

SUBMISSION

SUBMISSION TO

**Senate Rural & Regional Affairs & Transport
Reference Committee**

IN RESPONSE TO

**Review of Management of the Removal of the
Fee Rebate for AQIS Export Certification
Functions**

September 2009

PREFACE

The red meat sector is now Australia's No.1 agricultural enterprise. The Australian Meat Industry Council (AMIC) is the only employer association and recognised Peak Council in Australia, representing the commercial export and domestic processing industry.

AMIC is also the Peak Council representing the post-farm gate sector including smallgoods manufacturers, wholesalers, distributors, boning rooms and independent retail butchers – in total, close to 3,000 member companies representing over 55,000 workers directly employed in meat processing, exporting, wholesaling and retailing in Australia.

In addition, there is conservatively at least the same number again of Australian's involved in the road transport, shipping, carton and equipment manufacture, insurance, banking, laboratories and other ancillary industries – all dependent on the red meat processing and export sector for a proportion of their livelihood – an industry worth an estimated A\$17 billion to the Australian economy in total in 2007.

AMIC provides services and support to members that improves their working environment and is focused on achieving the best outcomes for the industry and its members as part of one voice on issues critical to their business.

KEY ISSUES ARISING OUT OF THE GOVERNMENT'S DECISION TO RETURN TO FULL COST RECOVERY FOR AQIS EXPORT CERTIFICATION CHARGES

Background

- The export rebate was the outcome of the Productivity Commission Review in 2000.
- The case has never been made to justify the removal of this rebate. AMIC was open and clear on its position well before the Beale Review began but was never consulted by the Beale Review on the issue.
- This Government has failed to acknowledge and accept that there are legitimate costs for Government in maintaining market access.
- No other comparable country in the world places such an extreme tax burden on its export industry.
- Removal of the rebate places Australia's most successful agricultural export industry at a competitive disadvantage in the export market place for questionable philosophical reasons.

Financial considerations

- Once the rebate is removed the export processing sector (84 establishments) will pay the government approximately \$84m for the right to operate in the export sector an average of **\$1 MILLION per plant**.
- Exporters in many other countries pay very little or nothing (the US industry contributes **10-12% of FSIS** operating costs compared to **Australia's industry funding 100%** of AQIS operating costs).
- The \$32m removed by the rebate decision is equivalent to the legitimate costs of government (market access, verification and certification) and therefore should remain as a government cost.
- The removal of the 40% rebate will see government charges to individual plants increase by more than **80%**.
- The red meat industry employs 55,000 people, many in remote and regional Australia and earns approximately \$8.7 billion (MLA data) in export earnings.
- The industry is sustainable, clean and green and is a real benefit to this country.
- Many small to medium-sized businesses will not be able to sustain this sudden cost increase and marginal players may be forced to leave the export sector if not the whole industry. Even larger businesses will defer or cancel development plans and/or close down some capacity.
- The monopoly government service has been inefficient, and beyond influence or challenge and yet industry is required by government decision to pay for it.

- Industry has no input into government staffing and policy decisions and yet is expected to fund the bureaucracy without question.
- Once again this provides the competitive edge to live exports where both the animals and the jobs are exported.
- Our export industries are price takers and the additional \$32m of costs will pass back to the already struggling production sector.
- The meat inspection reform agenda is a technical issue that should have technical milestones. The reform agenda however has been compromised by imperatives tied to a political decision to return to full cost recovery that has set unrealistic timeframes for its implementation.

Solution

1. Identify legitimate costs of government and fund them accordingly.
2. Allow at least 12 months for the staged phase in of any rebate removal (proposed date for implementation 1st July 2010).
3. Radically improve the AQIS service so that it is responsive to industry needs and reflects world's best practice.
4. The Ministerial Task Force set up to oversee the reform agenda continue in this role until the reform agenda has been fully implemented.
5. In the medium term, place AQIS operations under a Management Board consisting of elected industry members, government officials, and an independent financial expert.
6. Ensure that any future structural changes are vetted by the Board and implemented in a responsible manner.
7. If government is serious about the meat inspection reform agenda then it should not be seeking full cost recovery for the service until the productivity gains and efficiencies already identified have actually been delivered. We should not be endangering market access by expediting the reform agenda faster than our key customers have time to absorb it.

REVIEW OF MANAGEMENT OF REMOVAL OF FEE REBATE FOR AQIS EXPORT CERTIFICATION FUNCTIONS

1. INTRODUCTION

The Australian Meat Industry Council (AMIC) on behalf of the red meat processing and export sector, welcomes the opportunity to make the following comments on the Review of the management of the removal of the fee rebate for the Export Certification Functions...

The red meat processing and export sector represents the largest agricultural enterprise in Australia and one that is dependent on export markets for its viability. Close to 70% of our beef production and close to 60% of our sheepmeat production is exported to over 100 countries worldwide, worth close to A\$ 8.7 billion FOB to the Australian economy in calendar year 2007. This includes exports of tallow, hides, skins and other by products. Australia is now one of the largest red meat exporters in the world.

AMIC represents the commercial post- farm-gate red meat sector in Australia. As the country's largest agricultural export enterprise, this submission will focus on those issues most pertinent to its long term viability and what we believe is fair and reasonable.

2. WHY A VIABLE AGRICULTURAL EXPORT SECTOR IS IMPORTANT

The Australian red meat industry relies on exports. There is little we can do about the natural barriers we face, such as distances from abattoir to port and from port to customer. But we must try to reduce the regulatory barriers such as tariffs, quotas and non tariff trade barriers tied to technical market access issues that block access to many of our markets in one way or another. 'On-shore' demand for most of our production while important, is not growing at levels that will sustain the current industry structure, so export markets are the key to expanded sales.

The role of trade liberalisation in keeping costs down at home is also important, given the water and environmental land-use constraints and the limited number of Australian consumers relative to the global market. An open market and a competitive economy however are important for a sustainable red meat processing and export sector.

Growing and maintaining export demand is the source of higher prices and improved margins for the Australian industry long term. Those agricultural commodities that have seen the greatest real price improvements over the past 40 years have been those where export demand has driven growth. World food stocks are reportedly the lowest in 30 years. Recent food security concerns globally only enhances the opportunity for Australia to secure more long-term access for all agricultural products including red meat in the highest priced global markets. Adding cost in Australia through higher government charges fundamentally undermines that market access objective, especially when our international competitors are not facing the same costs. We must be seeking to remove cost from the production process not add to it if we are to remain globally competitive.

3. BACKGROUND TO THE ISSUE

April 2008

AMIC's position on a return to full cost recovery was clear and apparent well before the Beale Review was concluded. In AMIC's submission to the Beale Review on April 30 it clearly enunciated its opposition to the removal of the 40% rebate and identified the implications for the productivity of regionally based employers its removal would have.

The submission also identified the productivity gains that could be obtained from a restructure of AQIS and a review of the meat inspection model currently in place. AMIC also identified market access as a number one priority and the critical role of the Ag Counsellors in delivering that access.

September 2008

On September 11, APC Chairman, Gary Burrige and AMIC Executive Steve Martyn met with Minister Burke and advisors in Lismore. They expressed AMIC's opposition to the removal of the 40% rebate and the implications for industry. The Minister advised a decision had not been taken and that our arguments should be enunciated in a report to Canberra.

October 2008

On October 3, APC Chairman, Gary Burrige wrote to the Minister thanking him for the meeting in Lismore and expressing our ongoing opposition to the removal of the 40% rebate. As requested a Ministerial briefing note on AMIC's opposition to the removal of the 40% rebate was provided. In addition, a summary of meat inspection systems in other countries was provided to show the uncompetitive position the Australian industry would be put in if it was exposed to full cost recovery.

November 2008

On November 25, APC Chairman, Gary Burrige received a letter from the Minister advising no decision had been taken on the removal of the 40% rebate and encouraging AMIC to continue to submit its concerns to Canberra over the issue.

December 2008

On December 8 - APC Chairman, Gary Burrige wrote to the Minister advising that recent modelling had indicated a cost to the meat industry of over \$60 million would exist if the CPRS scheme was implemented as proposed. When this was added to the \$32 million cost impost from full cost recovery for AQIS export certification charges it would in AMIC's opinion lead to marginal players leaving the industry and a substantial restructure of the business operations of those remaining. AMIC also advised that it had commissioned independent research to identify the regional impact of the removal of the 40% rebate and that Government should avail itself of that research before making any decisions.

On December 18 A.M. – The Minister announced the 84 recommendations from the Beale Review were accepted in principle by the Government including a recommendation of a return to full cost recovery for AQIS export certification charges but that a suitable process of consultation with industry would take place before any final decision was taken.

On December 18 P.M. - Ministerial advisers commit to a meeting with AMIC in early 2009 as part of that consultative process. AMIC accepts the Minister's offer for a meeting in mid to late January..

January 2009

AMIC forms an AMIC Beale Review Committee and works throughout the Christmas/New Year break to develop a reform package to present for consideration by the Minister.

February 2009

The meeting with Minister Burke finally takes place on February 3 in Canberra where Gary Burrridge as Chairman of the APC is told the decision has been taken and that a return to full cost recovery will occur. The \$40 million rebate had gone. AMIC gives a presentation on the Strategic Evaluation Group (SEG) deliberations of the previous 5 years and the significant productivity gains and efficiencies that had already been developed and tested through that process. **AMIC's position is that it can only accept full cost recovery if those efficiencies and productivity gains are implemented.**

The Minister agrees to AMIC's request to form a Ministerial Task Force (MTF) made up of AQIS and AMIC personnel to progress a Meat Inspection reform agenda.

THE BEALE REVIEW DECISION

- The Federal Government decision to accept the Beale Review recommendation that ***export certification functions should return to 100% cost recovery broke a 9 year commitment from the Federal Government.***
- The decision represented up to \$32m additional cost for the red meat processing sector at a time it could ill afford to absorb an increased tax from Government given the global credit crisis.
- The Red Meat Industry refuted the argument that this was a subsidy. The recommendation had been made without a true understanding of the Government contribution in the first place nor the implications of its removal on the viability of the export sector.
- AMIC supported the basic thrust of the Beale Review but funding shortfalls generated by the formation of the proposed National Biosecurity Australia should not be borne by the meat industry. We do not believe the case has been made in the Review for the imposition of this tax either in a policy sense or an economic sense and the red meat processing sector and indeed the whole red meat supply chain unanimously oppose the proposal.

The Issues

- The decision by the Australian Government in November 2001 to cut AQIS Certification charges from 100% to 60% was unconditional and without any sunset proviso.. Processors have made their long term investment and expansion plans in good faith on that basis ever since. The Government decision in November 2001 was the culmination of years of campaigning against unfair "user charges" in which major studies by the Business Council of Australia, RIRDC, MLA and the Productivity Commission all played an important part. Those studies reaffirmed the basic economic principle that a "user charge" in excess of marginal cost is a tax.
- The Government has not accepted that there are legitimate costs for government in maintaining market access for meat products on the export market that are not present on the domestic market. The Beale Review itself supported this notion. The decision essentially imposed costs our competitors do not pay.
- The current AQIS budget for the meat certification program was around \$79m in 2007/2008. Industry paid approximately \$47.5m of this to cover the cost of meat inspectors, health certificates and certification. The government paid approximately \$32m which covered overheads of the Department and the market access requirements of Government.

- The Government's own Beale Review highlighted these functions should be funded from the Commonwealth budget rather than via cost recovery mechanisms.
- The red meat industry employs close to 50,000 people nationwide, primarily in country towns and regional areas and generates close to \$8 billion in export income for Australia. Many AMIC members consider the Government's multi-million dollar crises support and handouts to other industries does not compare well with the removal of a \$32m rebate for this heavily export oriented sector.
- The Beale Report clearly links the removal of the 40% rebate to changes in work practices within the Department. To impose a 40% tax on the industry and increase its overheads without corresponding efficiency gains in AQIS and departmental services is contrary to the philosophy of the Beale Review itself and would place exporters at a commercial disadvantage to our trading competitors. AMIC was not consulted on this decision by the Beale Review .
- These costs will need to be passed on to the producing sector and will place at risk employment in the industry across rural and regional Australia. Competing countries do not impose these costs on their meat export industries.
- Recent advice to Government about the increased profitability of the red meat industry because of exchange rate movements is commercially illusionary. Margins in the red meat processing sector remain tight. Quotes in the newspaper that "the removal of the subsidy equates to only a 0.5% currency movement in the Australian dollar" is commercially naïve and has no basis in real life. The margins within the processing sector irrespective of currency movements vary little between 1-2%.
- AQIS fees are already on an upward trajectory currently estimated at an additional 10% in 2009/2010. Cultural and operational change is now essential if real productivity gains are to be achieved. Making industry pay 40% more for a monopoly service we all agree needs change is not the answer and is not fair.
 - AMIC's concerns have been about delivering cost savings for all members big and small. Initial proposals have suggested there is not as much in the reforms for the smaller players yet they will wear a huge cost increase with the implementation of full cost recovery. This is likely to alter the competitive position of many smaller players. This is not something that can be identified and resolved quickly.
 - Both the Government and Austrade issued statements following the Federal Budget this year, extolling the virtues of the export sector and its crucial role in the Australian economy in raising average levels of productivity, driving creativity and innovation and helping to raise living standards by creating prosperity for the whole community. Both Tim Harcourt Chief Economist with Austrade and Trade Minister Crean highlighted the importance exporters play as employers in these difficult times. Given the tough trading environment at present it seems to be in total contrast to Government policy to be increasing export certification charges on Australian agriculture at this crucial period.

The Impact

- The proposed approach to the funding base resembles a tax on the export sector rather than any removal of a subsidy. A number of major studies have reaffirmed the basic principle that a "user charge" in excess of marginal cost is a tax.
- AMIC has undertaken sensitive, detailed research of individual plant data to demonstrate the regional implications of the proposed change. This data was neither available nor sought by the Beale Review during their deliberations and is yet to be considered by the Government.
- That research identifies there will be clear adverse impacts on processor profitability varying from a decline of over 2% to over 25% with smaller scale facilities suffering bigger declines in profitability. The four case studies undertaken reflected investment plans totaling \$5-10m will be deferred, current operations reviewed, production levels in some

cases reduced, and employment adversely affected. As the meat industry is one of the major regional employers in Australia, this impact would seem a contradiction to the fundamental rationale for the Government's stimulus package. (See Attachment 1).

- Preliminary calculations would suggest that removal of the 40% contribution could add up to \$5.00 per head to cattle and up to \$0.50 per head on sheep. In the context of the thin operating margins all processors trade under, this will represent increases of upwards of \$150,000 for smaller plants to in some cases \$1.5 million additional cost per registered export establishment for the service they are receiving now. This is not the marginal cost of the service being delivered and will have to be passed on to the producer if many regional businesses are to remain viable. This research was offered to government. They have not asked for a copy.

AMIC's Position

AMIC's position on this issue has not changed throughout this debate. There must be agreement to postpone any decision to remove the Government's 40% contribution to AQIS export charges until they can be matched with the implementation of the efficiencies and productivity gains proposed by industry. AMIC sought the establishment of a Ministerial Task Force to immediately review these proposals but without the added pressure of impending cost increases from Government for a service industry has no control over.

AMIC will accept a return to full cost recovery for those costs directly associated with the delivery of the service provided the productivity gains and efficiencies proposed by industry are implemented such that they offset the cost increases proposed. Industry has throughout the debate reserved the right to reject full cost recovery if AQIS cannot or are unable to implement the cost efficiencies identified and promised.

The Ministerial Task Force (MTF)

As part of the agreement in February, the Minister established a Ministerial Task Force (MTF) made up of AMIC and AQIS members to oversee the negotiation of a Meat Inspection Reform Agenda that would deliver the productivity gains and efficiencies to offset the increased costs associated with the removal of the 40% rebate.

After 4 months of intense negotiations, the AMIC Committee came to an agreement with the Federal Government in early June over a package totalling \$29 million that was to include a range of meat industry reforms and AQIS efficiencies along with technology improvements, IT upgrades, a new plant performance rating tool (PPRT) and in particular, new market access consultation arrangements between Government and industry.

As part of the package, Government agreed to a moratorium on any increase in AQIS fees and charges until October 1, 2009. Within this period AMIC asked for a full independent review of AQIS costs and services to be undertaken with a view to clarifying the true costs of the service and to review options that could provide the basis for an agreed approach to full cost recovery in the future. The costs of AQIS certification charges had continued to increase substantially despite attempts to reign them in.

An explanatory note was sent to each AMIC export member outlining the key parameters of the review and inviting each member to prepare submissions on the issue to be considered by the review. Ernst & Young were charged with the challenge of reporting back to the Task Force by September 1.

a. The Ernst & Young Review of AQIS Charges

Ernst & Young were requested to identify the legitimacy of DAFF pass through costs (Corporate overheads), identify the cost drivers behind the recent blow out in AQIS budget, and offer opinions as to the most equitable and transparent charging regime for AQIS and Industry in a cost recovered environment.

Ernst & Young held extensive consultations with industry members to ascertain their perspective on the government's changes and the likely impact on their export business.

At the time of writing Ernst & Young have produced a draft report that clearly implicates the Canberra central office bureaucracy as the primary driver in the cost blow out. Central office costs are identified as being responsible for more than one third of the \$15 million increase in Program costs from 2005-06 to date.

The Ernst & Young investigation shows Australian industry is being saddled with cost increases that are substantially more than the rate of inflation are not related to industry activity but are the result of inefficient bureaucratic procedures. To date industry has no right of reply or input into these charges – the government simply demands industry pay.

b. Current State of Play

At each meeting of the MTF, the realities of the challenge ahead and the obstacles to overcome in delivering the reform agenda became more evident. A total of 10 different meat inspection models were ultimately considered as further complications especially around timelines, industrial relations and maintenance of market access became evident with each, all of which has continued to delay any agreement on, and therefore start to, the reform agenda.

AMIC wrote to the Minister on the 17th June 2009 confirming the Australian Red Meat Industry's support for the proposed meat industry reform package agreed at the MTF. We also emphasised our right to reject full cost recovery if AQIS were unable to deliver the reforms proposed in the time frames originally intended.

By August 11, AMIC had to advise the Minister that after further extensive and prolonged deliberations through the MTF, there appeared to be no meat inspection reform model which could be taken to conclusion by AQIS and the meat industry within the time frame originally imposed by the government ie by 30 June 2010. It also appeared that the latest AQIS recommended model under consideration at the time would take at least 12-18 months to complete from commencement, assuming there were no insurmountable industrial relations hurdles. Legal advice was still to provide the level of confidence necessary to actually implement the preferred model in question.

We reaffirmed the earlier AMIC view that this reform process will take longer than 12 months and require more resources than have been committed to the current MTF process. Therefore, on behalf of the industry, AMIC was seeking a more strategic timetable and approach to removal of the 40% export rebate. This request was consistent with our position from the beginning that any move to full cost recovery needed to be commensurate with mutually agreed efficiency savings. The proposed model was only an interim step to MSEP+1 and MSEP our agreed ultimate goal and would not deliver the tangible offsets originally hoped for. On this basis, the industry believed that full cost-recovery for the existing service should not be re-introduced until this reform process was complete.

While industry members and Department staff have honestly, fairly and energetically entered into negotiations to identify reforms available to us, we now understand that these reforms may well only be available over a significantly longer timeframe than that currently covered by the Government's Export Certification Reform Package. Earlier commitments on a revision of existing standards including the MISS standard has been withdrawn or revised and consequently the original efficiencies and cost savings put on the table by AQIS back in April 2008 have had to be withdrawn at least in part. Even so, it remains industry's intention to continue to support the reform process, and to work with AQIS to drive change towards our ultimate objective. It has become clear that these reforms can not be achieved within the time frames to which we originally committed.

On this basis, AMIC has sought the Government's understanding and support for the necessary reform process going forward that recognized:

- the challenging reform agenda for the meat sector that will take at least 18-24 months to complete.

- that any AQIS staff redundancies that may result will need to be managed over a longer period (09/10 and 10/11) and should be fully funded by the Government (their employer) not industry
- that ongoing Ministerial leadership and support, as demonstrated for other sectors that employ similar or less people than the meat sector, is crucial to successful reform
- that it is critically important to the successful completion of the reform agenda that there is a change agent within AQIS committed full-time to meat certification reform that industry can rely upon to effect the change we all agree is necessary.
- that a moratorium on implementing a program of full cost-recovery for AQIS export certification charges be put in place until the reform process is completed.

The Solution

AMIC still considers that the opportunity for reform is too valuable to squander. We seek government support to grab this opportunity and despite the challenges ahead, take it to the next level and sustain it until its completion.

- The Australian processing sector through AMIC has taken a responsible approach to this issue. We have not asked for handouts like a number of other industries. On the contrary, we have developed a structured plan to deliver greater efficiencies in AQIS and departmental services and we have provided this to the Government with a comprehensive overview of the Plan. We are of the firm view there are major savings to be achieved in AQIS services if Government is really willing to adopt change. We only ask it be given a realistic timeframe for delivery before any increased taxes are imposed.
- It would be grossly unfair to impose any inter-departmental overhead costs on an industry already burdened by the current global credit crisis and impending increased costs under the Carbon Pollution Reduction Scheme. The challenge in the broader context is about Australia's number one agricultural enterprise remaining globally competitive.
- The car industry employs the same number of Australians as the meat industry, around 50,000 people, but generates export revenue 2.5 times that of the car industry at over A\$8.2 billion. The car industry received an A\$6.2 billion assistance package from the Federal Government last year. The export meat industry is not looking for a handout - only a hold on any increase in Government costs until mutually agreed productivity gains and efficiencies can be implemented.
- Industry is prepared to absorb more responsibility and invest in functions previously part of the AQIS regulatory framework. The AMIC meat inspection reform proposal has the potential to drive new efficiencies for both government and industry. If Government agrees change is required, industry should not be burdened with the full cost of that service until the proposed productivity gains have been implemented?
- We should not be seeking full cost recovery for AQIS export certification charges until the productivity gains and efficiencies already identified have been actually delivered. This should allow at least a 12 months staged phase in of any rebate removal beginning 1st July 2010. We should not be endangering market access by expediting the reform agenda faster than our key customers have time to absorb it.

Australian Meat Industry Council
September 2009