal Products Act 1999 requires that the Minister is 'satisfied' that affected parties 'agree or substantially agree' with the change;
- and the Wine Act 2003 requires that the Minister is 'satisfied' that affected parties 'agree or do not substantially disagree' with the changes

How are the fees set?

The current fees are set at a fixed amount, calculated by multiplying a fixed time for providing the service by the regulated hourly rate of \$135.

PROBLEM

Figure 1 sets out the services where the fixed fee does not always reflect the length of time it typically takes to provide the service. This means customers who request more complex services are not paying the full cost of the service they receive, while others with less complex services are sometimes paying too much.

These services have been identified using staff judgement (data is not available from such sources as time recording).

Some services involve less time than is regulated for, most involve more. MPI estimates that, overall, it under-recovers by approximately \$100,000 per annum as a result of this problem. Most of this deficit is occurring as a result of the significantly lower rates for services related to risk management plans (RMPs).

Figure 1: Current chargeable times versus typical actual times

Application form code: service	Regulation reference	Typical number of annual applications	Chargeable time under Regulations (hours)	Typical processing time per application (hours)	
				New application	Renewal
Dairy (D): Animal Products (Dairy Industry Fees, Charges, and Levies) Regulations 2015					
Non dairy (ND): Animal Products (Fees, Charges, and Levies) Regulations 2007					
AP4: Application for registration of a Risk Management Programme (RMP)	D Approval 2 ND Item 1	130	1	3 Custom RMP 2 Template RMP	
AP5: Application for registration of an RMP under new operator	D Approval 2 ND Item 1	112	1	1	-
AP6: Application for registration of an amendment to an RMP	D Approval 2 ND Item 2	114	0.5	2.5 Custom RMP 1.5 Template RMP	
AP7: Application for recognition of a person (APA)	D Approval 5 ND Item 13 ND Item 14	89	1	1.25	0.5
AP8: Application for recognition of an agency (APA)	D Approval 5 ND Item 13 ND Item 14	-	1	1.25	0.5
AP18: Application for recognition under the Recognised Laboratory Programme (RLP) as an animal products laboratory	D Approval 5 ND Item 13 ND Item 14	11	1	1.25	0.5
AP50: Fee in relation to minor updates of an RMP	D Approval 6 ND Item 3	288	0.5	1 Technical 0.5 Non-Technical	
AP65: Application for approval of maintenance compound (non-dairy)	ND Item 44	836	0.5	1	0.5
Delivery of specialist services by technical staff	ND Part 3	N/A	0.25	N/A	
DPF15: Dairy maintenance compound approval or recognition	D Maintenance Compounds	307	0.5	1	0.5
Application for product disposition	D Compliance and Monitoring	329	1	1	
DPF15: Dairy maintenance compound approval or recognition	D Compliance and Monitoring	307	0.5	1	0.5
Wine Regulations 2006					
WA4: Application for registration of a Wine Standards Management Plan (WSMP)	Item 3 Item 4	10	1	2.5 Custom WSMP 1.5 Template WSMP	

Application form code: service	Regulation reference	Typical number of annual applications	Chargeable time under Regulations (hours)	Typical processing time per application (hours)	
				New application	Renewal
WA6: Application for registration of significant amendments to a WSMP	Item 5	52	0.5	1	-
WA7: Application for recognised person (Wine)	Item 9	-	1	1.25	0.5
WA8: Application for recognised agency (Wine)	Item 9	-	1	1.25	0.5
WL1: Application for recognised wine laboratory	Item 9	-	1	1.25	0.5

Notes:

1. Some services, such as recognitions, last for multiple years. As such, where there are low numbers of businesses, volumes can strongly vary.
2. 'Application Code' refers to the code such as 'AP4' that each application form for an approval is identified by. Some Regulations may apply to multiple forms and some forms may be for services under multiple Regulations.
3. 'Form' refers to the information that a person or business is required to provide to MPI to support their application.

COST RECOVERY PRINCIPLES AND THE OVERALL APPROACH TO COST RECOVERY

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

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 guidelines² and in the Animal Products Act 1999 and the Wine Act 2003.³

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 are met, the Efficiency and Equity principles say that the beneficiaries of services should generally pay for services. That is, beneficiaries pay 100% of costs unless there is a strong efficiency or equity reason why they should not.

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

² <https://www.mpi.govt.nz/dmsdocument/30855/direct>

³ <https://www.legislation.govt.nz/act/public/1999/0093/latest/whole.html#DLM35716>
<https://legislation.govt.nz/act/public/2003/0114/latest/DLM223236.html>

Overall approach to cost recovery

The requirement to meet a level of Transparency and Justifiability and the default of beneficiary pays results in the following overall approach:

Customers/beneficiaries generally pay

Customers/beneficiaries should generally pay for the services they demand.

Charging beneficiaries encourages them to demand or use only the quantity and quality of services that they value highly enough. If the cost is subsidised by others, then beneficiaries will demand more services (with the cost being met by others). The extra demand from a subsidy is an inefficiency as it results in more use of resources in production than people value and are willing to pay for.

Charging beneficiaries helps ensure MPI service volumes or quality are not higher than is economically efficient.

When beneficiaries might not pay

Beneficiaries might not pay full costs in four situations:

Transparency and justifiability

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

In this situation it may be appropriate for MPI to:

- change fees/levies to the level that can be justified for the time being; and
 - cover the remainder of costs; or
 - recover the deficit from a future time period after further work is undertaken;
- guarantee that prices will not exceed a certain level over the next period;
- charge fees at a fixed level, rather than variable with time, to encourage efficient service delivery. ⁴

Administration costs

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

Externalities

The third is where there are externalities. Externalities are positive or negative impacts on third parties from the demand and supply of a good or service. MPI primarily deals with negative externalities. An example is the risk that arises from consumers demanding, and importers supplying, overseas products. A negative externality on a third party is the biosecurity risk from pest incursions on domestic farmers. Charging importers for MPI activities to reduce the risk encourages importers to reduce the risk and, therefore, need for the service. ⁵

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.

⁴ This last approach is that used in the status quo and in some of the options.

⁵ Administration costs of charging to account for externalities are also relevant.

OPTIONS

Identifying options

Feasible options are those that can address the problem and the Cost Recovery Principles. This section identifies feasible options by running through each element of the policy rationale above:

- that beneficiaries pay, unless:
 - MPI has not or cannot sufficiently met the Transparency and Justifiability principles
 - administration costs are prohibitive
 - there are externalities such that someone other than the beneficiary should pay
 - or there are equity reasons.

'Beneficiaries pay, and Issues around the Transparency/Justifiability of costs and around equity concerns has led to the options identified below. Appendix 2 sets out the identification of options in more detail.

List and description of options

Figure 2: Options

Structure and level of fees		
<u>Option</u>	<u>Description</u>	<u>Why is this an option?</u>
Status quo	Current fees	
Option (1)	Fully variable charges	Efficiency – A pure beneficiary pays approach would see businesses paying for the precise time involved with providing services (e.g. down to 15-minute increments).
Option (2a)	Standardised charges with a half-hour threshold <ul style="list-style-type: none"> • standard time charged is the typical time from Figure 1 • if the threshold is reached, the actual time is charged (in 15-minute increments) 	Transparency and Justifiability – Time spent by MPI staff can be variable due to natural variation in productivity (not everyone completes tasks at the same speed). As such, it might not be reasonable to charge some businesses a lower price and others a higher price because of chance.
Option (2b)	Standardised charges with a one-hour threshold	
Option (2c)	Standardised charges with a two-hour threshold	
Option (2d)	Standardised charges with no threshold	
Timing of changes		
<u>Option</u>	<u>Description</u>	<u>Why is this an option?</u>
As soon as possible	1 July 2021 start date	Cost recovery changes are usually brought in immediately after the Government makes decisions.
Defer the changes	1 July 2022 start date	Equity – The upheaval of Covid including higher business costs means producers are looking for cost savings. While the Government has so far preferred to deal with the impacts on businesses through central supports such as the wage subsidy and through supports to banks (to then support bank customers), industry has asked whether

ESTIMATED FINANCIAL AND ECONOMIC IMPACTS

This section briefly discusses the financial and economic impacts of the options. Changes in MPI's fees are changes in business costs. This feeds through to business margins and, over the medium- to longer-term, to market prices and quantities.

Compared to the status quo, Options (1) to (2d) increase total costs to industry across the fees listed in Figure 1 by about 80% or less than \$0.1 million per annum.

Although the proposed increase in revenue is proportionately large (80%), the total amount of extra revenue is estimated at less than \$0.1 million per annum and is spread across a wide range of industries and a large number of businesses.

For instance, most of the cost increase (\$55,000) is associated with RMPs. There are 1,408 businesses across 1,612 sites with 1,683 RMPs in total. The per business increase is, therefore, around \$40 per annum.

The negative impact of cost increases on demand for MPI services, reduce industry production, and increase market prices, the impact is proportional to the size of the costs increases. The options involve negligible cost increases and, therefore, negligible impact on demand for MPI services and prices and volumes.

ASSESSMENT AGAINST THE PRINCIPLES

Introduction

This section sets out a brief assessment of the options against MPI's Cost Recovery Principles. This section does this by considering the two core Efficiency questions around the structure of fees:

- Should the time allowed for each service change from current amounts?
- If so, should the time allowed be fully flexible, or should it still involve an element of standardisation?

In addition, there is an Equity question about from when any new structure should be implemented.

Summary assessment

It is MPI's assessment that Option (2b) provides the best balance between charging beneficiaries for the cost of services and accounting for variability in MPI productivity and encouraging MPI to be efficient.

In terms of time, MPI considers, on the basis of current information about Government preferences, that Option (2b) should be implemented as soon as possible. If the Government considers further support should be offered to businesses, Option (2b) could be deferred until 1 July 2022.⁶

Fuller assessment

Should the standard time change from the current times?

The first question is should the standard time charged for services be changed. This question gets at whether the status quo should be kept or whether another option (Option (1) to 2(d)) should be chosen.

While MPI does not have a central record of historical time recording data, MPI has conducted a review involving surveying staff views and having that reviewed by MPI management. MPI considers that staff should have a reasonable idea of how long it typically takes them to provide a service. Time recording

⁶ 1 July to 30 June is the reporting year for Government financials.

data would provide greater certainty but, overall, MPI considers that staff judgements should provide a medium level of confidence about the actual time spent on each service.

The overall difference between (staff judgements of) actual time and the regulated time is significant. Actual time is about 80% higher than currently regulated.⁷

If MPI had low confidence that actual times differed from regulated times – either because of the quality of information or because the difference was small – then changing charges would not meet the Justifiability and Efficiency principles.

MPI considers that changing the standard time is justified as the staff survey provides sufficient confidence around the typical times and the 80% (or more) variance is large enough to do something about. Doing so will also help meet the Efficiency principle by charging beneficiaries for the service rather than charging some beneficiaries too much and others too little (and having the Crown pick up the deficit).

Because of this, **the status quo is not MPI's preferred option.**

Compared to the status quo, Options (1) to (2d) increase total costs to industry across the fees listed in Figure 1 by about 80% or less than \$0.1 million per annum.

How much flexibility should there be?

Option (1)

If MPI could ensure that each staff member had equal and consistent levels of productivity and could clearly demonstrate time spent through proper time recording, Option (1) would be preferred. The risks around transparency and justifiability would be low and, so, beneficiaries should pay the cost associated with their demand for services.

Likely variability in staff productivity means that charging exactly the time spent on each service cannot be fully justified and that some level of standardisation might be justified. Additionally, imperfect transparency around MPI time recording means that there should be some incentive on MPI to keep processing times low.

If MPI had good time recording data, including information about how complex the business application was, a statistical analysis of natural variability versus application complexity might have been possible. This information does not exist. While MPI considers there to be sufficient confidence about the actual typical time spent delivering services, it is harder to be sure about how much variability there is from the typical time in processing each business's application. Some applications take much longer than the typical time, but MPI can't say with confidence how many applications.

Because of this lack of confidence, **Option (1) is not MPI's preferred option.** MPI does not consider that a fully flexible charging regime could meet the Justifiability principle and, as some businesses would be charged more and some less due to chance differences in staff productivity, it would also not meet the Efficiency principle.

Option (2d)

MPI is aware that some applications are complex and take much more time than standard. For this reason, it would not be efficient to average those costs over all businesses, meaning that **Option (2d) is not MPI's preferred option.**

Options (2a) to (2c)

This leaves Options (2a) to (2c). Without time recording data and other information, there remains some uncertainty as to the best approach. A lower threshold (such as with Option (2a)) risks charging businesses more for natural time variability, but will capture more of those businesses where

⁷ This estimate includes services where the typical time is lower than regulated, so the actual variance between actual and regulated time will be higher.

complexity is the true driver of more time being spent. A higher threshold (such as with Option (2c)) risks not charging businesses their true cost where complexity and customisation is the driver, but captures more situations where natural time variability is the cause.

Some of the uncertainty is reduced by noting that staff consider that a custom RMP can take around an hour longer than a template RMP (see

Figure 1). This suggests that more complex applications of any kind might take about an hour longer than more simple ones. It seems unlikely that services that normally take one hour to one and a half hours should take longer than two hours to two and a half hours unless complexity is the main driver.

Because of this, though there remains some uncertainty, it is MPI's judgement that Option (2b) provides the best threshold (one hour) for correctly separating situations where complexity in the application is driving higher processing times and where processing times are more likely to be the result of natural variations in productivity. **Option (2b) is MPI's preferred option** in terms of the structure and levels of fees.

When should any changes take effect from?

The final question relates to whether it is fair that the costs increase during the immediate post-Covid period.

Submissions highlighted accumulating cost pressures from various sources including due to Covid (while submissions did not explicitly mention freight costs, this is one which has been reported in the news and highlighted by submitters on other proposals consulted on at the same time) and, for wine, loss of revenue from tourism. It is highly likely that profit margins are temporarily lower due to Covid in the form of higher costs and, possibly, lower prices due to recessions overseas.

While the changes will result in small increases to business, costs add up. Businesses will be looking for savings from many sources. Deferring cost increases was not an option included in consultation, but it is reasonable for submitters to enquire about it. Submissions from New Zealand Winegrowers and The New Zealand Food & Grocery Council preferred that increases for wine charges be deferred until June 2022.

The Government has so far preferred to deal with the impacts on businesses through central supports such as the wage subsidy and through supports to banks (to then support bank customers). On the basis of this, MPI's preferred approach is to implement Option (2b) as soon as possible.

If the Government considers that past and current central supports adequately address Equity concerns, then implementing Option (2b) as soon as possible should be favoured on Efficiency and Equity grounds. If the Government has further concerns about the cost to businesses, then deferring Option (2b) by a year might be favoured.

There are no historical debts that would need to be written-off as a result of deferral, but about \$0.1 million would be unrecovered for a further year.

CONSULTATION

MPI consulted on these proposals in 2019 and again in 2021 via consultation documents published online and emailed to identified industry participants.

Industry submissions supported the introduction of a threshold and generally supported the proposed fees. One area of disagreement was New Zealand Winegrowers and The New Zealand Food & Grocery Council preferring that increases be deferred until June 2022.

Submissions raised the following specific issues:

- Whether a proportional threshold (e.g. adding 50%) should be adopted rather than a fixed threshold.
- Whether some of the typical times were too high.
- Whether the changes could be deferred one year.

Proportional threshold

MPI considers that the use of percentages as a threshold instead of a fixed time period as proposed is not a viable option. Approximately two thirds of the approvals we are proposing to adjust are half hour long renewals meaning that any proportional threshold will be too low to be administratively efficient and will have limited impact on driving MPI efficiency.

MPI considers that a one hour threshold will drive efficiency and capture longer applications while also being simple for MPI to administer. While different thresholds could be set for different fees, it would make charging more complex, meaning it could become difficult for fee payers to estimate costs. As such, MPI recommends continuing with the proposal as consulted.

Typical times

The following fees were queried by one submitter.

AP4: Application for registration of a Risk Management Programme

Submitter comment: “We strongly oppose a 2 hour maximum fee [for a template approval]... Our recommendation is a minimum of 1.5 hour fee for templates with increments provided for additional time”

MPI response: MPI considers the proposals reflect the time it takes to process an application. A breakdown of time required for a new custom or template application can be found below.

Steps	Template time (hours)	Custom time (hours)
Receipt, acknowledgement and pre-screening (incl. technical pre-screen) of application	0.50	0.50
Technical assessment of information supplied	1.00	2.00
Delegate approval of application	0.25	0.25
Updating of public register/database, issuing formal docs	0.25	0.25
Total Time	2.00	3.00

AP6: Application for registration of an amendment to an RMP

Submitter comment: “We do not agree with the proposal [to increase template amendment times from 0.5 hours to 1.5 hours]... 1 hour should be the target.”

MPI response: The steps in the table for AP6 above of receipt, technical assessment, delegate approval, and update register are the same for AP. AP6 is less complicated than AP4 and, so, only an hour is required to receive and assess the application. The half hour is still required in total for delegating approval and updating the public register. This half hour might explain the difference in expectations between MPI and the submitter.

AP65: Application for approval of maintenance compound (non-dairy)

Submitter comment: The increase for maintenance compounds (from 0.5 hours to 1.0 hours) is excessive and that a smaller increase would be sufficient. Alternatively, they suggested a differential charging structure with different rates for simple and complex applications.

MPI response: The steps in the table for AP6 above of receipt, technical assessment, delegate approval, and update register are the same for AP. AP65 is typically less complicated than AP4 and AP6, so, only half an hour is required to receive and assess the application. The half hour is still required in total for delegating approval and updating the public register. This half hour might explain the difference in expectations between MPI and the submitter.

Timing of changes

Some submitters asked for a deferral in changes by a year. This issue is discussed in the 'When should any changes take effect from?' section above and in the 'Conclusions and recommendations' below.

ADDITIONAL REQUIREMENTS FOR CHANGES MADE PART-WAY THROUGH A FINANCIAL YEAR

As noted in the 'How are the levies regulated?' section of the 'Status quo' section, there is an additional requirement for changes made part-way through a financial year. This legislative requirement is that the Minister needs to be 'satisfied' that affected parties 'agree or substantially agree' with changes under the Animal Products Act 1999 and 'agree or do not substantially disagree' with changes under the Wine Act 1999.

Legislation emphasises that the Minister needs to be satisfied. As such, this CRIS does not say whether the Minister should be satisfied or not.

The 'Consultation' section covers submitters views. Industry submissions supported the introduction of a threshold and generally supported the proposed fees. One area of disagreement was New Zealand Winegrowers and The New Zealand Food & Grocery Council preferring that increases for wine charges be deferred until June 2022.

CONCLUSIONS AND RECOMMENDATIONS

MPI's preferred approach is for Option (2b) to be implemented as soon as possible. If the Government considers further support should be offered to businesses, Option (2b) could be deferred until 1 July 2022.

Structure and level of charges

MPI considers that there is sufficient evidence that the true typical time spent on the services covered by this CRIS are different from those times that are set in regulation. For this reason, MPI proposes replacing the current regulated times, with the typical times in Figure 1.

By reducing typical charges for some, and increasing charges for others so that under-recovery does not continue, this part of the proposal best meets the Efficiency principle.

However, MPI considers that there are some transparency and justifiability issues that means MPI cannot charge for the precise time spent on an application.

MPI considers that it is sometimes hard to be confident about how much actual times vary from the typical time is due to natural variability in staff productivity and how much is due to complexity with the application. This relates to the Justifiability principle (and flows further through to the Efficiency principle).

A lack of comprehensive time recording raises Transparency concerns such that some level of financial risk on MPI through not being able to charge fully variable fees is likely to incentivise MPI to keep processing times low. This relates to the Transparency principle (and flows through to the Efficiency principle).

The typical difference in times between template and custom RMPs is about an hour. This seems a reasonable basis for establishing a threshold of an hour before higher-than-standard costs would be charged. Anything within that threshold would be charged at a fixed rate, encouraging MPI to keep processing times low.

MPI's preferred option is therefore Option (2b) – standardised typical charges with a one-hour threshold beyond which charges reflect actual time.

Option (2b) replaces the current regulated rates in Figure 1 with the typical times in Figure 1 and only charges higher fees if the actual time is more than an hour higher than the typical time. As an example,

it typically takes two hours to approve a new Risk Management Programme (RMP) application, if the time threshold is set at one hour above the time of the fixed fee, then:

- If the application takes two-and-a-half hours to process, \$270 would be charged. This is the same as the fixed rate set of two hours (at an hourly rate of \$135) as two and a half hours is within the two hour standard time plus one hour threshold.
- If the application took four hours to process, the applicant would be charged \$540 to process the application (four hours at the hourly rate).

All options, including Option (2b), carry about an 80% increase in the fees (less than \$0.1 million per annum) relative to the status quo.

Timing of changes

While agriculture production volumes are largely unaffected by Covid, MPI does not have timely information about the value of production and exports or of costs. It is highly likely that profit margins are temporarily lower due to Covid in the form of higher costs and, possibly, lower prices due to recessions overseas and, for the wine industry, from lower tourism.

The Government has so far preferred to deal with the impacts on businesses through central supports such as the wage subsidy and through supports to banks (to then support bank customers). This, combined with the general approach to Equity of beneficiaries rather than taxpayers paying, means that MPI's preferred option is to implement Option (2b) as soon as possible rather than delay a year.

The Government may, however, determine that further weight should be given to business concerns. In this case, deferring Option (2b) until 1 July 2022 might be preferred.

IMPLEMENTATION PLAN

If agreed the changes proposed will be made through amendments the Animal Products (Dairy Industry Fees, Charges and Levies) Regulations 2015, the Animal Products (Fees, Charges, and Levies) Regulations 2007, and the Wine Regulations 2006. The amendments will then be publicly notified in the New Zealand Gazette. Implementation will apply from 1 October 2021 (if the Government selects MPI's preferred approach around timing) and MPI will notify fee payers of the new rates that will apply prior to this, as well as updating its application forms and other material that include the new rates.

Administration costs for MPI are expected to be low with staff required to demonstrate when processing times exceed the threshold.

MPI understands that industry would prefer to have as early an indication of fee changes as possible so they can build them into contracts with customers. MPI will be endeavouring to progress cost recovery changes faster in future.

MONITORING AND EVALUATION OF SERVICES AND COST RECOVERY SETTINGS

MPI recognises that performance reporting is a critical component in providing transparency to industry and other interested parties, as well as ensuring ongoing system efficiency. This is explicitly acknowledged in the policies and guidance on our Principles.

To improve transparency, MPI has worked with industry to create a framework for reporting on the performance of cost-recovered services for all sectors. This has involved publishing annual reports about MPI's performance for the primary sectors. Performance reporting is an area for ongoing development for MPI – the annual reports currently focus on transparency around financial data and there is scope to use them to report against performance metrics (once developed).

The issues considered in this CRIS are, however, narrow and the scope of the CRIS is limited to considering how the regulations can best reflect, and address uncertainty in, actual time spent processing applications.

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 the Animal Products Act 1999 and the Wine Act 2003.⁸

The legislative definitions and interpretation of these are set out under each of the four principles 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.'

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.'

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.'

Interpretation

Efficiency is made up of several elements:

- (1) Costs should be the lowest necessary to meet customer demand. Customers can include businesses, members of the public, and the Government including other agencies. Meeting customer demand might involve treating different customers differently.
- (2) Costs should be charged to:

⁸ <https://www.legislation.govt.nz/act/public/1999/0093/latest/whole.html#DLM35716>
<https://www.legislation.govt.nz/act/public/2003/0114/latest/DLM223236.html>

- (a) Who benefits 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.
- (b) Whose behaviour can reduce the need and cost of the service – Typically both the supplier (MPI) and the customer will be able to do things to reduce the need and cost of the service. For example, MPI could adopt innovative technologies to reduce labour costs, while businesses might locate in urban, rather than rural, areas to reduce distance from market (including MPI's services).

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

Where there are externalities, it may be efficient to charge the third party as well, or instead of, charging the customer/beneficiary.

- (3) Charges should account for administrative costs – sometimes it will be administratively prohibitive to charge according to (2)(a) or (2)(b) so a simplified approach is warranted.
- (4) Charges should be competitive neutral – MPI should not use any dominant market position to charge inflated prices and make more than a fair economic return.

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.'

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.

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 3 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 require⁹ 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

⁹ 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.

identified if costs have not been sufficiently justified, or affected parties have not had a reasonable opportunity to test the costs.

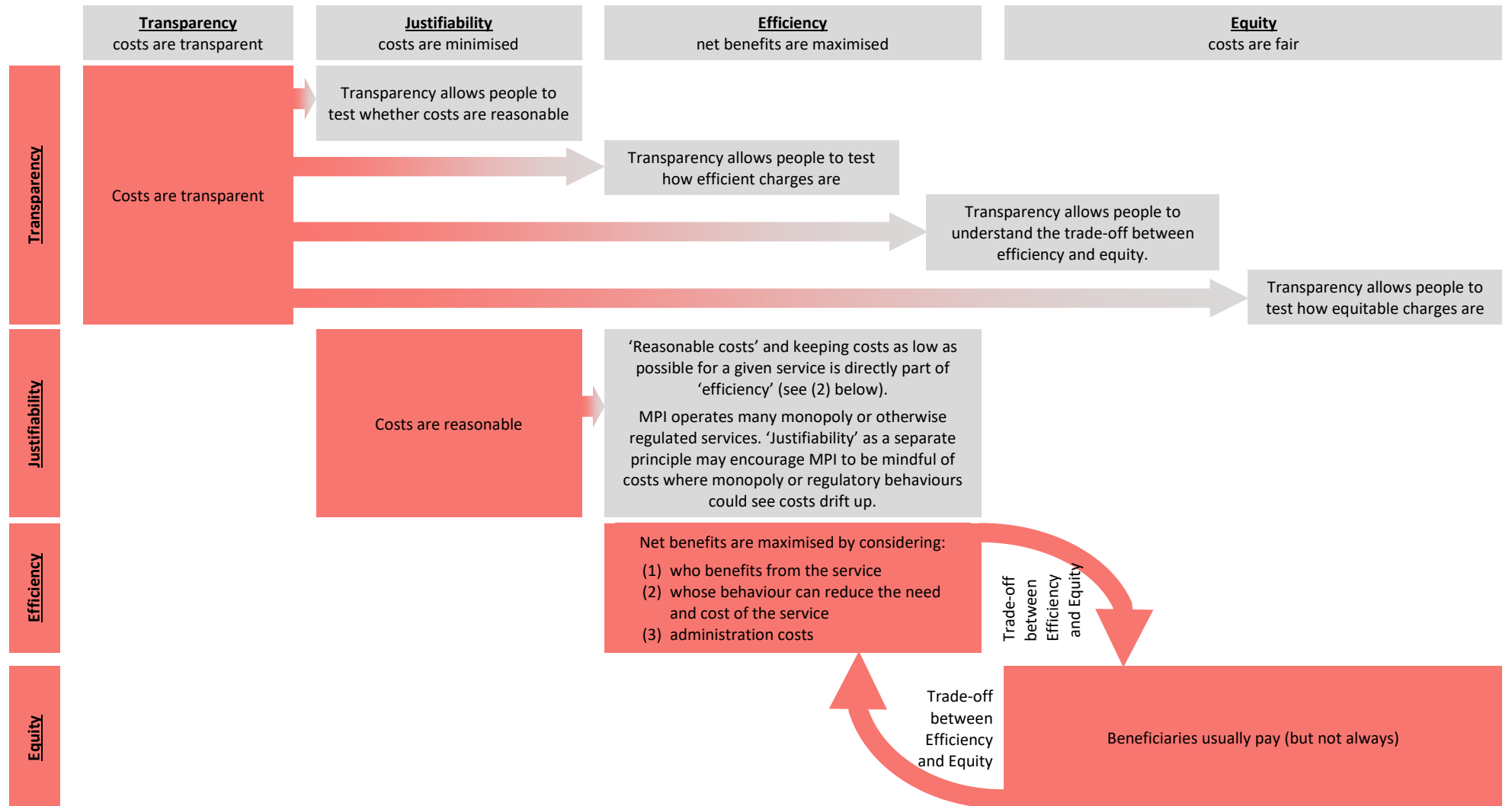
There will sometimes be trade-offs between Efficiency and Equity

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 pay for a service through Crown funding rather charging beneficiaries or those whose behaviour can reduce the need for the service (see (2)(a) and (2)(b)), 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.

Figure 3: Relationship between the Cost Recovery Principles



APPENDIX 2: IDENTIFYING OPTIONS

Beneficiaries pay

A pure beneficiary pays approach would see businesses paying for the precise time involved with providing services (e.g. down to 15-minute increments).

This approach is Option (1).

Transparency and Justifiability

There are some issues¹⁰ that mean that charging as precisely as 15-minute increments would not meet the Transparency and Justifiability principles.

A smaller issue is that while the relevant MPI business unit has been using time recording for invoicing purposes, it has not collected that data over time in a central spot for any monitoring, reporting and performance review purposes. Until that happens, the potential for time recording to be a fully reliable basis for precise charging and for demonstrating productivity is limited. Charging a fixed rate mitigates this by encouraging MPI to provide services as time efficiently as possible (as MPI receives no revenue to cover time spent in excess of the fixed amount). This issue is considered small as MPI could begin collecting that information.

A second, bigger, issue is that, even if actual time spent was centrally recorded, time spent by MPI staff can be variable due to natural variation in productivity – not everyone completes tasks at the same speed. As such, it would not be reasonable to charge some businesses a lower price and others a higher price because of chance.

This second factor is primarily why the current charges are fixed.

Options (2a) to (2d) have:

- standard charges to account for variability in productivity and to encourage MPI to be efficient
- and various time thresholds which, when reached, a fully time-variable charge applies instead of the standard charge.

Administration costs

MPI's cost recovery regime operates, with industry approval, on a basis of frequent reviews to ensure significant surpluses and deficits do not arise or are addressed quickly when they do. It is administratively easy for MPI to change the levels of charges. It is expected to be administratively easy for businesses to change their accounting settings too. The minor administration costs of frequent changes are already factored into MPI's approach of frequent reviews and changes.

Options that allow charges other than the current fixed charge will require staff to record when this happens. This is considered to be a negligible cost.

No options are required to address administration costs.

Externalities

The services provided are private goods. There appear to be no externalities – positive or negative – associated with these services.

No options are required to address externalities.

¹⁰ On meeting MPI's consultation requirements, MPI considers that the discussion document did a sufficient job setting out the issues discussed in this CRIS though it could have set out the discussion more fully.

Equity

MPI has identified one element of fairness that could be relevant to the analysis.

The upheaval of Covid including higher business costs means producers are looking for cost savings. While the Government has so far preferred to deal with the impacts on businesses through central supports such as the wage subsidy and through supports to banks (to then support bank customers), industry has asked whether cost increases could be deferred.

This CRIS considers an option to implement new charges from 1 October 2021 and from 1 July 2022.