



# Amending the Cost Recovery Arrangements for Export Certification

Regulatory Impact Statement

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## **Agency Disclosure Statement – Amending the Cost Recovery Arrangements for Export Certification**

This Regulatory Impact Statement has been prepared by the Ministry for Primary Industries (MPI).

It provides an analysis of options to fund MPI's dairy export assurance programme once the dairy industry transitions to the electronic export certification system used for non-dairy animal product exports (AP E-Cert).

The preferred policy option would fund the dairy assurance programme using transaction and usage charges set by Director-General notice (the same cost recovery method used to fund the non-dairy animal product assurance programme). The preferred option is expected to be revenue neutral, but may result in slight changes to costs for some individual businesses. There is some uncertainty about:

- the level of AP E-Cert use charges. It is difficult to estimate how dairy users will use AP E-Cert; and
- the changes MPI will make to traceability requirements following the recommendations arising from the Government Inquiry into the Whey Protein Contamination Incident. Traceability changes have the potential to impact E-Cert use by requiring the dairy industry to submit more documents to AP E-Cert.

MPI will monitor the situation and take appropriate steps to ensure cost recovery is appropriate and meets the cost recovery principles of transparency, justifiability, equity and efficiency required by the Animal Products Act 1999.

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**Ministry for Primary Industries**

# Amending the Cost Recovery Arrangements for Export Certification

## STATUS QUO

MPI operates an official assurance programme for plant and animal exports

The Ministry for Primary Industries (MPI) issues export certificates to provide assurance from the New Zealand Government to importing countries that New Zealand products are fit for purpose, meet domestic food safety requirements and importing countries market access requirements. Section 60 of the Animal Products Act 1999 requires exported animal product to meet overseas market access requirements.

A core component of MPI's assurance programme is the web based applications (E-Cert) used to issue export assurances for New Zealand plant and animal exports. MPI's E-Cert applications enable exporters to electronically request export certificates and other eligibility documentation<sup>1</sup> from MPI, and supports MPI to process these requests and issue documentation to exporters and importing countries.

The E-Cert application that is used for dairy exports (Dairy E-Cert) is different to the application used for non-dairy animal product exports<sup>2</sup> (AP E-Cert). Dairy E-Cert was originally built for the dairy regulatory regime that existed prior to 2005 under the Dairy Industry Act 1952. The previous regulatory regime required significant manual processing by MPI staff. In 2005, dairy joined meat and seafood to be regulated under the Animal Products Act. This ensured a consistent, risk-based, regulatory regime applied to all animal product export industries. However, a separate assurance and cost recovery regime was created under the Animal Products Act to enable Dairy E-Cert to continue until an improved web-application was developed and less manual processing was required.

Appendix 1 shows the quantity of each type of electronic document processed by AP E-Cert and Dairy E-Cert, the value of the trade that the systems facilitate, and the number of users of these systems.

### MPI is migrating the dairy industry to the AP E-Cert application

MPI is nearing the end of a six-year programme to upgrade, merge or retire MPI's E-Cert applications for animal exports. Many of the software platforms, including Dairy E-Cert, used prior to this upgrade programme were old, had poor functionality and were incompatible with the data exchange requirements of China, the USA, and Canada. An upgrade to the AP E-Cert application (phase 1) was successfully implemented in June 2012. A second significant upgrade to the AP E-Cert application (phase 2) will be implemented in June 2014.

The next phase in the upgrade programme is to transition dairy industry users to the upgraded AP E-Cert application and progressively decommission the Dairy E-Cert application.

The rebuilt AP E-cert offers a number of significant benefits over Dairy E-Cert:

1. greater flexibility for creating export certificates that meet changing overseas market requirements;
2. anti-fraud functionality, which is particularly important for many of our most important markets, including China;

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<sup>1</sup> Eligibility declarations and documents contain information about the product and its market eligibility.

<sup>2</sup> Non-dairy animal product sectors are sectors such as meat, seafood, wool, bee products etc.

3. greater reliability than the current systems and lower maintenance costs;
4. access to better export data for trade responses and planning; and
5. compliance with the United Nations Centre for Trade Facilitation and Electronic Business (UNCEFACT) data standard for export certification and allows direct system-to-system connections with importing countries. China has explicitly expressed a desire to move to this standard.

MPI has engaged extensively with major trading partners, particularly Canada, the EU, the USA, and China to ensure system compatibility. A pilot involving all dairy companies exporting to Australia, Korea, Singapore, South Africa, and the United Arab Emirates will begin in July 2014. If the pilot is successful and dairy users and other trading partners are ready, all dairy users will be progressively migrated to AP E-Cert.

MPI has a Business Continuity Plan and will continue to run Dairy E-Cert in parallel during the pilot and early transition period to ensure that if any issues or disruptions arise a contingency plan is in place.

Dairy E-Cert is funded by a different cost recovery approach than AP E-Cert

Section 113 of the Animal Products Act requires the Minister and MPI to recover the costs of administering the Act that are not funded by Government. Section 113 also requires cost recovery to be conducted in an efficient, equitable, transparent and justifiable manner. Export certification is considered a private good and is not funded by government.

Current E-Cert cost recovery arrangements are set out in Appendix 3 and summarised below:

- Dairy product – under the Animal Product (Dairy Industry Fees & Charges) Regulations 2007, the issue of all official assurances for dairy exports is charged on an hourly rate basis (equating to between \$65 and \$115 for each export certificate issued); and
- Non-dairy animal product – under the Animal Products (Fees, Charges, and Levies) Regulations 2007 there are two components to official assurances charges for non-dairy exports:
  - a fixed fee per certificate (currently \$36 per export certificate issued<sup>3</sup> and \$412 for reissue when demanded by the importing country); and
  - a formula-based charge for use of the E-Cert system, which has time-based and transaction-based components.

## Problem Definition

The cost recovery approach used to fund dairy assurance will not be transparent, efficient, equitable and justifiable once dairy is transitioned to AP E-Cert

The hourly rate charge in the Animal Product (Dairy Industry Fees & Charges) Regulations 2007 was designed for the current E-Cert system. AP E-Cert is automated and processing is performed mostly by the application. AP E-Cert will not require as much manual processing by MPI staff.

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<sup>3</sup> Waivers are in place that reduce this fee to \$17.50 for wool, hides, skins and game trophies, \$20 for fish (including shellfish), and \$25 for other animal products.

Continuing to charge dairy users solely on an hourly rate basis would be inappropriate as charges would be based on use of MPI's servers, rather than staff time spent processing export documentation. Charging dairy users on an hourly rate basis is likely to result in over-recovery or under-recovery as dairy users are likely to pay higher charges when MPI's servers are slow and lower charges when the servers run fast.

Under or over recovery would be inefficient as it would not encourage efficient use of MPI's services by industry users. Over or under recovery would also be inequitable as dairy AP E-Cert users would be subject to a different charging method and potentially pay more than non-dairy AP E-Cert users. Imposing higher charges for one group of users using an identical service would not be justifiable, nor would it reflect a transparent cost allocation.

These outcomes are inconsistent with the Animal Product Act requirements for cost recovery to be transparent, efficient, equitable and justifiable.

## Objectives

The objectives are to:

- ensure dairy assurance cost recovery meets the Animal Product Act requirements for cost recovery to be transparent, efficient, equitable and justifiable; and
- maintain an appropriate level of funding for the dairy assurance programme.

# Regulatory Impact Analysis

## OPTIONS

MPI considered two options to align dairy and non-dairy cost-recovery following amalgamation. These included

1. Option 1: Maintain the status quo
2. Option 2: Continue to cost recover, but align the cost recovery approach used to fund the dairy assurance programme with the approach used for non-dairy.

Consideration of Crown funding as an option for funding the dairy assurance programme is out of scope. Export assurance, including dairy assurance, is considered a private good. Moving to Crown funding would therefore be inappropriate.

# Analysis

## OPTION 1 – STATUS QUO

For the reasons given in the problem definition, option 1 would not meet the Animal Product Act requirements for efficient, equitable and justifiable cost recovery. Option 1 would maintain funding for the dairy assurance programme, however there would be some uncertainty about the level of recovery given the potential for under or over-recovery.

## OPTION 2 – ALIGN DAIRY WITH NON-DAIRY

Option 2 would ensure cost recovery meets the Animal Product Act requirements for efficient, equitable and justifiable cost recovery. Option 2 is equitable in that users of AP E-Cert would be charged using the same mechanism with a proportionate share of direct and indirect costs.

MPI's regular industry reporting and consultation process when setting fees supports efficiency, transparency and justifiability. Reporting to industry ensures fees are transparent, justifiable and reflect an efficient level of service provision. Funding the programme by transaction and usage charges has also been shown to encourage efficient use of AP E-Cert by non-dairy animal product users.

The ability to adjust fees by notice rather than regulation ensures MPI has sufficient flexibility to maintain an appropriate level of funding for the dairy assurance programme and adjust fees to address any under or over recovery before significant deficits or surpluses accrue.

## COST IMPACT OF OPTION 2

The cost of MPI's dairy assurance programme is currently around \$3.8m (around 0.03% of the value of dairy exports). The fee for issuing an electronic export certificate for dairy consignments will drop from between \$65 – \$115 to around \$36 for each certificate issued.

AP E-Cert usage charges will be introduced for the dairy industry based on the formula in Part 6 Schedule 1 of the Animal Products (Fees, Charges, and Levies) Regulations. MPI's modelling indicates that the new usage charges will offset the lower fees for export certificates. As noted in the disclosure statement, there is some uncertainty about how much the dairy industry will use the AP E-Cert system and this will impact on their usage charges. MPI expects that industry users will achieve a steady state of use within 6 months once users become familiar with the system.

AP E-Cert use will be monitored and the Director-General has the power to apply discounts or adjust the charging rates, if necessary, to support equity, efficiency, transparency and justifiability.



## Conclusion

MPI's preferred Option is Option 2 as it will result in more efficient, equitable, transparent and justifiable cost recovery. Option 2 will also ensure an appropriate level of funding for the dairy assurance programme.

## Consultation

Dairy industry processors and exporters, including the Dairy Companies Association of New Zealand, have been fully engaged in, and support, the project moving the dairy industry to AP E-Cert. MPI established the Dairy Certification Transition Liaison Group to oversee the E-Cert transition programme of work and ensure it met the needs of industry and government. This Liaison Group consists of representatives from MPI, third-party verifiers, and New Zealand's top six dairy exporters, which include Fonterra, Tatua, Synlait, Open Country Dairy, Westland, and Dairy Goat Cooperative.

MPI released a discussion document titled: '*Dairy Export Official Assurances: Charging for Use of Animal Products E-Cert System*' in February 2013. The document set out proposals to align the dairy and non-dairy animal product E-Cert systems. MPI received six submissions seeking clarity on how the AP E-cert system works and what the charges would be under the new regime. MPI responded directly to submitters on all issues.

MPI followed the formal consultation round up with a series of road shows across the country for the dairy industry in late 2013. The road shows covered the differences between Dairy E-Cert and AP E-Cert, the plan for how dairy users will transition to AP E-Cert, including training, and provided an opportunity for individuals to raise any issues with MPI.

# Implementation

## REGULATORY CHANGES

The Animal Products (Dairy Industry Fees and Charges) Regulations will need to be amended to align the cost recovery approach with the cost recovery approach in Schedule 1, Part 6, of the Animal Products (Fees, Charges and Levies) Regulations.

Additional minor changes that will be made to the Animal Products (Fees, Charges and Levies) Regulations at the same time include:

1. revoking clauses 2 and 3 in Schedule 1 Part 6 of the Animal Products (Fees, Charges and Levies) Regulations to remove the requirement to fund half the assurance programme by usage charges and half by transaction charges; and
2. updating the reference to “Ministry Verification Agency” in Schedule 1 Part 6 of the Animal Products (Fees, Charges and Levies) Regulations to “Recognised Agency” with corresponding changes to the new Animal Products (Dairy Industry Fees and Charges) Regulations.

Regulatory impact analysis was not performed for these amendments as change 1. will reduce costs for business and 2. is minor and technical **Implementation**

The amendments are intended to come into force on 1 July 2014 as part of MPI's implementation programme for transitioning the dairy industry into the AP E-Cert system. A slight delay to commencement may be necessary to ensure compliance with the 28 Day Rule.

## Monitoring and Review

MPI monitors E-Cert cost recovery on a monthly basis to ensure the fees set in notice remain appropriate.

MPI provides financial information to industry representatives on the AP E-Cert Steering Group, which covers:

- the annual AP E-Cert budget;
- monthly reporting of AP E-Cert revenue;
- quarterly reporting of AP E-Cert expenditure; and
- quarterly update of performance against annual budget

MPI will review the effectiveness of the preferred option and any over or under recovery that eventuates as part of a wider food sector cost recovery review currently underway.

## Appendix 1: Dairy and non-dairy use of E-Cert

Table 1 shows the quantity of each type of electronic document processed by AP E-Cert and Dairy E-Cert, the value of the trade that the systems facilitate, and the number of users of these systems. Users include exporters, processors, inspectors and verifiers.

Table 1: Dairy and non-dairy use of E-Cert (2012-2013)

E-Certification documents	Number Issued	Value of Trade (2013)	Number of Users
AP E-Cert Eligibility Documents	380,000		
AP E-Cert Eligibility Declarations	41,000	\$6.6 billion	5,000 – 6,000
AP E-Cert Export Certificates	100,000		
AP E-Cert Database Transactions	14,250,000		
Dairy E-Cert Summary of Records	65,000	\$13.4 billion	2,000
Dairy E-Cert Exports Certificates	50,000		

## Appendix 2: Current and Proposed Dairy Export Certification Fees<sup>4</sup> from 1 July 2014

### 1. Current Dairy E-Cert fees - *current Animal Products (Dairy Industry Fees and Charges) Regulations 2007, Schedule, Part 1:*

Service Area	Type of fee	Fee
Issue of official assurance	Issue fee	\$140.28 per hour or part hour
	Disbursements	Actual cost

### 2. Current non-dairy AP E-Cert fees that would apply to dairy - *under Animal Products (Fees Charges and Levies) Regulations 2007, Schedule 1 part 1 and Part 6:*

Service area	Type of fee	Fee
Certification	Fixed charge	\$36.80
Re-issue of certificate, where replacement demanded by importing country	Fixed charge plus hourly rate, capped	\$421.16 per replacement certificate plus assessment charge of \$140.28/hour for any hours exceeding 3 hours, to a maximum of \$1,022
AP E-cert transactions (EC)	Formula - Cost per database transaction plus cost per second	Set by Notice: (currently) \$0.14 + \$0.20
AP E-cert transactions (EDec)	Formula – Cost per database transaction plus cost per second	Set by Notice: (currently) \$.08 + \$0.11

Disbursements will continue to be charged on an actual and reasonable basis, as per Section 120 of the Animal Products Act 1999.

<sup>4</sup> Fees are GST inclusive; proposed fees may differ from those currently shown in Regulations due to the change of GST rate from 1 October 2010.