

Application of Cost Recovery Principles

Australian Maritime Safety Authority

Department of Agriculture and Water Resources

Department of Health

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Canberra ACT

14 May 2019

Dear Mr President

Dear Mr Speaker

In accordance with the authority contained in the *Auditor-General Act 1997*, I have undertaken an independent performance audit in the Australian Maritime Safety Authority, the Department of Agriculture and Water Resources and the Department of Health. The report is titled *Application of Cost Recovery Principles*. Pursuant to Senate Standing Order 166 relating to the presentation of documents when the Senate is not sitting, I present the report of this audit to the Parliament.

Following its presentation and receipt, the report will be placed on the Australian National Audit Office's website — <http://www.anao.gov.au>.

Yours sincerely



Grant Hehir
Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

AUDITING FOR AUSTRALIA

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Summary and recommendations

Background

1. Cost recovery is one element of the Australian Government's 'Charging Framework', implemented in July 2015 across the general government sector to improve the consistency of charging activities and help determine when it is appropriate to charge for a government activity.¹ The Department of Finance has issued the *Australian Government Cost Recovery Guidelines* (Cost Recovery Guidelines) to support the implementation of the Charging Framework. The Cost Recovery Guidelines must be applied by all non-corporate Commonwealth entities, and by corporate Commonwealth entities where the Finance Minister has made a 'government policy order' that applies the Australian Government cost recovery policy to them.²
2. The Cost Recovery Guidelines (paragraph 15) state that entities must apply the following three principles across all stages of the cost recovery process: transparency and accountability; effectiveness and efficiency; and stakeholder engagement.
3. This audit considers the application of cost recovery principles in the: Australian Maritime Safety Authority (AMSA); Department of Agriculture and Water Resources (Agriculture); and Department of Health (Health) for the Therapeutic Goods Administration (TGA).³

Rationale for undertaking the audit

4. The government charges people and businesses to recover the costs of providing some services. In auditing cost recovery in the selected entities, the Australian National Audit Office examined whether the Cost Recovery Guidelines were applied effectively, so that charges were set to not over- or under-recover costs, and stakeholders were engaged in the processes for setting charges.

Audit objective and criteria

5. The objective of the audit was to assess whether selected regulatory entities effectively apply the cost recovery principles of the Australian Government's cost recovery framework.
6. Reflecting these principles, the audit criteria were:
 - Are the entities' cost recovery arrangements transparent and do they promote accountability?

1 Department of Finance, *Australian Government Charging Framework*, Resource Management Guide No. 302, July 2015. Available from <https://www.finance.gov.au/resource-management/charging-framework/>, [accessed 14 January 2019].

2 Department of Finance, *Australian Government Cost Recovery Guidelines*, paragraph 7, p. 4. Available from <https://www.finance.gov.au/resource-management/charging-framework/>, [accessed 14 January 2019]. The *Public Governance, Performance and Accountability (Charging for Regulatory Activities) Order 2017* requires all the agencies listed in the Order Schedule to apply approved regulatory charging activities, specifically cost recovery.

3 Agriculture and Health are non-corporate Commonwealth entities and therefore automatically required to adhere to the cost recovery policy and associated principles. The Minister for Finance has made a government policy order that applies the cost recovery policy to AMSA.

- Are the entities' cost recovery arrangements effective and efficient?
- Have the entities engaged stakeholders effectively in the design, planning and implementation of their cost recovery programs?

Conclusion

7. Health, Agriculture and AMSA have each been partially effective in implementing the cost recovery principles of the Australian Government's cost recovery framework.

8. Each entity has scope to improve the transparency and accountability of its cost recovery arrangements, mainly through more current and/or comprehensive reporting of performance in Cost Recovery Implementation Statements. Otherwise, the governance and internal accountability arrangements of the three entities are fit for purpose.

9. Each entity also has scope to improve the effectiveness of its cost recovery arrangements. AMSA and Health have significantly over-recovered costs in recent years. Agriculture has over-recovered costs through levies and under-recovered costs through fees. There is no assurance that entity charges recover the efficient costs of their activities, although Agriculture has benchmarked some of its costs. Entities' cost recovery policies and cost recovery methodologies are at varying levels of being fit for purpose, with Health's approach for the TGA the most complete.

10. Each entity regularly engages with stakeholders on cost recovery through industry consultative committees, but none have documented cost recovery engagement strategies. Health has been largely effective in engaging with stakeholders to develop and implement the TGA's cost recovery activities, and has regularly updated the TGA's Cost Recovery Implementation Statements to support this engagement. AMSA and Agriculture have focused on consulting on the introduction of new or revised cost recovery arrangements and have not always updated their Cost Recovery Implementation Statements to support engagement on cost recovery of existing regulatory activities.

Supporting findings

Transparency and accountability

11. AMSA, Agriculture and Health have not fully complied with key requirements of the Cost Recovery Guidelines, particularly those relating to Cost Recovery Implementation Statements, with Agriculture and AMSA not updating these at least annually as required. Each entity has policy approval to charge for its regulatory activities and services and has legislative authority to charge, although Health has ministerial, not government policy approval, to meet the cost of fee-free activities through higher charges on other users. The Department of Finance should refine the Cost Recovery Guidelines to provide greater clarity on some requirements and take steps to promote greater levels of compliance with the Guidelines.

12. The three entities have reported on cost recovery performance principally through their Cost Recovery Implementation Statements and annual reports. However, Agriculture and AMSA have not updated their Cost Recovery Implementation Statements annually to include actual and updated financial data. Agriculture's last Cost Recovery Implementation Statement and accompanying report on performance was in 2015–16 and AMSA did not publish a Cost Recovery

Implementation Statement for 2017–18. There is scope for each entity to improve the level of information on cost recovery performance included in their Cost Recovery Implementation Statements and annual reports.

13. Each entity has established effective cost recovery governance and accountability arrangements. The arrangements include an internal management committee to oversee cost recovery activities and provide guidance to staff on implementation of cost recovery policies, and reporting to the committee and entity executive board on cost recovery performance.

Efficiency and effectiveness

14. There has been significant misalignment between revenue and expenses for AMSA and the TGA, with the costs of some activities being consistently over-recovered and others consistently under-recovered. Overall, Agriculture has had a proportionately small under-recovery on its cost-recovered activities.

15. AMSA and Health need to be more proactive in addressing structural over- and under-recovery of the costs of their activities. AMSA and Agriculture have reviewed their cost recovery legislated charges every four to five years. While this provides certainty to industry and the entities, charges should be reviewed and adjusted more frequently where there are structural misalignments in expenses and revenues for cost-recovered activities.

16. AMSA does not recover the full cost of its fee-based activities, and funds the shortfall from levy-based revenue. If it is not feasible to recover the full costs of these activities, AMSA should seek the government's approval of the partial recovery, and how the shortfall is to be met, with disclosures of any cross-subsidies included in its Cost Recovery Implementation Statements. AMSA should also examine suitable proxies for its levy-based charges in its review of charges related to the introduction of the National System.

17. Agriculture recovers the costs of activities provided to specific individuals or organisations through a combination of fees and levies, rather than recovering their full cost through fees, as required by the Cost Recovery Guidelines. Agriculture should use the current review of its charging arrangements to align the structure of its fees and charges with the requirements of the Cost Recovery Guidelines.

18. There is scope for all three entities to improve their costing practices. The cost model used by AMSA does not accurately capture the costs of providing the regulatory activities or calculate charges that are aligned to those costs. While Agriculture uses an activity-based methodology, it is not possible to determine the full cost of the output from Agriculture's model. Health also uses traditional activity-based costing for the TGA's activities, with the cost of regulatory activities linking to the prices and estimated revenues for those activities, although Health could improve the attribution of effort to regulatory activities.

19. None of the three entities have incorporated efficient costs in their cost recovery models and only Agriculture has sought to benchmark the costs of its regulatory activities with those of other entities. There is an opportunity for the Department of Finance to examine how benchmarking can be further encouraged and facilitated.

Stakeholder engagement

20. None of the three entities have documented ongoing cost recovery engagement strategies. Rather, the entities have stakeholder engagement strategies for specific cost recovery activities and/or have drawn on broader engagement frameworks for the entity. The lack of documented ongoing cost recovery engagement strategies is reflected in little coverage of the issue in the entities' Cost Recovery Implementation Statements. Notwithstanding the lack of a documented strategy, Agriculture and Health have adjusted their consultative arrangements in response to stakeholder feedback. AMSA's stakeholder engagement has focused on implementing the National System and not directly on cost recovery of regulatory functions related to this audit.

21. Health has actively and regularly engaged with stakeholders on the TGA's activities through cost recovery policy development, implementation and review stages. AMSA and Agriculture have mainly consulted on new or changed cost recovery activities, although they do regularly engage with industry through their industry consultative committees. There is scope for all three entities to implement performance measures for consultation on cost recovery to promote continuous improvement of cost recovery stakeholder engagement processes.

Recommendations

Recommendation no. 1

Paragraph 2.41

The Australian Maritime Safety Authority, Department of Agriculture and Water Resources and Department of Health:

- (a) ensure that their Cost Recovery Implementation Statements are fully compliant with the Cost Recovery Guidelines, including in relation to required updates; and
- (b) report annually in their Cost Recovery Implementation Statements on their cost recovery performance at the regulatory activity level.

Australian Maritime Safety Authority: *Agreed.*

Department of Agriculture and Water Resources: *Agreed.*

Department of Health: *Agreed.*

Recommendation no. 2

Paragraph 2.48

The Department of Finance:

- (a) advises entities at the start of each budget year of their obligation to update their Cost Recovery Implementation Statements;
- (b) reviews and refines the Cost Recovery Guidelines to address issues listed at Appendix 2 of this audit; and
- (c) explores additional mechanisms to improve entities' compliance with the Cost Recovery Guidelines, including through the biennial charging survey.

Department of Finance: *Agreed.*

**Recommendation
no. 3**

Paragraph 3.61

The Australian Maritime Safety Authority:

- (a) as part of its planned review of its charging arrangements following the introduction of the National System, examines the use of tonnage-based proxies for its levies to enable charges to be closely linked to the level of efficient regulatory effort expended for the specific outputs;
- (b) develops a cost recovery model that aligns revenues of outputs within regulatory activities to the efficient cost of providing those outputs;
- (c) reviews charges for regulatory activities covered by the Regulatory Functions Levy and the Marine Navigation Levy to enable alignment of the costs and revenues under each levy arrangement;
- (d) examines ways to reduce the cost of providing its fee-based services; and
- (e) seeks a decision from the government on how the cost of its fee-based services should be met if it cannot fully recover the cost of these services.

Australian Maritime Safety Authority: Agreed.

**Recommendation
no. 4**

Paragraph 3.63

The Department of Agriculture and Water Resources:

- (a) uses the current review of its charging arrangements to align its fees and levies with the Cost Recovery Guidelines; and
- (b) develops a cost recovery model that aligns the prices, expenses and revenues of outputs within regulatory activities to the efficient cost of providing those outputs.

Department of Agriculture and Water Resources: Agreed.

**Recommendation
no. 5**

Paragraph 3.68

The Department of Health:

- (a) implements a consistent quality assured approach for the collection of staff effort data for use in the cost recovery model of the Therapeutic Goods Administration;
- (b) adjusts charges to reduce cross-subsidisation across industry sectors; and
- (c) further reviews the cross-subsidisation of fee-free services and seeks a decision from the Government on how the cost of the services should be met.

Department of Health: Agreed.

**Recommendation
no. 6**

Paragraph 4.10

The Australian Maritime Safety Authority, Department of Agriculture and Water Resources and the Department of Health:

- (a) implement ongoing stakeholder engagement strategies for their respective cost recovery arrangements in consultation with stakeholders;
- (b) include these planned engagement strategies in their draft Cost Recovery Implementation Statement each year; and
- (c) include performance measures for engagement on cost recovery in their Cost Recovery Implementation Statements.

Australian Maritime Safety Authority: *Agreed.*

Department of Agriculture and Water Resources: *Agreed.*

Department of Health: *Agreed.*

Summary of entity responses

22. The proposed audit report was provided to the audited entities, which provided summary responses that are set out below. Their full responses are reproduced at Appendix 1.

Australian Maritime Safety Authority

23. The Australian Maritime Safety Authority (AMSA) welcomes the audit report and findings, which to a significant extent mirror our own self-assessment in areas that require improvement. It provides AMSA with insights into the overall cost recovery management process and supports the improvements we are currently putting in place to strengthen our compliance and future cost recovery performance.

24. AMSA notes and agrees with the recommendations presented. With regard to the structure and pricing for levies, AMSA proposes to work with both the Department of Infrastructure, Regional Development and Cities, and the Department of Finance, to dovetail any structural considerations to the upcoming review of the domestic commercial vessel regulatory charging activities in 2020–21.

25. AMSA is committed to ongoing improvements in our cost recovery arrangements.

Department of Agriculture and Water Resources

26. The department welcomes the audit report, and acknowledges the ANAO's overall findings and recommendations. The department is pleased that the report highlights the robust approach to cost allocation and cost modelling that is already in place for our regulatory functions.

27. The department remains committed to continuous improvement of the cost recovery arrangements in place for its regulatory functions. These improvements will underpin a stable and contemporary cost recovery approach that continues to support the regulatory functions of the department.

28. The department acknowledges the importance of stakeholder engagement as a key part of the cost recovery process, and will continue to develop and implement robust stakeholder engagement processes for cost recovery.

Department of Health

29. The Department of Health (the department) welcomes the findings in the report and agrees with the recommendations relating to the TGA's cost recovery activities.

30. The audit found while every entity had scope to improve the effectiveness of cost recovery arrangements, it was pleasing to note the TGA's cost recovery policies and methodology are largely compliant with the Department of Finance's Cost Recovery Guidelines (CRGs). The department is fully committed to the effective implementation of the requirements set out in the CRGs and has already taken steps to address issues identified in this audit.

31. The department notes the ANAO has identified specific areas for further focus, including over recovery of costs, authority for fee-free services and the department's consultation strategy in the Cost Recovery Implementation Statement (CRIS). Most over recovery occurred in two sectors (prescription medicines and medical devices) as a result of delayed expenditure because of later than planned implementation of major reform projects while the Medicines and Medical Devices Review was underway. TGA revenue resulting from underlying fees and charges continued to be mostly on budget. The TGA will continue to review its fees and charges regularly to ensure they are aligned with revenue and costs as closely as possible for each sector. There is a need to provide for investments in updating ICT systems to ensure they meet regulatory needs. The TGA will consult with the industry before any changes are made.

32. The report noted providing certain fee-free services by the TGA is inconsistent with the CRGs. In accordance with the recommendation in the report, the department will seek a decision from the Government for relevant authority for these services.

33. The department continues to improve its stakeholder engagement on the TGA's cost recovery, including adjusting its consultative arrangements in response to stakeholder feedback and including the planned stakeholder strategy in the CRIS, as recommended in the report.

Department of Finance

34. Finance agrees with the findings of the Report and notes the relevance of the key learnings to Commonwealth entities. The findings will support continuous improvement by entities in effectively implementing the cost recovery principles.

Key messages from this audit for all Australian Government entities

35. Below is a summary of key messages from this audit that may be relevant for the operations of other Australian Government entities.

Policy/program implementation

- Transparency is key to cost recovery as it allows for consideration of industry views on regular cost recovery arrangements, major changes to these arrangements, any variations from requirements of the Cost Recovery Guidelines, and levels of over- and under-recovery over time. In this light, the Cost Recovery Implementation Statements of the Department of Health

were updated regularly and included disclosure on where its approach was not fully consistent with the Cost Recovery Guidelines.

- Cost recovery approaches should clearly apply the Cost Recovery Guidelines' principle of efficiency. Entities should benchmark key activities, understand trends in charges and prices over time (that can demonstrate efficiency improvements), otherwise identify where efficiencies can be achieved, and incorporate these elements in cost recovery models.

Audit findings

1. Background

Cost recovery

1.1 Cost recovery of Australian Government regulatory activities is defined as:

... the Australian Government charging the non-government sector some or all of the efficient costs of a specific government activity. That activity may include the provision of goods, services or regulation, or a combination of them.⁴

1.2 Cost recovery is one element of the Australian Government's Charging Framework, implemented in July 2015, to apply across the general government sector, to improve consistency of charging activities and help determine when it is appropriate to charge for a government activity. The policy underpinning the Charging Framework notes that cost recovery can:

- promote equity, whereby the recipients of a government activity, rather than the general public, bear its costs;
- influence demand for government activities;
- improve the efficiency, productivity and responsiveness of government activities and accountability for those activities; and
- increase cost consciousness for all stakeholders by increasing awareness of how much a government activity costs.⁵

1.3 Charging decisions are made by the Australian Government. Based on the type of activity, policy outcomes sought and relevant public interest considerations, the government may decide to charge for an activity, taking into account the following Charging Policy Statement:

Where specific demand for a government activity is created by identifiable individuals or groups they should be charged for it unless the Government has decided to fund that activity. Where it is appropriate for the Australian Government to participate in an activity, it should fully utilise and maintain public resources, through appropriate charging. The application of charging should not, however, adversely impact disadvantaged Australians.⁶

1.4 There are two types of cost recovery charges:

- cost recovery fees — fees charged when a good, service or regulation is provided directly to a specific individual or organisation; and
- cost recovery levies — charges imposed when a good, service or regulation is provided to a group of individuals or organisations (for example, an industry sector) rather than to a specific individual or organisation.

4 Department of Finance, *Australian Government Cost Recovery Guidelines*, Resource Management Guide No. 304, July 2014 — Third Edition, p. 1. Available from <https://www.finance.gov.au/resource-management/charging-framework/>, [accessed 14 January 2019].

5 Department of Finance, *Australian Government Cost Recovery Guidelines*, Resource Management Guide No. 304, July 2014 — Third Edition, p. 1, paragraph 3.

6 Department of Finance, *Australian Government Charging Framework*, Resource Management Guide No. 302, July 2015, p. 7.

1.5 Fees are charged for pre-market activities, such as the issue of licences, registrations, approvals and patents, while levies cover post-market activities, including monitoring and compliance, investigations and enforcement. Fees are to reflect the efficient unit cost of a specific good or service, while levies are to reflect the overall efficient costs of an activity.⁷ Generally, fee related activities are relatively easy to cost with a degree of precision, while levies are more difficult to estimate and are generally applied to an industry sector, and not to an individual.

1.6 Both fees and levies need statutory authority to charge (legislation), although levies also require a separate and specific taxation act. Cost recovery revenue from levies differs from general taxation as it funds activities provided to the group that pays the levy.

1.7 The Department of Finance has issued the *Australian Government Cost Recovery Guidelines* (Cost Recovery Guidelines) to support the implementation of the government's Charging Framework. The Cost Recovery Guidelines are a sub-set of the Charging Framework and must be applied by all non-corporate Commonwealth entities, and by corporate Commonwealth entities where the Finance Minister has made a 'government policy order' that applies the Australian Government cost recovery policy to them.⁸

1.8 Four stages are identified in the Cost Recovery Guidelines:

Stage 1: Australian Government policy approval to cost recover.

Stage 2: Cost recovery model and Cost Recovery Implementation Statement (CRIS).

Stage 3: Implementation.

Stage 4: Portfolio charging review.

1.9 The Cost Recovery Guidelines (paragraph 15) state that the following three principles must be applied across all stages of the cost recovery process: transparency and accountability; effectiveness and efficiency; and stakeholder engagement.

1.10 In 2017–18 reported revenue from regulatory charging in entity financial statements totalled \$2.0 billion against reported expenses of \$2.2 billion.

Cost recovery by the audited entities

1.11 This audit considers the application of cost recovery principles in the:

- Australian Maritime Safety Authority (AMSA);
- Department of Agriculture and Water Resources (Agriculture); and
- Department of Health (Health) for the Therapeutic Goods Administration (TGA).⁹

7 Department of Finance, *Australian Government Cost Recovery Guidelines*, Resource Management Guide No. 304, July 2014 — Third Edition, p. 3.

8 Department of Finance, *Australian Government Cost Recovery Guidelines*, paragraph 7, p. 4. The *Public Governance, Performance and Accountability (Charging for Regulatory Activities) Order 2017* requires all the agencies listed in the Order Schedule to apply approved regulatory charging.

9 Agriculture and Health are non-corporate Commonwealth entities and have a legislative responsibility under Section 21 of the *Public Governance, Performance and Accountability Act 2013* to adhere to the Cost Recovery Guidelines. The Minister for Finance has made a government policy order that applies the cost recovery policy to AMSA.

1.12 In 2017–18, the revenue raised from the cost recovery activities covered in this audit for these three agencies was approximately \$372 million — AMSA \$128 million, Agriculture \$91 million and Health \$153 million.

Australian Maritime Safety Authority

1.13 AMSA was established under the *Australian Maritime Safety Authority Act 1990* as the national regulatory authority to:

- promote maritime safety and protection of the marine environment;
- prevent and combat ship-sourced pollution in the marine environment;
- provide infrastructure to support safe navigation in Australian waters;
- provide a national search and rescue service to the maritime and aviation sectors; and
- provide, on request, services of a maritime nature on a commercial basis to the Commonwealth and/or states and territories.

1.14 AMSA has been recovering costs for ship and seafarer safety, environmental protection and navigation infrastructure since its inception in 1990. These costs are recovered through:

- the Marine Navigation (Regulatory Functions) Levy for the provision of maritime safety and regulatory activities on international and national commercial shipping operations;
- the Protection of the Sea Levy to prevent and combat ship-sourced pollution;
- the Marine Navigation Levy to develop and maintain aids to coastal navigation; and
- fees for marine services, including services to seafarers and coastal pilots, such as issuing seagoing qualifications, inspections and surveys and ship registrations.¹⁰

1.15 AMSA also now collects fees for service for marine surveyor accreditation, issuing exemptions and ‘equivalent means of compliance’¹¹ to the domestic commercial vessel fleet under the National System for Domestic Commercial Vessel Safety (National System).¹² This is outside the scope of this audit.

10 AMSA, *Cost Recovery Implementation Statement — Provision of infrastructure to support safe navigation in Australian waters, environmental marine protection, seafarer and ship safety, and marine services 2018–19*, pp. 2–3.

11 An equivalent means of compliance is an alternative way of achieving a safety outcome. It must be at least as effective as the usual solution of meeting the relevant required outcomes or requirements. See <https://www.amsa.gov.au/vessels-operators/domestic-commercial-vessels/equivalent-means-compliance>, [accessed 27 September 2018].

12 *Marine Safety (Domestic Commercial Vessel) National Law Act 2012* and regulations. The National System replaced the state and territory regulatory arrangements and is being phased in over a 10-year period from 1 July 2018. On 2 July 2018, the Deputy Prime Minister announced that, in implementing the National System for Domestic Commercial Vessel Safety from 1 July 2018, the Government had agreed to provide an additional \$10 million funding, increasing the Federal Government’s total contribution to \$65 million over ten years, and increasing total funding by all governments to \$112.4 million. As a result, no levy will be charged to industry for the first three years of AMSA’s service delivery.

Department of Agriculture and Water Resources

1.16 The audit examined Agriculture's food export certification activities, which occur across four cost recovery arrangements — meat exports, dairy exports, fish and egg exports and non-prescribed goods.¹³ The department commenced partial cost recovery of export certification activities in 1979 and implemented full cost recovery from 1 January 1991.¹⁴

1.17 To certify a product's compliance with relevant Australian regulations and the importing country's requirements, the department undertakes a range of activities that are cost recovered, including the:

- development, implementation and monitoring of operational policy and systems that support compliance with Australian export controls and any additional importing country requirements that maintain access to export markets for Australian agricultural food products;
- provision of inspection and auditing activities to ensure that the production, storage, handling and transportation of meat, dairy, fish and egg and non-prescribed goods intended for export comply with the conditions of the Australian export controls and any additional requirements imposed by an importing country;
- issue of permits, health certification and other documentation necessary to confirm compliance with Export Control Orders and any additional importing country requirements; and
- management of quota allocation and quota certification to enable exporters to access tariff rate concessions offered under trade agreements.

Department of Health (Therapeutic Goods Administration)

1.18 The TGA is Australia's regulatory authority for therapeutic goods.¹⁵ Industry sectors to which cost recovery applies are: prescription medicines; over-the-counter medicines; complementary medicines; medical devices including in-vitro diagnostic devices; and blood, blood products and biologicals. Cost recovery activities include:

- pre-market assessment of medicines and devices for inclusion in the Australian Register of Therapeutic Goods;
- post-market monitoring and enforcement of standards; and

13 Details of Agriculture's cost recovery of food export certification activities are provided in Department of Agriculture and Water Resources, *Cost Recovery Implementation Statement — Food Exports Certification, 2015–16*.

Non-prescribed goods are specific goods that are derived from animals and plants which for export certification purposes do not fall under the category of prescribed goods as outlined in relevant legislation. Examples include animal by-products, wool, skins and hides (Cost Recovery Implementation Statement, p. 3).

14 Department of Agriculture and Water Resources, *Cost Recovery Implementation Statement Food Exports Certification, 2015–16*, p. 3.

15 Therapeutic goods comprise prescription medicines, vaccines, sunscreens, vitamins and minerals, medical devices, biologicals, blood and blood products. TGA, *TGA Cost Allocation Methodology, v 1.2*, April 2017, p. 5.

- licensing of Australian manufacturers and verifying overseas manufacturers' compliance with Australian standards.¹⁶

1.19 The costs of regulatory activity within the scope of the *Therapeutic Goods Act 1989* have been fully cost recovered since 1999. Most of Health's funding for the TGA (\$153.0 of \$155.3 million for 2017–18)¹⁷ is from cost recovery. Legislative authority for TGA fees and charges is through the *Therapeutic Goods (Charges) Act 1989*.

Rationale for undertaking the audit

1.20 The government charges people and businesses to recover the costs of providing some services. In auditing cost recovery in the selected entities, the Australian National Audit Office (ANAO) examined whether the Cost Recovery Guidelines were applied effectively, so that charges were set to not over- or under-recover costs, and stakeholders were engaged in the processes for setting charges.

Audit approach

Audit objective, criteria and scope

1.21 The objective of the audit was to assess whether selected regulatory entities effectively apply the cost recovery principles of the Australian Government's cost recovery framework.

1.22 Reflecting these principles, the audit criteria were:

- Are the entities' cost recovery arrangements transparent and do they promote accountability?
- Are the entities' cost recovery arrangements effective and efficient?
- Have the entities engaged stakeholders effectively in the design, planning and implementation of their cost recovery programs?

1.23 The scope of the audit was the application of the cost recovery principles for: AMSA's four levies or fees outlined in paragraph 1.14 (domestic commercial vessel fleet activities are outside the scope of the audit); Agriculture's food export certification activities; and Health's cost recovery activities for the TGA. The Department of Finance was also included in the audit in light of its responsibilities for developing and promulgating the Australian Government's Charging Framework, including the Cost Recovery Guidelines.

Audit methodology

1.24 The audit method comprised: document collection from each of the three audited entities; interviews with entity staff; interviews with staff of the Department of Finance; and analysis of the information collected during the audit.

16 TGA, *Cost Recovery Implementation Statement*, Version 1.6, February 2019, p. 5.

17 TGA, *Cost Recovery Implementation Statement*, Version 1.6, February 2019, p. 38.

1.25 The audit was conducted in accordance with the ANAO Auditing Standards at a cost to the ANAO of approximately \$560,000. The team members for this audit were John McWilliam, Renina Boyd, Nathan Callaway, Lachlan Fraser, Gabrielle Davy, Esther Barnes and Andrew Morris.

2. Are the entities' cost recovery arrangements transparent and do they promote accountability?

Areas examined

This chapter examines whether the cost recovery arrangements of AMSA, Agriculture and Health were transparent and promoted accountability.

Conclusion

Each entity has scope to improve the transparency and accountability of its cost recovery arrangements, mainly through more current and/or comprehensive reporting of performance in Cost Recovery Implementation Statements. Otherwise, the governance and internal accountability arrangements of the three entities are fit for purpose.

Areas for improvement

The chapter has two recommendations aimed at: the three audited entities improving compliance with the Cost Recovery Guidelines (paragraph 2.41); and the Department of Finance supporting higher levels of compliance more broadly and refining the Cost Recovery Guidelines where appropriate (paragraph 2.48).

Have entities complied with key requirements of the Cost Recovery Guidelines?

AMSA, Agriculture and Health have not fully complied with key requirements of the Cost Recovery Guidelines, particularly those relating to Cost Recovery Implementation Statements, with Agriculture and AMSA not updating these at least annually as required. Each entity has policy approval to charge for its regulatory activities and services and has legislative authority to charge, although Health has ministerial, not government policy approval, to meet the cost of fee-free activities through higher charges on other users. The Department of Finance should refine the Cost Recovery Guidelines to provide greater clarity on some requirements and take steps to promote greater levels of compliance with the Guidelines.

2.1 Entities are required to comply with key requirements of the cost recovery framework and Cost Recovery Guidelines.¹⁸ These requirements include that:

- entities and responsible ministers must have policy approval from the Australian Government to cost recover (paragraph 33);
- there must be a statutory authority to charge (paragraph 34);
- entities must undertake a risk assessment and agree on a risk rating with the Department of Finance (paragraph 60); and
- entities must document each cost recovered regulatory activity in a Cost Recovery Implementation Statement (CRIS) before charging begins (paragraph 39).

18 The Cost Recovery Guidelines state that they 'must' be applied by relevant entities (paragraph 7). However, the Guidelines distinguish between mandatory requirements (entities 'must') and better practices (entities 'should').

Policy approval

2.2 Policy approval for the three entities' charging policies and changes to them are summarised in their CRISs. As shown in Table 2.1, AMSA and Agriculture had policy approvals for the cost recovery activities examined. Health had the required policy approvals for Therapeutic Goods Administration (TGA) charges, except for fee-free services where there was ministerial approval rather than the required government approval.

Table 2.1: Policy approval of cost recovery in the three entities

Australian Maritime Safety Authority
<p>In establishing AMSA under the <i>Australian Maritime Safety Authority Act 1990</i>, the explanatory memorandum for the Australian Maritime Safety Authority Bill 1990 stated that 'the Government intends that the Authority will run its commercial services on a self-funded basis; services which cannot be provided on a self-funded basis (such as search and rescue) will be paid for by the Commonwealth', and AMSA would receive the revenue from the Marine Navigation Levy and the Protection of the Sea Levy (clause 48). The explanatory memorandum for the Marine Navigation (Regulatory Functions) Levy Bill 1991 also stated that the purpose of the bill was to give effect to the government's decision, announced on 21 August 1990, to recover the costs of maritime safety and regulatory functions from commercial shipping. In 2011, the government approved the Australian International Shipping Register to encourage Australian participation in the international shipping trade to be regulated by AMSA on a cost recovery basis. AMSA's charges were last amended in 2015.¹</p>
Department of Agriculture and Water Resources
<p>Agriculture commenced partial cost recovery of export certification activities in 1979 and implemented full cost recovery from 1 January 1991 (although costs were not fully recovered for Australian Quarantine Inspection Service activities until 2015). Most recently, policy authority for cost recovery of continued export certification was confirmed in the 2015–16 Budget, when the government approved and announced a redesign of the department's biosecurity and export cost recovery arrangements.</p>
Therapeutic Goods Administration
<p>The 1997–98 Budget, Budget Paper No. 2, Part II: Revenue Measures stated that the TGA would fully recover all costs from industry from 1998–99.</p> <p>Health has obtained ministerial approval to increases in charges, including those resulting from implementation of the government's Medicines and Medical Devices Review reforms, aimed at improving access to therapeutic goods for consumers and reducing red-tape for industry.</p> <p>Following a Portfolio Charging Review in 2017 (see Table 3.1 and paragraph 3.39), Health obtained ministerial approval, but not the required government policy approval, to meet the cost of fee-free services indirectly from other charges.</p>

Note 1: Although outside the scope of this audit, AMSA obtained policy approval for fees related to the new National System for Domestic Commercial Vessel Safety, for which it assumed full responsibility on 1 July 2018.

Source: Entity CRISs.

2.3 Paragraph 33 of the Cost Recovery Guidelines requires entities and responsible ministers to obtain government approval for a new cost recovery 'model' or significant changes to a cost recovery 'model'.¹⁹ The Department of Finance (Finance) advised that the intention of this requirement is that entities and responsible ministers obtain government approval on how costs

19 Figure 3 of the Guidelines (p. 19) states that entities are expected to develop a 'high level' cost recovery model in Stage 1 and a detailed cost recovery model in Stage 2. The reference to a 'high level' cost recovery model in Stage 1 appears to be to the type of cost recovery arrangements to be applied, whereas the detailed cost recovery model in Stage 2 is to the tool to be used to measure and account for costs and revenues and determine the prices to be set.

are to be recovered — through levies or fees — and the legislative authority to be provided, rather than on the details of the cost recovery model used to determine the appropriateness of amounts that are charged. Finance also advised that policy approval is only required where changes to charges are either material, sensitive or complex and that the responsible minister or accountable authority can approve changes of an operational nature. To avoid ambiguity, Finance should clarify the use of the term ‘model’ in this context in any future review and revision of the Cost Recovery Guidelines.

Statutory authority to charge

2.4 Each entity’s cost recovery charges (levies and fees described at paragraph 1.4) have a statutory basis and are underpinned by specific legislation or legislative instruments.

Risk assessments of cost recovery activities

2.5 Each entity completed Finance’s risk assessment template for charging for regulatory activities, and rated their cost recovery risks as ‘medium’. AMSA and Agriculture last updated their risk assessments in 2015. Health last updated the TGA’s risk assessment in 2016. As required, AMSA’s and Agriculture’s ratings were agreed with Finance. Health’s risk assessment for the TGA in 2016 was provided to Finance as part of the proposed Budget measures, although Health did not obtain Finance’s agreement to the rating.

2.6 There have been changes to the TGA’s charges since 2016 resulting from implementation of recommendations of the Medicines and Medical Devices Review, but Health has not completed a further risk assessment of the impact of these changes.²⁰ AMSA and Agriculture have not reviewed their risk ratings since charges were last changed in 2015. It is important that arrangements are in place to provide assurance that the risk assessment of charging arrangements remains appropriate, even where there are no changes to charges.

2.7 To provide the necessary assurance that the risk assessment of an entity’s charging arrangements remains appropriate, the Cost Recovery Guidelines could require entities to review the continuing suitability of the risk assessments of their cost recovery arrangements at set minimum periods or whenever significant changes are made to the cost recovery arrangements.

Cost Recovery Implementation Statements

2.8 The CRIS is the primary document for explaining an entity’s cost recovery charging policies and providing key information on the implementation and performance of cost recovery activities. The Cost Recovery Guidelines require that:

20 The Government announced a review by an expert panel of Medicines and Medical Devices Regulation in October 2014. The review examined Australia’s medicines and medical devices regulatory framework and processes with a view to identifying:

- areas of unnecessary, duplicative, or ineffective regulation that could be removed or streamlined without undermining the safety or quality of therapeutic goods available in Australia; and
- opportunities to enhance the regulatory framework so that Australia continues to be well positioned to respond effectively to global trends in the development, manufacture, marketing and regulation of therapeutic goods.

See <http://www.health.gov.au/internet/main/publishing.nsf/Content/Expert-Review-of-Medicines-and-Medical-Devices-Regulation> [accessed 13 March 2019].

- each cost recovered regulatory activity, regardless of financial value, must be documented in a CRIS before charges commence (paragraph 39);
- the CRIS must be published on the entity's website before charging begins (paragraph 40);
- the CRIS is updated, in consultation with stakeholders, at the commencement of each financial year and, as necessary, throughout the year to reflect any changes in the cost recovery model and updated financial and non-financial performance information (paragraphs 40, 124 and 125);
- the CRIS provides information on 11 separate criteria (paragraphs 41 and 104); and
- the CRIS is certified by the accountable authority of the entity; approved by the responsible Minister; and agreed for release by the Minister for Finance if the cost recovery risk rating is 'high' (paragraphs 42 and 105).

2.9 The Australian National Audit Office (ANAO) has assessed the CRISs of all three entities as not fully compliant with the Cost Recovery Guidelines (see Table 2.2).

Table 2.2: Assessment of entity Cost Recovery Implementation Statements against the Cost Recovery Guidelines

CRIS criterion	AMSA	Agriculture	TGA
Each cost recovered activity, regardless of financial value, must be documented in a CRIS before charges commence.	◆	◆	◆
A CRIS is published at the commencement of each financial year and updated progressively throughout the year.	▲	■	◆
Background information on the cost recovered activity, including its purpose, policy outcomes and outputs and description of the activity and the stakeholders who pay charges or may be affected by the charges.	◆	◆	◆
Details of the Australian Government policy approval to cost recover the activity.	◆	◆	▲
Details of the legislation authorising the cost recovery charges, including links to primary and secondary legislation.	◆	◆	◆
An explanation of the costing model for the activity — a description of how the model has been broken into outputs and processes and how these have been costed, including cost drivers and assumptions.	▲	▲	◆
An explanation of the design of cost recovery charges — which types of charges have been used and why, including their link to the outputs and processes of the activity.	◆	◆	◆
The cost recovery risk assessment (CRRR) rating — the result of the assessment and factors contributing to the rating.	◆	◆	◆
A stakeholder engagement strategy, including a summary of the latest engagement round — who was consulted and when, what their views were and how those views have been considered.	▲	◆	◆
Financial estimate for the activity (i.e. expenses and revenue) for the budget year and forward estimates.	▲	▲	▲
Reporting on the financial and non-financial performance of the activity.	▲	■	◆

CRIS criterion	AMSA	Agriculture	TGA
Key forward dates and events, including the next portfolio charging review.	▲	■	◆
The CRIS is certified by the accountable authority of the entity, approved by the responsible Minister, agreed for release by the Finance Minister if the cost recovery risk rating is 'high', and published on the responsible entity's website before charging begins.	◆	◆	▲

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: ANAO assessment of entity CRISs for activities within the scope of the audit against the mandatory criteria for CRISs in the Department of Finance's Cost Recovery Guidelines (paragraphs 40, 41, 104, 105, 124 and 125). The assessment is based on relevant CRISs published since 2015–16, but with particular focus on the most recently available CRIS for each entity.

2.10 The main areas of the CRISs' non-compliance with the Cost Recovery Guidelines were:

- performance reporting: in part, because of a failure to update the CRIS at least annually to include reports on performance — see section starting at paragraph 2.18;
- updates to estimates and the underlying methodology used to determine these estimates — again partly due to a failure to update the CRIS at least annually; and
- key forward dates: the key forward dates envisaged in the Cost Recovery Guidelines are not always being shown in the CRIS.

2.11 AMSA and Agriculture have not always updated their CRISs at the start of each financial year for the budget year and forward estimates period (and as necessary throughout the budget year), as required by the Cost Recovery Guidelines (paragraphs 124 and 125). AMSA did not update its CRIS in 2017–18, while Agriculture last updated its CRIS in 2015–16. Health has updated its TGA-related CRIS regularly, but has not always provided estimates for the four forward years.

2.12 Both AMSA and Agriculture questioned the need to update their CRISs each year, as no changes in charges were proposed. Agriculture advised that it sets CRISs on a four-year cycle and there have been no changes to legislated prices over this period. Agriculture also noted that it had delayed updating its CRIS because of continuing work requested by its Minister on proposed changes to charges since 2015–16. For example, Agriculture proposed to its Minister that it would issue a CRIS as a basis for consulting with industry on revised charges in 2018–19, but the Minister for Agriculture instead deferred this to enable detailed consultation with industry and implementation of the changes in 2019–20. However, as explained at paragraphs 124 to 126 of the Cost Recovery Guidelines, updates to a CRIS are needed not just to explain changes in charges, but to provide performance information and updated estimates of revenues and expenses for each forward estimates period.

2.13 The ANAO notes that, while paragraphs 124 and 125 of the Cost Recovery Guidelines clearly state the CRIS should be updated at the commencement of each budget year for the budget year and forward estimates period, paragraph 40 only states that an initially-approved CRIS 'should be amended to reflect any changes to the cost recovery model and updated regularly with financial and non-financial performance information'. This difference in wording should be amended to avoid possible misunderstandings about the timing of updates to the CRIS.

2.14 Health questioned the need to obtain ministerial approval to updates of a CRIS where there has been no significant change to the entity's cost recovery policy and the minister has separately approved any changes in charges.

Role of the Department of Finance

2.15 Finance advised the ANAO that it is aware that many entities do not update their CRISs, as required, although it does not systematically take this up with them. While it is the responsibility of entities to comply with the Guidelines, Finance has a role in promoting compliance with the Guidelines, given its policy responsibility. To help promote compliance with the Guidelines, Finance should advise entities at the start of each budget cycle (for example, in the annual Budget circular) of their responsibility to update their CRISs. In doing so, it could also remind entities of the level of information to include in the CRIS.

2.16 Finance should also update and refine the Cost Recovery Guidelines to remove ambiguities and help promote compliance with them, including through addressing issues raised in this report (see Appendix 2).

2.17 Finance conducts a biennial survey of charging by entities to provide data on trends and opportunities and reports to the government on key issues.²¹ This survey provides an opportunity for Finance to collect information on issues entities have in complying with the Cost Recovery Guidelines and identify where the Guidelines could be refined to enable greater compliance.

Have entities reported on performance on an ongoing basis?

The three entities have reported on cost recovery performance principally through their Cost Recovery Implementation Statements and annual reports. However, Agriculture and AMSA have not updated their Cost Recovery Implementation Statements annually to include actual and updated financial data. Agriculture's last Cost Recovery Implementation Statement and accompanying report on performance was in 2015–16 and AMSA did not publish a Cost Recovery Implementation Statement for 2017–18. There is scope for each entity to improve the level of information on cost recovery performance included in their Cost Recovery Implementation Statements and annual reports.

2.18 A key part of achieving transparent cost recovery arrangements under the Cost Recovery Guidelines (paragraph 27) involves ongoing and timely performance (financial and non-financial) reporting. This includes (paragraph 123) that an entity must report on cost recovery:

- at an aggregate level in the entity's annual financial statements, in accordance with the financial reporting rules; and
- at the cost-recovered activity level on the entity's website as part of the CRIS.

2.19 As discussed in paragraph 2.12 of this report, paragraphs 124 and 125 of the Guidelines require entities to update the CRIS at the commencement of each budget year (and throughout the

21 The 2017 survey focused on entities in the general government sector, with 138 non-corporate and corporate Commonwealth entities in scope.

year as required), although paragraph 40 is not consistent with other paragraphs. The ANAO's analysis is based on the guidance at paragraphs 124 and 125.

2.20 The ANAO's assessment of the entities' cost recovery performance reporting is presented in Table 2.3. The assessment indicates scope for improvement in the level of information on cost recovery performance included in CRISs and annual reports, including by:

- reporting on performance annually at the activity level;
- developing metrics for cost recovery financial performance — each of the three entities provided historical performance of their cost recovered activities, but did not have metrics on balancing revenue and expenses for their activities over nominated timeframes and managing reserves; and
- providing explanations of factors affecting performance, including changes in costing methodologies.

Table 2.3: Performance reporting on cost recovery activities, 2015–16 to 2018–19

Reporting element	AMSA	Agriculture	TGA
Financial performance reporting	▲	▲	◆
Non-financial performance reporting	▲	▲	◆

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: ANAO analysis of entity cost recovery and performance reporting documentation.

Australian Maritime Safety Authority

2.21 AMSA's CRISs from 2015–16 have included financial and non-financial performance information as required by the Cost Recovery Guidelines, and have been published on its website. The section on financial performance in AMSA's most recent CRIS for 2018–19²² included information and reporting on expenses, revenue and the balance of these. Reporting was provided on actuals for five financial years (2013–14 to 2017–18) and estimates for two financial years (2018–19 and 2019–20). It did not include estimates for the four forward years because of uncertainty about the impact of the National System (see paragraph 1.15) after 2019–20. This section also explained how surpluses were used. However, AMSA's:

- CRISs have not provided disaggregated historical financial performance information at the regulatory activity level (that is, by levy type and for fees-for-service — they have only provided consolidated financial information for all cost recovered activities) — so that it is not possible to see how well distinct charging activities have been performing; and
- failure to publish a CRIS in 2017–18 meant that there was a delay in the release of financial performance information for 2016–17.

22 Australian Maritime Safety Authority, *Cost Recovery Implementation Statement: Provision of infrastructure to support safe navigation in Australian waters, environmental marine protection, seafarer and ship safety, marine services, 2018–19*, pp. 18–19. AMSA also published a CRIS for the National System for Domestic Commercial Vessel Safety in June 2018. The National System is not within the scope of this audit.

2.22 AMSA's CRISs have included non-financial performance measures with reports on performance against these measures provided in AMSA's annual reports, not in the CRIS. In its 2017–18 annual report, AMSA reported that it fully met five of its performance targets and partially met the remaining three.

Department of Agriculture and Water Resources

2.23 Agriculture's most recent CRIS (published in 2015–16) for the food export program is available on its website and includes performance information.²³ As required by the Cost Recovery Guidelines, the CRIS contains financial and non-financial performance information including:

- financial performance information and reporting on actual expenses, revenue and the balance of these for 2011–12 to 2014–15; and
- two non-financial performance measures against the four export types.²⁴

2.24 As noted at paragraph 2.12, over the past four financial years, Agriculture has not updated its CRIS annually, as required by the Cost Recovery Guidelines, despite the 2014–15 CRIS indicating that financial reporting for 2015–16, 2016–17 and 2017–18 would be updated in 2016, 2017 and 2018, respectively. While Agriculture has not updated its CRIS, it has regularly consulted industry on cost recovery issues through consultative committees (see Chapter 4).

2.25 Agriculture has reported against the two (non-financial) performance measures in its 2015–16 CRIS in its annual reports. In its 2017–18 annual report, Agriculture reported that it met both of its performance targets in 2017–18.

Therapeutic Goods Administration

2.26 Health makes the TGA's CRIS publicly available on the TGA website and, since 2015–16, these have been updated at least annually, and sometimes more frequently. The most recent CRIS for the TGA (February 2019, covering 2018–19) includes financial and non-financial performance information for its regulatory activities.²⁵ However, this CRIS provided reports on actual revenue and expenses for only three years — 2015–16 to 2017–18 (Health has indicated that in future it will provide this information for five years) — and financial estimates were included for only two forward years 2018–19 and 2019–20 (unlike CRISs for earlier years, which included estimates for all forward years).

2.27 The section on non-financial performance in the TGA's CRIS includes six performance indicators, which are the key performance indicators from the Australian Government's Regulator Performance Framework. Health publicly reports against these six performance indicators in an annual self-assessment report against the Regulator Performance Framework. The most recent

23 Department of Agriculture and Water Resources, *Cost Recovery Implementation Statement, Food exports certification, 2015–16*.

24 The four export types are meat exports, dairy exports, fish and egg exports, and non-prescribed goods.

25 Therapeutic Goods Administration, *Cost Recovery Implementation Statement, Version 1.6* (February 2019). The financial information included estimates for 2018–19 and 2019–20. Earlier versions of the CRIS for 2018–19 only included an estimate for 2017–18 and did not include estimates for 2018–19 and 2019–20.

report was for 2017–18.²⁶ Health reported that it achieved (met or substantially met) all of its non-financial performance targets for the TGA in 2017–18.

2.28 The ANAO notes that the Regulator Performance Framework performance indicators focus on broad aspects and impacts of regulation (such as reducing regulatory burden, transparency and continuous improvement) but not on the performance of individual activities. The Cost Recovery Guidelines state that achieving transparency in cost recovery activities involves reporting performance at the regulatory activity level (paragraph 27). Accordingly, Health could provide specific non-financial performance indicators for the TGA’s cost recovery activities to supplement or replace the Regulator Performance Framework performance indicators. This view is consistent with that of a review that Health commissioned of the TGA’s cost recovery arrangements in November 2016, which recommended that the ‘TGA should provide additional information in its CRIS to document the performance of individual activities’.

Have entities implemented effective governance and accountability arrangements?

Each entity has established effective cost recovery governance and accountability arrangements. The arrangements include an internal management committee to oversee cost recovery activities and provide guidance to staff on implementation of cost recovery policies, and reporting to the committee and entity executive board on cost recovery performance.

2.29 Under the Cost Recovery Guidelines, entities are expected to manage the implementation and operation of cost-recovered activities consistent with Australian Government policy approval, relevant legislation, the Cost Recovery Guidelines and the broader resource management framework (paragraph 108). This includes having arrangements in place to monitor and report on the production of the outputs of the regulatory activity against financial estimates and performance targets and identifying the need for, and timely implementation of, operational or policy changes.

Australian Maritime Safety Authority

2.30 AMSA commissioned a review of its cost recovery framework, which reported in 2018. This review found that AMSA lacked internal documentation that specifically outlines its cost recovery process and procedures and had incomplete documentation to support cost recovery decisions, stakeholder engagement and the cost recovery model, as required by the Cost Recovery Guidelines. The review also identified changes that were needed to AMSA’s cost model. Following this review, AMSA has redeveloped its cost recovery model and data collection arrangements to improve the allocation of costs to activities and outputs. It has also prepared a draft Cost Recovery Policy statement. AMSA has not yet documented its cost recovery systems and procedures, but advised the ANAO that, after further refinement of its cost recovery model and data collection arrangements, it plans to do so by 30 June 2019.

2.31 AMSA’s Finance and Business Services Directorate in the Corporate Services Division manages the authority’s cost recovery operations, in consultation with other divisions. In March

26 Therapeutic Goods Administration, *Regulator Performance Framework — Self-assessment Report July 2017 to June 2018*.

2018, to enable the views of divisions to be considered in the redevelopment and implementation of its costing approach, AMSA established an internal Cost Recovery Consultative Committee, which includes representatives from each division.

2.32 Internally, regular financial and non-financial performance reports are provided to the AMSA Executive and AMSA Board. Other than in relation to cost recovery for the National System, AMSA advised that the CRISs and the annual report are the only documentation provided to the Portfolio and Minister on cost recovery outcomes. While the implementation of the AMSA Cost Recovery Consultative Committee is a sound initiative, AMSA has not actively managed the alignment of expenses and revenues (see paragraphs 3.25 to 3.29).

2.33 To help ensure that charges are implemented efficiently, AMSA has been working with Marine Operations Division staff to increase their awareness and understanding of the cost recovery arrangements and provide accurate attribution of their time to levy-based and fee-based activities. It is also planning to provide feedback to operational staff on the results of cost recovered activities to promote more active involvement in the outcomes being achieved.

Department of Agriculture and Water Resources

2.34 Agriculture's Industry Support Branch in the Finance and Business Support Division manages the department's cost recovery activities. It is responsible for oversight of overall cost recovery performance and maintenance of Agriculture's cost recovery model. The branch has a team of 11 staff dedicated to the management of cost recovery.

2.35 Agriculture established a Cost Recovery Board in 2016 to oversee its cost recovery activities. This Board includes representatives of relevant divisions and meets quarterly (initially it generally met monthly). At each meeting, it monitors cost recovery performance across the department. The Agriculture Executive Management Committee is also briefed on cost recovery policy issues, such as the findings and recommendations of a 2017 Cost Recovery Revenue Taskforce, and on cost recovery performance through monthly reports from the Chief Finance Officer.

2.36 In 2016, Agriculture prepared a cost recovery policy statement. In 2017, Agriculture prepared a high-level cost recovery allocation policy statement for staff, which provides policy guidance for cost allocation in the department to ensure efficient and effective business planning, control and accountability. Other guidance for staff is provided, for example, on use of the activity recognition tool.

2.37 Agriculture established a team in 2014 to review its cost recovery arrangements at the time and has adopted a similar approach to a current review of its cost recovery arrangements.

Therapeutic Goods Administration

2.38 In response to a recommendation of Health's 2016–17 portfolio charging review, in May 2018 Health established a unit in its Financial Management Division to:

- be the policy owner of charging for the department;
- provide guidance and advice on charging to those areas of the department, such as the TGA, that cost recover some or all of the cost of their operations;
- maintain a central register of all charging activities across the portfolio;

- work across the portfolio to ensure CRISs are reviewed and updated annually and completed to a consistent standard; and
- ensure that, where possible, a consistent costing model is used for charging activities across the portfolio and that costing models for charging activities are robust enough to estimate both direct and indirect costs.

2.39 There is a small team in Health's Regulatory Practice and Support Division that manages the TGA's cost recovery activities, with the support of staff from the department's Financial Management Division.

2.40 Oversight of the department's cost recovery activities is provided by the Health Products Regulation Group Executive, to which reports are provided. Health also established an internal committee — the Expert Review Implementation Committee — to oversee the implementation of the government's Medicines and Medical Devices Review reforms (referred to in Table 2.1). The Health Minister is briefed at least annually on the department's cost recovery performance and on possible changes to its charging arrangements.

Recommendations

Recommendation no.1

2.41 The Australian Maritime Safety Authority, Department of Agriculture and Water Resources and Department of Health:

- (a) ensure that their Cost Recovery Implementation Statements are fully compliant with the Cost Recovery Guidelines, including in relation to required updates; and
- (b) report annually in their Cost Recovery Implementation Statements on their cost recovery performance at the regulatory activity level.

Australian Maritime Safety Authority: Agreed.

2.42 AMSA's responses to each sub-recommendation are:

- (a) *AMSA is working on putting into place procedures to strengthen its cost recovery compliance processes.*
In relation to the non-publishing of the 2017–18 CRIS, the delay in publishing was due to the focus on the introduction of domestic commercial vessel (National System) activities and the work related to establishing an Activity Based Costing system across the combined domestic and international infrastructure platforms.
- (b) *AMSA will review the current processes and will put into place a methodology to breakdown costs for individual charging activities, subject to materiality.*

Department of Agriculture and Water Resources: Agreed.

2.43 *The department agrees with Recommendation 1.*

2.44 *As the ANAO notes in the report, the department has had a process during 2017 and 2018 to review existing cost recovery arrangements and update the existing CRISs.*

2.45 *The department will continue to work closely with the Department of Finance to maintain continued compliance with the whole of government charging framework, including the Cost Recovery Guidelines.*

2.46 *The department will also continue to refine its regular reporting arrangements to optimise effective reporting on cost recovery outcomes.*

Department of Health: Agreed.

2.47 *The ANAO noted the TGA's Cost Recovery Implementation Statements (CRIS) had been updated regularly, at least annually, as required by the Cost Recovery Guidelines. The TGA is also taking steps, in updating their CRIS, to include further information on performance at the regulatory activity level.*

Recommendation no.2

2.48 The Department of Finance:

- (a) advises entities at the start of each budget year of their obligation to update their Cost Recovery Implementation Statements;
- (b) reviews and refines the Cost Recovery Guidelines to address issues listed at Appendix 2 of this audit; and
- (c) explores additional mechanisms to improve entities' compliance with the Cost Recovery Guidelines, including through the biennial charging survey.

Department of Finance: Agreed.

2.49 *Finance agrees with Recommendation 2, which is being implemented as part of Finance's ongoing work to strengthen guidance in relation to charging across the Commonwealth.*

2.50 *Finance will continue to utilise budget processes and the biennial charging survey to support entities in complying with their requirements.*

3. Are the entities' cost recovery arrangements effective and efficient?

Areas examined

This chapter examines the effectiveness and efficiency of the entities' cost recovery arrangements.

Conclusion

Each entity has scope to improve the effectiveness of its cost recovery arrangements. AMSA and Health have significantly over-recovered costs in recent years. Agriculture has over-recovered costs through levies and under-recovered costs through fees. There is no assurance that entity charges recover the efficient costs of their activities, although Agriculture has benchmarked some of its costs. Entities' cost recovery policies and cost recovery methodologies are at varying levels of being fit for purpose, with Health's approach for the TGA the most complete.

Areas for improvement

This chapter has three recommendations aimed separately at the three entities to improve aspects of cost recovery arrangements, including aligning revenues and expenses of outputs in cost recovery models, and adjusting charges to reduce cross-subsidisation across industry sectors (paragraphs 3.61, 3.63 and 3.68).

Do cost recovery charges recover the full costs, or agreed partial costs, of the regulatory activity?

There has been significant misalignment between revenue and expenses for AMSA and the TGA, with the costs of some activities being consistently over-recovered and others consistently under-recovered. Overall, Agriculture has had a proportionately small under-recovery on its cost-recovered activities.

AMSA and Health need to be more proactive in addressing structural over- and under-recovery of the costs of their activities. AMSA and Agriculture have reviewed their cost recovery legislated charges every four to five years. While this provides certainty to industry and the entities, charges should be reviewed and adjusted more frequently where there are structural misalignments in expenses and revenues for cost-recovered activities.

AMSA does not recover the full cost of its fee-based activities, and funds the shortfall from levy-based revenue. If it is not feasible to recover the full costs of these activities, AMSA should seek the government's approval of the partial recovery, and how the shortfall is to be met, with disclosure of any cross-subsidies included in its Cost Recovery Implementation Statements. AMSA should also examine suitable proxies for its levy-based charges in its review of charges related to the introduction of the National System.

Agriculture recovers the costs of activities provided to specific individuals or organisations through a combination of fees and levies, rather than recovering their full cost through fees, as required by the Cost Recovery Guidelines. Agriculture should use the current review of its charging arrangements to align the structure of its fees and charges with the requirements of the Cost Recovery Guidelines.

Portfolio charging reviews

3.1 Under the Cost Recovery Guidelines, departments of state are required to review all charging activities within their portfolios at least every five years, in consultation with the portfolio entities and the Department of Finance (paragraphs 17 and 44). Review reports must be submitted to the responsible minister and copied to the Finance Minister (paragraph 47); they are not published. Any significant policy recommendations must be approved by the government and documented before changes to cost recovery arrangements are implemented.

3.2 Portfolio charging reviews were completed for the Department of Infrastructure, Regional Development and Cities (including AMSA) in 2015 and for the Department of Health (including the TGA) in 2017, and the outcomes of these reviews are shown in Table 3.1. A portfolio charging review is being undertaken for Agriculture and expected to be completed in 2019. The timing of this review is consistent with the schedule of portfolio charging reviews issued by the Department of Finance.

Table 3.1: Outcomes of portfolio charging reviews for the Australian Maritime Safety Authority and the Therapeutic Goods Administration

Department of Infrastructure, Regional Development and Cities: Australian Maritime Safety Authority
<p>While levy revenues exceeded costs over the four years that were examined (2010–11 to 2013–14) in the portfolio charging review, the Marine Navigation Levy incurred deficits in three of those years.</p> <p>The review identified three potential opportunities to expand charging activities, although the opportunities presented both logistical and operational issues.</p> <p>In response to the findings of the 2015 portfolio charging review, AMSA advised that it is investigating these opportunities. As at January 2019, it had not completed a review of options to address the misalignment of costs and revenues identified in the review.</p>
Department of Health: Therapeutic Goods Administration
<p>The Health portfolio charging review recommended improvements to the management of charging activities across the Health portfolio (for example, robustness of cost recovery models and regular updates of CRISs), as well as measures to address specific issues relating to cost recovery by the TGA. The TGA issues are summarised below.</p> <p>Cross subsidy of fee-free programs</p> <p>In providing fee-free services for the Orphan Drug Program and the Special Access Scheme, and cross subsidising the cost of these schemes, Health is not compliant with the Cost Recovery Guidelines. The Orphan Drug Program is an activity undertaken for the public good, with the objective of bringing medicines for rare diseases to market that may otherwise not be available because they are not commercially viable. The Special Access Scheme refers to arrangements that provide for the import and/or supply free of charge of an unapproved therapeutic good, essential for treating or curing a terminally ill patient, on a case-by-case basis.</p> <p>While recognising inconsistency with the Cost Recovery Guidelines, the portfolio charging review supported the cross-subsidisation of these costs on the basis that:</p> <ul style="list-style-type: none">• cross-subsidisation of the Orphan Drug Program was confined to a small group of sponsors and did not extend to broader industry;• the fee-free waivers were supported by regulation; and• the cross-subsidies were consistent with the original government policy decision that the TGA's regulatory activities be fully cost recovered (although some TGA costs — for scheduling and other services — are met from the Budget).

The portfolio charging review therefore proposed — and the Minister for Health subsequently agreed — that the cross-subsidisation of fee-free services continue and that Health include information in relation to the costs of these services in its CRIS for the TGA. Health now does this. This issue is considered further at paragraph 3.39.

Under- and over-recovery of costs

While TGA regulatory activities were being fully cost recovered, there had been an imbalance of costs to revenue (over- or under-recovery) at the industry sector level that had occurred over time. The review report indicated that this was being addressed through changes to the TGA's cost recovery model and changes to regulatory business practices and processes arising from the Medicines and Medical Devices Review, which would in turn result in changes to fees and charges. These changes are being progressively implemented.

TGA reserves

The 2016–17 Budget measure 'Improving the Regulation of Therapeutic Goods in Australia' approved the projected expenditure of \$20.4 million from TGA reserves over four years to implement the recommendations of the Expert Panel Review of Medicines and Medical Devices Regulation. To prevent an unacceptable reduction in the level of the TGA's reserves (traditionally one-quarter of operating expenses), the Portfolio Charging Review proposed that fees and charges be increased progressively over 2017–18 and 2018–19 to restore the TGA's reserves. Action has since been taken to restore reserves (see paragraph 3.37).

Source: Infrastructure and Regional Development, Portfolio Charging Review Report, June 2015 and Department of Health, 2016–17 Portfolio Charging Review Report.

Entity charges — use of levies and fees

3.3 The Cost Recovery Guidelines state (paragraph 4) that:

- cost recovery fees will be imposed when a good, service or regulation is provided directly to a specific individual or organisation; and
- cost recovery levies will be imposed when a good, service or regulation is provided to a group of individuals or organisations (e.g. an industry sector) rather than to a specific individual or organisation.

3.4 The Guidelines also state (paragraph 36) that cost recovery charges should be: clear and easy to understand; closely linked to the specific regulatory activity; set to recover the full efficient costs of the specific regulatory activity; efficient to determine, collect and enforce; and set to avoid volatility while still being flexible enough to allow for changes based on fluctuations in demand or costs.

Australian Maritime Safety Authority

3.5 The overall structure of AMSA's charges (see paragraph 1.14) is consistent with the distinction in the Cost Recovery Guidelines relating to fees and levies. AMSA's charges were last revised in 2015.

3.6 Paragraph 94 of the Cost Recovery Guidelines indicates that, when designing a levy, the cost driver should approximate the level of resources used to provide the activity and that differentiated levy rates could be used to more closely reflect resources used by different groups based on their risk, size or other criteria. The Marine Navigation Levy and the Marine Navigation (Regulatory Functions) Levy are based on a sliding scale on the net registered tonnage of ships, while the Protection of the Sea levy is based on a rate per ton of the tonnage of ships. Fees are either a specified amount or an hourly rate. AMSA argues that these tonnage-based levies are easy to administer and accepted by industry. However, as required by paragraph 94 of the Cost Recovery

Guidelines, there is no clear relationship between AMSA's costs for these activities (for example, navaid maintenance (\$11.3 million in Protection of the Sea levy) and service contracts (\$17 million in the Marine Navigation levy)) and the tonnage of ships, so resulting in likely cross-subsidisation of the owners of smaller vessels by the owners of larger vessels. An alternative approach to using tonnage as a cost driver for levies, which would better relate charges to efficient regulatory effort, would be to differentiate the charges based on risk analysis of different classes of regulated entities and the routes they take.²⁷ AMSA is intending to review its charging arrangements following the introduction of the National System and there would therefore be an opportunity to examine suitable proxies for levy-based charges in this context.

Department of Agriculture and Water Resources

3.7 The application of Agriculture's fees for its biosecurity, live animal export, plant export and food export programs is detailed in the department's 2017 Charging Guidelines, which are available on the department's website.²⁸

3.8 Agriculture reviewed its charging arrangements in 2014–15, and legislation to support the revised charges came into effect on 1 December 2015. Since then, no new charges relating to food exports have been introduced and there have been no price increases. However, Agriculture has provided remissions where it has assessed that charges have exceeded costs.

3.9 Agriculture has a range of fees and levies, which are used to recover the cost of six fee-for-service functions and 11 levy functions (grouped into Program Management and Administration, Assurance and Incident Management). Fee bearing activities may include assessments of applications for export documents and issuing approvals/certification, inspections and audits of products for exports and other services. Levies include charges for registered establishments, slaughtering or dressing of animals, applications, livestock and meat export licences and export documents.

3.10 The explanatory memoranda for the legislation supporting the revised charges in 2015 stated that the reforms sought to align Australia's export certification system with an efficient and effective cost recovery model, consistent with the Australian Government Cost Recovery Guidelines. However, while Agriculture has a legislative basis for its levies, the Cost Recovery Guidelines indicate that some levy-based costs would more appropriately be recovered through fees.

3.11 Levy Program Management and Administration activities include workforce and business management, business system administration, stakeholder engagement, policy and instructional material, business improvement and other activities, such as organising initial appointments, staff training, assessment or mentoring and attending general phone and email enquiries. In its Charging Guidelines, Agriculture justifies recovery of these charges through levies on the basis that they have broad benefits, and do not benefit individual clients. However, this is not always the case. Further, many of the costs recovered through levies are enabling or indirect costs, and the Cost Recovery

27 For example, AMSA advised that there is a higher risk and regulatory effort for oil tankers and ships navigating around the Great Barrier Reef than most other parts of Australia's coastline.

28 Department of Agriculture and Water Resources, *Departmental Charging Guidelines 2017*, v.1.4.

Guidelines indicate (at paragraphs 84 to 87 and Figure 3) that fees should include both direct costs and an appropriate share of indirect costs.

3.12 By way of example, the cost of assessment and approval/certification issuing functions are recovered through three fees — electronic and manual document fees and replacement document fee. There is also a levy — the electronic document levy that is used to recover levy function costs. When an exporter applies for an electronic export permit, the invoice will have two amounts payable — the electronic document fee and the electronic document levy. Agriculture also has a levy for recovering the costs of a registration application, with no associated fee. The cost base for this charge is five per cent of the levy functions of a team in the Exports Division, which is responsible for: registering export establishments; developing export certification to meet new and changing importing country requirements; amending export requests for permit to export in response to changes required by exporters; and facilitating detained consignments.

3.13 The use of a levy as a charging mechanism for the recovery of expenses from an individual making an application is inconsistent with the Cost Recovery Guidelines principles (paragraph 54) that a cost recovery fee should be used when 'the activity and its costs can be linked to a specific individual or organisation' and 'a cost recovery levy should only recover the costs of the activity provided to a group of individuals or organisations that pay the cost recovery levy' (that is, the cost of activities such as policy development and development and promulgation of standards, but not overheads, such as property, IT and technical support costs (see paragraph 84 and Figure 2 of the Cost Recovery Guidelines). Agriculture's approach was criticised in reviews commissioned by the department of several of its cost recovery arrangements and some industry groups did not support the approach.²⁹

3.14 Agriculture has advised industry in the context of a review of its charging arrangements that it proposes to recommend to government that some, but not all, of the indirect costs of outputs in future be recovered through fees. However, it would be consistent with the Cost Recovery Guidelines for an appropriate share of all indirect costs of an enabling nature to be recovered through fees.

3.15 Agriculture is also considering whether fees for replacement export certificates would more appropriately become levies. The rationale for this proposed change is that some drivers of these services may be outside the control of an exporter (for example, because of a change by the importing country). However, such a change would be inconsistent with the principle in the Cost Recovery Guidelines that fees be charged when a good, service or regulation is provided directly to a specific individual or organisation.

3.16 Agriculture should use its current review of its charging arrangements to align the structure of its fees and levies with the requirements of the Cost Recovery Guidelines. It could also review fees that have not changed for around a decade. For example, the current fee of \$500 for replacement certificates was set in 2009, although the cost of these charges should have fallen in 2015 because of Agriculture's decision at that time to recover indirect costs of fees through levies.

29 One of these reviews related to the food export program — PwC, *Department of Agriculture and Water Resources — Meat Export Programme cost recovery arrangements independent review — Final Report*, February 2017.

Examination of Agriculture's 2015 cost model indicates that the \$500 fee for replacement certificates over-recovers the cost of these services by around \$200.

3.17 Fees are based on quarter-hourly rates, rather than a standard price for each service. This approach provides flexibility in charging where the length of time required is not known in advance. As Agriculture is currently reviewing charges, it may also be timely to consider alternative charging approaches that would provide greater certainty of the cost to industry.

Therapeutic Goods Administration

3.18 Fees are imposed for TGA pre-market services, such as the assessment of applications and evaluation of products, and levies are imposed for post-market processes, comprising compliance, enforcement and good manufacturing practice. Health's cost allocation methodology for the TGA calculates fees to be applied for specific services, while the levies are assessed by industry sector and apportioned across a class of stakeholders.³⁰

3.19 Fees are payable for the registration, listing or inclusion of a product on the Australian Register of Therapeutic Goods. Almost any product for which therapeutic claims are made is required to be entered into the Register. Fees vary according to the types of products under each category of registration, listing and inclusion on the Australian Register of Therapeutic Goods and are paid by the sponsors of a product. Fees are also charged for the assessment of the application for registration. These fees vary according to the risk level of the product.

3.20 The costs of post-market processes are more difficult to assign to individual companies and therefore are imposed through levies, apportioned to all sponsors of products registered, listed or included on the Australian Register of Therapeutic Goods and imposed as an annual charge.

3.21 This overall structure is consistent with the distinction in the Cost Recovery Guidelines between fees and levies, and changes to fees and charges are approved by the Minister for Health.

Alignment between expenses and revenue

3.22 The Cost Recovery Guidelines (paragraph 37) require entities to develop mechanisms to manage any under- or over-recovery of costs and prevent any systematic over- or under-recovery. The Guidelines also indicate that ideally expenses and revenue should be aligned on a yearly basis, but recognise that there can be justification for alignment over a longer period (for example, the business cycle of the activity). Requiring the alignment of expenses and revenue to be assessed as part of the annual Budget process would help to prevent any systematic over- or under-recovery of costs, particularly at the program or sector level. In this regard, it is important that entities clearly specify the period of time over which expenses and revenue are aligned.

3.23 A key issue in considering the alignment of expenses and revenue is the level in the output structure against which cost recovery should be measured — individual fee for service or fee category (see paragraph 1.4). Higher-level measurement of the alignment of expenses and revenue provides an entity with flexibility, but obscures under- and over-recovery results within the total

30 Users of the TGA's regulatory services (including monitoring of compliance with the regulatory framework) are broadly divided into the industry sectors listed at paragraph 1.18. The TGA undertakes some fee-free regulatory activities, including the Orphan Drug Program and the special access/authorised provider schemes. The cost of these schemes is cross-subsidised from other cost recovered services. Consideration of the TGA's approach to the recovery of these costs is at Table 3.1 and paragraph 3.39.

result. Variances at the output level and an explanation for these variances should therefore also be provided.

3.24 Regulatory agencies should actively manage under- and over-recovery results and maintain an agreed level of equity reserve (for example, three months working capital). Over-recovery results should be returned to industry (desirably the same client group) through reduced prices in the future or rebates to those who paid fees. Investment in the regulator's capability funded by equity reserves should be agreed with industry (evidenced by decision in industry consultative committee minutes). Under-recovery means that industry is being subsidised and there is the potential for higher charges in the future to recover the shortfall, with consequential market distortions.

Australian Maritime Safety Authority

3.25 AMSA's cost recovery financial performance over the five years from 2013–14 to 2017–18 is summarised in Table 3.2.31 This indicates that over this period AMSA:

- over-recovered costs across all of its regulatory activities by \$28 million;
- over-recovered costs in each year for activities covered by the Regulatory Function Levy and had an accumulated surplus for the period of \$40 million;
- over-recovered costs for four of the five years on activities covered by the Protection of the Sea Levy and had an accumulated surplus for the period of \$17 million;
- under-recovered costs for four of the five years on activities covered by the Marine Navigation Levy and had an accumulated deficit for the period of \$14 million; and
- under-recovered the cost of fee-for-service activities in each year and had an accumulated deficit of \$15 million.

3.26 As at 30 June 2018, AMSA had retained earnings of \$65 million.³² This includes reserves to meet the cost of environmental disasters (this capability is also met through a separate Pollution Response Reserve of \$50 million that was approved by the AMSA Board). The purpose of the reserve is to support AMSA's rapid response to major pollution incidents and to meet the costs of such incidents that are not recoverable from the ship owner or insurers.

31 The tables for Agriculture and the TGA include data for 2011–12 and 2012–13. AMSA does not have reliable cost recovery figures by regulatory activity for these years. Further, AMSA was unable to explain the large increase in fee-for-service expenses in 2016–17.

32 AMSA, *Annual Report 2017–18*, p. 95.

Table 3.2: Australian Maritime Safety Authority — Cost recovery financial performance 2013–14 to 2017–18 (\$'000)

	2013–14	2014–15	2015–16	2016–17	2017–18	Total
Marine infrastructure (Marine Navigation Levy)						
Expenses	36,244	35,264	34,580	41,134	31,874	179,096
Revenue	31,354	32,314	32,993	34,091	34,651	165,403
Over (+)/under (-) recovery	-4,890	-2,950	-1,587	-7,043	2,777	-13,693
Environmental marine protection (Protection of the Sea Levy)						
Expenses	34,871	32,795	34,654	29,128	30,219	161,667
Revenue	39,253	31,268	37,259	34,068	36,494	178,342
Over (+)/under (-) recovery	4,382	-1,527	2,605	4,940	6,275	16,675
Seafarer and ship safety (Regulatory Function Levy)						
Expenses	35,199	46,501	44,781	38,218	43,142	207,841
Revenue	46,315	48,349	49,266	51,211	52,488	247,629
Over (+)/under (-) recovery	11,116	1,848	4,485	12,993	9,346	39,788
Marine services and ship registration, including National System Tranche 1 (fee for service)						
Expenses	7,136	5,823	5,632	11,516	6,427	36,534
Revenue	4,111	3,658	4,631	4,922	4,077	21,399
Over (+)/under (-) recovery	-3,025	-2,165	-1,001	-6,594	-2,350	-15,135
Overall cost recovery performance						
Expenses	113,450	120,383	119,647	119,996	111,662	585,138
Revenue	121,033	115,589	124,149	124,292	127,710	612,773
Over (+)/under (-) recovery	7,583	-4,794	4,502	4,296	16,048	27,635

Note a: Reliable data are not available for the 2011–12 and 2012–13 financial years. There are also differences in the figures published in CRISs because of the differing treatment of insurance recoveries and incorrect inclusion of non-regulatory revenue.

Note b: The figures for 2015–16 and 2017–18 include insurance recoveries not received when the financial statements were completed.

Source: AMSA.

3.27 AMSA's financial performance indicates that there is a need for AMSA to restructure its charges for the Regulatory Function Levy and the Marine Navigation Levy so that revenues (and the resultant required charges) are aligned with AMSA's costs for those activities. The charging opportunities identified in the Portfolio Charging Review (see Table 3.1) could also be examined in this context.

3.28 As shown in Table 3.2, AMSA does not currently recover the full cost of its fee-based services. AMSA advised that the costs of many of these fee-based services are influenced by the requirements of international agreements or other countries. If, after further investigation, AMSA considers that it cannot fully recover the cost of its fee-based services, the appropriate action would be to ask government to approve the amounts to be recovered from industry and the arrangements for meeting the shortfall in costs.

3.29 AMSA's fees determination for regulatory activities covered in this audit was last revised in 2015.³³ There is a need for AMSA to update its fees determination more regularly to help address the under-recovery of costs relating to its fee-based services.

Department of Agriculture and Water Resources

3.30 Agriculture's cost recovery financial performance from 2011–12 to 2017–18 is summarised in Table 3.3. This indicates an under-recovery of \$3.3 million over the seven-year period and an under-recovery of \$13.3 million since 2015–16 when Agriculture last revised its cost recovery arrangements (compared to a planned under-recovery of \$5.2 million in the 2015–16 CRIS).

33 AMSA, *Australian Maritime Safety Authority Fees Determination 2015*, 21 September 2015. Available from <https://www.legislation.gov.au/Details/F2015L01477>, [accessed 18 January 2019].

Table 3.3: Agriculture and Water Resources — Cost recovery financial performance 2011–12 to 2017–18 (\$'000)

	2011–12	2012–13	2013–14	2014–15	2015–16	2016–17	2017–18	Total
Meat exports								
Expenses	71,612	72,316	75,772	77,705	94,250	83,982	83,832	559,470
Revenue	65,471	75,608	80,623	82,701	87,565	81,429	82,035	555,433
Net over (+)/under (-) recovery	-6,141	3,292	4,851	4,997	-6,685	-2,553	-1,797	-4,037
Dairy exports								
Expenses	1,978	2,152	1,979	1,862	2,401	3,005	3,773	17,149
Revenue	2,166	2,165	2,167	2,295	2,521	2,753	2,778	16,845
Net over (+)/under (-) recovery	188	13	188	433	120	-252	-995	-305
Fish and egg exports								
Expenses	3,722	3,408	3,335	2,768	3,033	4,165	3,724	24,155
Revenue	3,359	3,792	3,470	3,260	3,265	3,429	3,657	24,232
Net over (+)/under (-) recovery	-362	384	135	492	232	-736	-67	77
Non-prescribed goods								
Expenses	2,729	1,759	1,899	1,681	2,656	3,346	2,719	16,791
Revenue	2,343	2,426	2,411	2,493	2,688	2,622	2,806	17,790
Net over (+)/under (-) recovery	-386	667	512	812	31	-724	87	999
Overall financial performance								
Expenses	80,041	79,635	82,985	84,016	102,340	94,498	94,049	617,565
Revenue	73,339	83,991	88,671	90,749	96,039	90,233	91,277	614,300
Net over (+)/under (-) recovery	-6,702	4,356	5,686	6,734	-6,302	-4,265	-2,773	-3,265

Note: Differences in totals are due to rounding.

Source: Department of Agriculture and Water Resources.

3.31 To address the continuing accumulation of cost recovery reserves, the 2015–16 CRIS provided for temporary remissions (discounts) to be provided to exporters. As at 30 June 2018 Agriculture's cost recovery reserves for food exports was around \$5 million, compared to around \$6 million at 30 June 2017. Agriculture seeks to retain reserve balances of between zero and five per cent of annual program expenditure (that is, up to around \$4 million).

3.32 Agriculture commissioned a review of cost recovery arrangements related to meat exports in 2017. This review:

- identified an imbalance between revenue and expense for some activities that will potentially provide less equity for industry participants; and
- found that Agriculture should revise the way in which it distributes the expense base associated with the Program Management and Administration cost pool to accurately determine the levels of any over-recoveries.

3.33 Some changes to Agriculture's charges were announced in the 2018–19 Budget to address structural under-recoveries in some programs. The 2018–19 Budget measure included recovery of the costs of some export certification charges that are currently not cost recovered. Agriculture is currently reviewing and consulting with industry on its charges, with the aim of introducing revised charges from 1 July 2019.

Therapeutic Goods Administration

3.34 Health's cost recovery financial performance for the TGA over the seven years from 2011–12 to 2017–18 is summarised in Table 3.4.

Table 3.4: Therapeutic Goods Administration — Cost recovery financial performance 2011–12 to 2017–18 (\$m)

	2011–12	2012–13	2013–14	2014–15	2015–16	2016–17	2017–18	Total
Prescription medicines								
Expenses	55.9	59.4	61.0	58.1	63.2	68.4	68.2	434.2
Revenue	58.6	64.0	62.5	65.6	71.7	68.5	72.9	463.8
Over (+)/under (-) recovery	2.7	4.6	1.5	7.5	8.5	0.1	4.7	29.6
Over-the-counter medicines								
Expenses	9.1	8.5	9.1	7.9	5.1	5.7	5.3	50.7
Revenue	7.5	7.2	7.8	7.7	6.7	7.8	9.0	53.7
Over (+)/under (-) recovery	-1.6	-1.3	-1.3	-0.2	1.6	2.1	3.7	3.0
Complementary medicines								
Expenses	10.2	15.1	16.0	22.7	12.4	12.9	12.1	101.4
Revenue	9.6	11.1	11.9	11.4	15.7	13.8	14.5	88.0
Over (+)/under (-) recovery	-0.6	-4.0	-4.1	-11.3	3.3	0.9	2.4	-13.4
Medical devices, including in-vitro diagnostic								
Expenses	19.0	25.5	25.0	24.1	29.4	33.3	37.6	193.9
Revenue	24.4	26.4	31.6	32.0	34.3	37.2	40.6	226.5
Over (+)/under (-) recovery	5.4	0.9	6.6	7.9	4.9	3.9	3.0	32.6
Good manufacturing practice								
Expenses	9.9	10.0	13.1	12.9	13.2	14.4	14.9	88.4
Revenue	13.6	12.3	12.0	12.1	11.2	9.9	13.2	84.3
Over (+)/under (-) recovery	3.7	2.3	-1.1	-0.8	-2.0	-4.5	-1.7	-4.1
Blood, blood components and biologicals								
Expenses	5.6	5.6	4.0	3.3	2.9	3.6	3.6	28.6

	2011–12	2012–13	2013–14	2014–15	2015–16	2016–17	2017–18	Total
Revenue	2.2	2.5	3.1	2.0	2.2	2.6	2.4	17.0
Over (+)/under (-) recovery	-3.4	-3.1	-0.9	-1.3	-0.7	-1.0	-1.2	-11.6
Other activities (such as laboratory, medicines and chemical scheduling)								
Expenses	na	na	na	4.4	2.0	8.6	6.7	21.7
Revenue	na	na	na	8.0	2.0	1.7	2.7	14.4
Over (+)/under (-) recovery	na	na	na	3.6	0.0	-6.9	-4.0	-7.3
Overall cost recovery performance								
Expenses	109.7	124.1	128.2	133.4	128.2	146.9	148.4	918.9
Revenue	115.9	123.5	128.9	138.8	143.8	141.5	155.3	947.7
Over (+)/under (-) recovery	6.2	-0.6	0.7	5.4	15.6	-5.4	6.9	28.8

Note: These figures include revenue of approximately \$2–3 million per annum provided by the Government.

Source: TGA Cost Recovery Implementation Statements.

3.35 Table 3.4 indicates that, over the period for the TGA, Health:

- over-recovered across all industry sectors by \$28.8 million, with most of the over-recovery occurring in two sectors — prescription medicines and medical devices;
- consistently under-recovered costs on its 'Good manufacturing practice' and 'Blood, blood components and biologicals' industry sectors in all or most years and, in recent years, also 'Other activities', with under-recovery in recent years also being related to the implementation of the recommendations of the Expert Panel Review of Medicines and Medical Devices Regulation (see Table 3.1); and
- under-recovered the cost of complementary medicines across the period, but with over-recovery since 2015–16.

3.36 Health revised the TGA's charges in 2017–18 and 2018–19, some of which arose from the changed regulatory arrangements resulting from the 2014–15 Medicines and Medical Devices Review, to which the government responded in 2016. Despite under-recovery related to 'good manufacturing practice' since 2013–14, levies related to the manufacturing of medicines were reduced on 1 July 2018 (with an overall reduction for most medical devices of 4.96 per cent).

3.37 In the February 2019 version of the TGA's 2018–19 CRIS, Health stated that it aims to maintain accumulated reserves (which are in a special account and require government or ministerial approval to access) at around 25 per cent of operating expenses. As at 30 June 2018, TGA accumulated reserves totalled \$50.6 million or 33 per cent of annual revenue.

3.38 Health's 2016 portfolio charging review noted that, while it fully recovered the cost of the TGA's regulatory activities (apart from the small number of regulatory activities which were Budget-funded) between 2012–13 and 2016–17, the effectiveness of the TGA's costing model could be improved by reducing the level of cross-subsidisation that has occurred across industry sectors.

3.39 The portfolio charging review also found (see Table 3.1) cross-subsidisation of fee-free services. While the review recommended that this cross-subsidisation should continue, but with disclosure in the TGA's CRIS, this is non-compliant with the Cost Recovery Guidelines, which provide (Figure 12, page 38) that, where costs cannot be reasonably attributed to an individual or organisation, they should not be cost recovered. This suggests it would be more appropriate for these costs to be met from the Budget, in the same way that Health is funded for the TGA's scheduling and some other services from the Budget. Health did not obtain legal advice on the matter. While noting that the Minister for Health approved the continued cross-subsidisation of these costs, paragraph 33 of the Cost Recovery Guidelines requires that entities and responsible ministers must have policy approval from the Australian Government to cost recover. The ANAO considers that the continued practice of cross-subsidising fee-free services should be further reviewed and that Health submits a proposal to seek a government decision on the funding of the cost of these services.

Do the entities' cost recovery methodologies align costs and charges and promote the recovery of the efficient costs of the regulatory activity?

There is scope for all three entities to improve their costing practices. The cost model used by AMSA does not accurately capture the costs of providing the regulatory activities or calculate

charges that are aligned to those costs. While Agriculture uses an activity-based methodology, it is not possible to determine the full cost of the output from Agriculture's model. Health also uses traditional activity-based costing for the TGA's activities, with the cost of regulatory activities linking to the prices and estimated revenues for those activities, although Health could improve the attribution of effort to regulatory activities.

None of the three entities have incorporated efficient costs in their cost recovery models and only Agriculture has sought to benchmark the costs of its regulatory activities with those of other entities. There is an opportunity for the Department of Finance to examine how benchmarking can be further encouraged and facilitated.

Cost recovery methodologies

3.40 The cost recovery methodology underpinning the development of individual charges is critical to the implementation of the policy and its legitimacy. In particular, entities need to be able to demonstrate how charges have been calculated and the appropriateness of the amounts charged (paragraph 74 of the Cost Recovery Guidelines). To do this, entities need robust cost recovery tools or 'models', such as activity-based cost models.

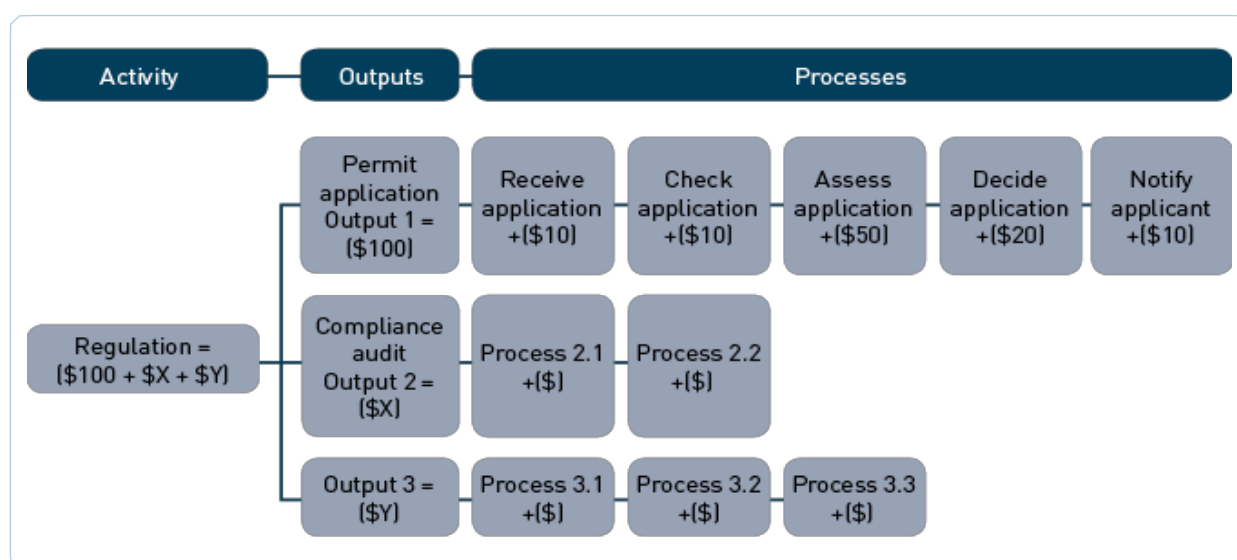
3.41 The Cost Recovery Guidelines (paragraphs 73) state that the cost recovery model should:

- identify outputs and business processes of the regulatory activity;
- accurately measure and assign costs to outputs and business processes;
- use relevant proxies for the allocation of indirect costs;
- track the degree of alignment between expenses and revenue; and
- produce relevant and timely reports for the regulatory activity.

3.42 The primary purpose of a cost recovery model is to determine the cost of all the outputs an agency provides to regulate an industry. The cost of the output is recovered through a cost recovery charge (fee or levy) based on an assessment of the nexus of the output and an individual participant in the industry, as well as consideration to the fairness of the costing (for example, rural providers would pay more for travel than metropolitan providers). The cost of the output is the basis for the charge.

3.43 The Guidelines provide the example of regulatory activity outputs or services and business processes shown in Figure 3.1. The Charging Framework states (Figure 1, page 6) that charges must reflect the efficient unit cost of a specific good or service, where revenue and expenses are closely aligned. In the Cost Recovery Guidelines' model, an example of an output, for which a price would be set, would be issuing a certificate and the regulatory activity would be the regulation of aspects of an industry, such as medical devices. In a typical activity-based costing model, 'activities' are what the Cost Recovery Guidelines term 'processes'.

Figure 3.1: Regulatory activity outputs and business processes



Source: *Australian Government Cost Recovery Guidelines*, July 2014 — Third Edition, p. 33.

3.44 The cost recovery models of the three entities were assessed using the framework shown in Appendix 3. The ANAO's assessment (summarised at Table 3.5) indicates scope for improvement in the methodologies used by all entities, although the cost model used by Health for the TGA is generally sound and reflects a genuine activity-based costing approach.

3.45 There is currently little discussion in the Cost Recovery Guidelines on ways of assuring the integrity of entity cost recovery tools/models. While Finance advised that the three entities had each consulted it on their cost recovery models, in reviewing the Cost Recovery Guidelines as proposed earlier (Recommendation No.2), it would be opportune for Finance to examine the best way of providing independent oversight of the integrity of entity cost recovery models. Finance could also examine the suitability of the models, commensurate with the materiality, complexity and sensitivity of the regulatory charging activity.

Table 3.5: The ANAO's assessment of entity cost models

Criteria	AMSA	Agriculture	TGA
Cost recovery and allocation methodology	▲	▲	◆
Measurement of and attribution of costs to processes and outputs	▲	▲	◆
Expected use of drivers to help set fees	▲	◆	▲
Technical	▲	▲	◆
Reporting	▲	▲	◆

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: ANAO analysis.

Australian Maritime Safety Authority's cost recovery model

3.46 Excluding cost recovery related to the National System, which is outside the scope of this audit, AMSA's cost recovery operations are based around four regulatory activities:

- Navigation infrastructure — development of safety and environmental protection standards to promote the responsible operation of vessels and safety of seafarers in Australian waters, and monitor and enforce compliance with these standards (with costs recovered through the Marine Navigation Levy);
- Environmental marine protection — preventing and combating ship-sourced pollution in the maritime environment (with costs recovered through the Protection of the Sea Levy);
- Seafarer and ship safety — providing systems that aid safe marine navigation (with costs recovered through the Regulatory Function Levy); and
- Marine services and ship registration — promoting seafarers' wellbeing, safety, competency and capability as an integral part of vessel safety (with costs recovered through fees for service).

3.47 AMSA does not recover the cost of its search and rescue operations, which are funded by the government as part of AMSA's community service obligations.

3.48 In April 2018, AMSA received a report it had commissioned on its cost recovery framework. The report identified a number of deficiencies in AMSA's cost recovery policies and practices, including:

- an inability to review the calculations and assumptions within the cost recovery model as AMSA's previous cost recovery system (TM1) was no longer supported and historical costing information was not available for the previous three financial years;
- a lack of internal documentation that outlines AMSA's cost recovery process and procedures and incomplete documentation to fully support the cost recovery decisions, stakeholder engagement and the cost recovery model;
- inconsistencies between the published 2016–17 CRIS for budgeted expenses and supporting documentation and work papers;
- a lack of evidence supporting the calculation of fee-for-service rates; and
- the need for AMSA to develop and regularly update a consolidated policy document outlining its methodologies for allocating costs, attributing revenue and calculating levies and charges, including standard operating procedures to ensure corporate knowledge is maintained with staff movements.

3.49 Since April 2018, AMSA has developed a revised cost recovery model (or suite of spreadsheet-based workbooks), which it has used to determine costs and revenue for 2017–18 and estimate costs and revenue for 2018–19 and the forward years. The model includes all AMSA regulatory activities, including the National System and search and rescue operations that are not cost-recovered.

3.50 AMSA has also provided increased support for operational staff to enable more accurate allocations of staff time and costs to be derived. AMSA advised the ANAO that it will continue to refine this revised cost model and develop supporting procedures over the next year.

3.51 The ANAO's assessment of AMSA's new cost recovery model (Table 3.6) indicates that it is not a fully functioning activity-based cost model and requires further work to enable it to: calculate costs at charge points; allocate corporate function costs accurately across all regulatory activities; and include accurate drivers of central costs and depreciation. It is not possible to determine from the model if the cost is the full or efficient cost of the output or service. However, the model has a clear overall structure; the data used in the model are apparent and calculations performed are transparent; and consideration has been given to the cost drivers used.

Table 3.6: The ANAO's assessment of AMSA's cost model

Criterion	ANAO assessment
<p>Cost allocation methodology</p> <p>▲</p>	<p>AMSA's methodology is based on a high-level mapping of input costs in the general ledger to processes (what AMSA calls activities) and service lines within AMSA, rather than to direct business units. The model calculates the full cost of the four regulated activities, the National System and non-cost recovered regulatory activities. It does not calculate costs for individual outputs or services (charges are set separately from the model) and so it is not possible to compare such costs with the charges that have been set.</p> <p>AMSA was unable to provide technical documentation to support its models, and indicated that it would be preparing this documentation as the model is further developed.</p>
<p>Measurement of and attribution of costs to processes and outputs</p> <p>▲</p>	<p>The model is not a fully functioning activity-based cost model and it does not calculate costs for particular outputs or services.</p> <p>The cost recovery model provides adequate evidence of the total cost of regulatory activities. However, the model does not calculate the cost of fee-based services at a level that allows a comparison of the cost of each service and the fee used to recover that cost. Levy-based costs are not calculated at the output level.</p> <p>Varying fee types — hourly rate, fixed and variable — are used within a single fee-based service, such as services to seafarers and coastal pilots, but there is little evidence to support the use of fixed and variable fees. Fees were revised in 2015–16 on the basis of calculations provided by AMSA's Marine Operations Division. This was a bottom-up process that estimated the cost of each service based on the time spent on each service and an hourly rate (not calculated within the model). These costs were not reconciled to the output costs generated by the cost model.</p> <p>Revenue is calculated by a separate team within AMSA, based on prior year revenue with an 'indexation' factor. Only high-level comparisons of revenue and costs are possible.</p> <p>Corporate type functions, including human resources, finance, information technology and the AMSA executive and Board, would normally be expected to be allocated to all outputs or services, including non-cost recovered outputs, using direct full-time equivalent staff (FTE) as a driver for all non-corporate staff. However, the AMSA model does not do this. It only allocates the corporate costs of \$22.6 million to the Marine Navigation, Protection of the Sea and Regulatory levies and Search and Rescue operations (budget-funded), with \$10.9 million (or 48 per cent) being allocated to the Regulatory levy; it does not allocate corporate costs to the National System or fee-based services. Reallocating the cost of these corporate functions to all regulatory activities would reduce the Regulatory Levy by approximately \$3.5 million, increasing the cost over-recovery of this levy from</p>

Criterion	ANAO assessment
	113 per cent to 124 per cent. This analysis also indicates that the National System is being cross-subsidised by other regulatory activities by around \$6.8 million in 2018–19.
Expected use of drivers to help set charges ▲	<p>Survey templates are completed by managers to enable direct costs to be assigned to business processes and regulatory activities based on effort. However, AMSA advised that these estimates are in need of refinement and that it is working with staff to improve the accuracy of these estimates.</p> <p>For some expenses, such as maintenance contracts, a detailed allocation process using various cost drivers has been undertaken. However, more work is needed to refine some of these drivers. For example, the allocation of costs of \$535 000 for maintenance of the Under Keel Clearance Management System in the Torres Strait should be improved. The model uses inconsistent and undocumented rules for the distribution of depreciation expenses.</p>
Technical ▲	The model has a clear structure with input calculations and output worksheets clearly identified. It also includes basic version control (such as date of last update and drivers used). However, it does not provide reconciliation to key data sources, specifically budgeted expenses and asset listings, with some figures not reconciling to the estimates in AMSA's Portfolio Budget Statement.
Reporting ▲	AMSA compares actual prior year expenses to the current budget year in the cost model at an output and organisational unit levels, not at the level at which charges are set. However, the tables prepared for inclusion in the CRIS have different expense totals to the cost model. There is also no table that links the Portfolio Budget Statement to the cost model and CRIS, with the same item having various names in different locations.

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: ANAO analysis of current CRIS model, used in the preparation of the 2018–19 CRIS for the National System and the draft 2018–19 CRIS for ship and seafarer safety, navigation infrastructure and environmental protection.

Department of Agriculture and Water Resources' cost recovery model

3.52 In 2014, Agriculture used spreadsheet-based models to determine if its cost recovery arrangements would be over- or under-recovered. This model was used as the basis for Agriculture's last CRIS in 2015. Agriculture implemented a new activity-based cost (ABC) system in December 2016 to replace its old system (TM1), and a new time recording system (TimeTiger) to replace a manual/spreadsheet process (running in parallel). Agriculture has been conducting a review of its charges and cost recovery arrangements in 2018–19, with a view to recommending changes to government for implementation in 2019–20. While Agriculture has a dedicated ABC system, it is continuing to use spreadsheet-based cost models to support this review. Agriculture advised that the ABC system will be used to calculate the final costs of the preferred options to be presented to the government.

3.53 The ANAO's assessment of Agriculture's cost model (Table 3.7)³⁴ found that Agriculture's 2014 model did not calculate costs for individual outputs/services and comparisons of the charges for individual outputs/services with their cost were therefore not possible. While Agriculture's current model does calculate costs for individual outputs/services, it is not possible to determine from the model if this is the full or efficient cost of the output or service.

Table 3.7: ANAO assessment of Agriculture's cost model

Criterion	ANAO assessment
<p>Cost allocation methodology</p> <p>▲</p>	<p>Agriculture's cost recovery methodology is to allocate corporate and business support costs to direct cost centres and from there to 17 activities divided into four groups. Three of these groups are recovered through levies and one is fee-based. This methodology is applied consistently across all cost recovery arrangements. Within the category of food export certification, there are separate arrangements for meat exports, dairy exports, fish and egg exports, and non-prescribed goods.</p> <p>Agriculture developed a high-level cost-recovery policy document and departmental charging guidelines to support its overall cost recovery approach. However, the cost allocation methodology and business rules for the 2014 model were not well documented.</p> <p>Agriculture has adequate documentation of its new ABC system. However, there is a need for more complete and clear documentation of the cost recovery model used in the current review process, which consists of three separate, but related, spreadsheets (for example, how the various spreadsheets work together and are updated has not been documented). Examination of the spreadsheets indicates that Agriculture's approach is to recover the full costs of the services. It does not examine whether these costs (and resultant prices) would be efficient.</p>
<p>Measurement of and attribution of costs to processes and outputs</p> <p>▲</p>	<p>Agriculture's 2014 cost model did not determine costs for individual outputs and the charges for those outputs. Rather, it calculated the cost at the overall process level. For example, in the case of dairy export assessment services — for the outputs of issuing manual certificates, electronic certificates and replacement certificates, industry clients are charged fees of different amounts, but these fees may not align to costs, which were not calculated.</p> <p>There is not an equitable share of indirect costs across all 17 activities for the reasons stated at paragraphs 3.13 and 3.14. Further, the allocation of indirect costs in the model was unclear because it did not include a whole-of-agency allocation of expenses and control total (that is, the models only included the arrangement's share of expenses).</p> <p>While the cost model Agriculture is using as part of its current pricing review does determine the cost for individual outputs, it is not possible to determine from the pricing model if this is the full cost. Cost allocation is done using the department's ABC system, extracts of which are used in the three workbooks. One of these workbooks, the pricing model, which is used to review charges, uses an extract that does not provide a breakdown of direct and indirect expenses at the output level.</p>
<p>Expected use of drivers to help set charges</p> <p>◆</p>	<p>In the 2014 model, Agriculture used management estimates of time usage for the allocation of overheads and some other expenses. While Agriculture had determined the time taken to complete each output and staff productivity, it did not use this information to calculate the cost of each output.</p>

34 This assessment is based on examination of the spreadsheet-based dairy and meat components of Agriculture's 2014 cost model and the spreadsheet-based models being used as part of its current pricing review.

Criterion	ANAO assessment
	Since 2016, Agriculture has been using time recording through a proprietary time application (TimeTiger) for the allocation of time of operational staff. The use of applications such as TimeTiger has the potential to be more accurate than management estimates and can be a better practice approach for capturing time use. Agriculture has also undertaken a review of its corporate drivers to reduce reliance on management estimates. The integrity of the data has not been assessed in the audit.
Technical ▲	The 2014 spreadsheet-based dairy and meat models did not have a clear structure and did not reconcile to total departmental expenses and enable comparisons with Portfolio Budget Statement data, so helping to ensure their integrity. They did not specify all data sources and did not have a data table to allow easy data reporting. Agriculture is using three spreadsheets per arrangement for its cost modelling as part of its current review of prices, which use some information from its ABC system. The spreadsheets are not linked, with data manually copied from one spreadsheet to another. Manual adjustments are made to data in the pricing spreadsheet that are not reflected in the expenses spreadsheet. The spreadsheets do not provide clear explanations of data sources and assumptions (for example, system extracts are undated, indexation and drivers are hard coded percentages without explanations) and do not reconcile to total departmental expenses and do not enable comparisons with Portfolio Budget Statement data.
Reporting ▲	Examples of cost recovery arrangement reports have been provided. The ABC system has the capability to provide a wide range of reports. However, Agriculture could usefully review the methodology underlying these reports. One report provided to the ANAO used budget drivers to allocate actual expenses, resulting in inaccurate unit costs.

Note 1: PwC, *Department of Agriculture and Water Resources — Plant cost recovery arrangements independent review — final report*, 24 June 2016, p. 6.

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: ANAO.

Therapeutic Goods Administration's cost recovery model

3.54 Health uses an activity-based cost model for the TGA that was developed in 2013–14. Wherever possible, the processes behind each output in a regulatory activity were mapped and built from the 'bottom up' and the results were incorporated into a comprehensive spreadsheet-based model. In 2015–16 Health purchased proprietary activity based costing software ('CostPerform') and moved the spreadsheet model into that platform, which it still uses. The TGA cost recovery model identifies each regulatory activity and the outputs contributing to each regulatory activity undertaken within the regulatory areas.

3.55 The ANAO's assessment of the TGA model (Table 3.8) indicates that the model is well-structured, calculates prices for regulatory activities based on expected volumes and the cost of outputs that contribute to those regulatory activities, and enables reporting of costs and revenues. However, the allocation of staff effort is based on annual surveys of line areas, which are not performed consistently across the entity and have a measure of subjectivity. Health advised the ANAO that it will endeavour to improve the quality of staff effort data for cost allocations.

Table 3.8: ANAO assessment of the TGA cost model

Criterion	ANAO assessment
Cost allocation methodology ◆	The TGA model has a documented cost recovery methodology (latest version 2018) that includes hierarchies, cost elements, allocation rules, data sources and assumptions. Health maintains a technical document that fully explains the cost attribution process.
Measurement of and attribution of costs to processes and outputs ◆	<p>For a new regulatory activity, or a significant change to a regulatory activity, the initial prices are created using a bottom-up costing, where a separate work effort spreadsheet is used to determine what individual processes and tasks the team will be required to undertake as part of TGA outputs. The productive hours and the proportionate FTE charge for corporate/indirect costs are then included to determine a final fully-loaded hourly rate, which is entered into the TM1 finance and business management system.</p> <p>For existing regulatory activities, a top-down approach involving a staff survey is used to monitor the cost recovery performance, reporting and identify if a significant change is required to an individual fee. The survey allows a review of the classification of processes and tasks undertaken by teams, and provides a check on the work Health undertakes to complete outputs and a regulatory activity.</p> <p>The TGA model has two types of indirect (enabling) costs, which are appropriately attributed to outputs:</p> <ul style="list-style-type: none"> • corporate costs which consist of pure overheads such as ICT, accommodation, human resources, finance and stationery, which are allocated across the model based on FTE; and • secondary corporate costs, such as depreciation, which are charged to where the asset is located, i.e. the specific regulatory area.
Expected use of drivers to help set charges ▲	<p>Health aims to conduct the staff survey annually or when there is a significant change. The last survey was conducted in 2018 and the results sent to branch heads in September/October 2018 for updates. No survey was conducted in 2017, which Health advised was largely due to the implementation of the Medicines and Medical Devices Review recommendations. The surveys are completed by each regulatory team's manager, utilising various input methods. For example, some managers use direct input from staff, while others estimate how long it takes for their staff to complete a task. To provide robust cost driver data, it would be preferable for Health to adopt a consistent approach and to quality assure the data.</p> <p>The annual volume estimate is based on historical actual data and forward estimates using information provided by regulatory teams on future trends and activities. Indexation of prices occurs outside the model and is based on a long-established (10 year) formula accepted by industry. The policy and formula are approved by the Minister each year.</p> <p>In terms of corporate (indirect) costs, prior to 2012–13 all corporate costs were in-house (within TGA) but, in 2015, the TGA's corporate services were transferred to the broader department, which charges corporate costs against TGA regulatory activities based on the number of FTE in each regulatory branch.</p>
Technical ◆	<p>The model is a combination of activity analysis/identification, financial data extracted from the budget management system, analysis in CostPerform and management of revenue through the SAP financial management information system.</p> <p>Cost driver data are through staff effort, volume data are based on actuals and forecast trends and the data contained in CostPerform are used to undertake monthly analysis. Master data (cost centre and general ledger) are contained in the budget management system and uploaded into CostPerform.</p>

Criterion	ANAO assessment
Reporting ◆	Health monitors the alignment between the TGA's expenses and revenue through monthly finance reports. Each month the model is updated with year-to-date budget figures from TM1, including expenses and revenues, FTE, volume and revenue sales. This data extract is also saved in the TGA's records management system as a reference.

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: ANAO.

Measuring the efficient costs of regulatory activities

3.56 Cost recovery involves the Australian Government charging the non-government sector some or all of the efficient costs of a specific regulatory activity (paragraph 2 of the Cost Recovery Guidelines). Financial estimates should therefore be based on 'efficient costs', which the Cost Recovery Guidelines (paragraph 83) define as 'the minimum costs necessary to provide the regulatory activity while achieving the policy outcomes and legislative functions of the Australian Government'.

3.57 To help ensure that efficient costs are recovered, the Cost Recovery Guidelines state (paragraph 53) that entity staff should, among other things, remove incentives for 'cost padding', inefficiency and the expansion of the activity beyond the original policy intent and, where possible, benchmark the regulatory activity and its business processes.

3.58 Agriculture and AMSA have not changed their charges since 2015. Health's charges for the TGA have included increases for indexation, including increases in salary costs (although Health has absorbed some of these increased salary costs).

3.59 Action that entities have taken to help assure that efficient costs are used are summarised in Table 3.9.

Table 3.9: How entities seek to ensure that efficient costs are used

Australian Maritime Safety Authority
<p>AMSA outsources many of its regulatory processes to private operators who are certified by AMSA and then engaged directly by shipping companies. These operators are responsible for setting their own charges and ensuring that they are cost competitive.</p> <p>AMSA advised the ANAO that it actively monitors and reviews overhead costs. It also advised that, from 2018–19, it plans to compare budgets and forecasts to a domestic and an international regulatory body that provide similar charging activities, such as the Civil Aviation Safety Authority and Maritime NZ. These two agencies have been identified as providing similar services to those of AMSA, although with different funding streams.</p> <p>AMSA advised the ANAO it believes that industry has been reasonably satisfied with its cost recovery on international operations to date. This reflects a perception that Australia compares favourably with other countries, both in the charges that are imposed and the way the industry is regulated. However, as noted at paragraph 3.25, AMSA has been significantly over-recovering the cost of its regulatory activities, indicating that its charges are too high.</p> <p>As noted at paragraph 3.28, AMSA does not currently recover the full cost of its fee-paying services. To fully recover costs without increasing fees, AMSA would need to find efficiencies in these services, while still meeting international obligations. The Deputy Prime Minister's statement on arrangements for the National System indicated that the delay in implementing the levy would provide more time for AMSA to engage with industry on the most efficient and effective ways to implement the National System and that a review of all costs and charges for the National System will be conducted in 2020–21. This review could also identify opportunities to reduce costs and charges related to international shipping operations, for example, by achieving economies of scale by combining fee for service operations for international and domestic shipping.</p>
Department of Agriculture and Water Resources
<p>Agriculture compared the estimated indirect expenses for 2016–17 in its CRIS with those of 12 entities across eight other portfolios to assess the efficiency of its costs. It found that indirect expenses represented 28 per cent across all of its recovery programs, compared with an average of 21 per cent for all entities (but 39 per cent for the TGA, and less than 20 per cent for the Food Exports Program).</p> <p>When Agriculture revised its cost recovery framework in 2015, the Agriculture Minister advised that, following the redesign of the cost recovery arrangements, the department had the opportunity to analyse its regulatory activities and develop agreed benchmarks. In 2015 Agriculture commissioned a review and validation of the department's resource optimisation model, which included benchmarking components of the model with other government agencies or third-party sources. This review sought to identify opportunities for the department to achieve efficiencies.</p> <p>In 2015, the department's Australian Bureau of Agricultural and Resources Economics and Sciences (ABARES) published a report of a study of cost recovery arrangements for export certification services in the United States, Canada, Chile, Thailand, the Netherlands, Germany, Ireland and Poland. This study was intended to support Agriculture's revision of cost recovery arrangements for biosecurity and export services and to estimate the impacts of cost recovery charges for export certification on the competitiveness of Australia's major agricultural and fisheries exports. This study compared the impact on the competitiveness of Australian agricultural exports under different cost recovery scenarios (no cost recovery, partial cost recovery and full cost recovery) and found that the department's export certification costs had a small impact on trade competitiveness, measured as a change in the value of exports. Agriculture has updated the data in the report as part of the current review of its cost recovery arrangements.</p> <p>Agriculture's charges for food export certification services have not changed since 2015, notwithstanding industry concerns at the time that Agriculture's charges were too high (and some charges have not changed since 2011–12, indicating that some charges may have been set without adequate regard to the cost of providing those services). Agriculture has also not used its cost recovery model to determine the efficient cost of individual outputs/services.</p> <p>Agriculture has commissioned three reviews of the department's cost recovery on biosecurity, meat exports and plants in response to industry concerns that its charges are too high. While finding that the</p>

charging structure and general methodology currently used by the department is broadly consistent with the Cost Recovery Guidelines and its own Cost Recovery policies, the reviews identified a number of areas for improvement. For example, the meat review noted that:

- fees had not been repriced in a number of instances, removing alignment of expenses to those clients driving them; and
- levy prices were too high because of the department's approach to the treatment of overhead expenses and that greater certainty of recovery and alignment of expenses to those who create them can be achieved through amendments to the treatment of overhead expense.^a

Agriculture has been reviewing its charges and is planning to revise them in 2019–20.

Therapeutic Goods Administration

Health has attempted to benchmark the TGA's operations with those of other international medicines regulators. For example, it has sought to compare its operations with those of the European Medicines Agency and the US Food and Drug Administration. However, given the differences in the operations of these administrations, no meaningful results on the efficiency of TGA charges were obtained. Benchmarking of some aspects of Health's operations, such as records management and information and communications technology (ICT) has also been attempted. Again, these have not focused on the cost of these operations.

Note a: PwC, Department of Agriculture and Water Resources — *Meat Export Programme cost recovery arrangements independent review — final report*, February 2017, pp. 6 and 11.

Source: ANAO analysis.

3.60 This analysis indicated that AMSA and Health have undertaken little or no benchmarking of the cost of their regulatory services. However, there is scope for this to occur for these two entities and for Agriculture to increase its benchmarking comparisons and to use its cost model to help determine efficient costs. For example:

- as noted, AMSA plans to compare budgets and forecasts to a domestic and an international regulatory body that provide similar charging activities, such as the Civil Aviation Safety Authority and Maritime NZ on the basis that they provide similar services to those of AMSA;
- the 2015 benchmarking study commissioned by Agriculture noted that, through its consultations, several departments were interested in resource optimisation and it recommended that Agriculture leverage this interest by creating working groups and continually benchmarking progress against like agencies; and
- many of the services provided by the three entities, such as inspections, although related to different regulatory activities, are similar and therefore could be benchmarked across entities. For example, there is the opportunity to benchmark the full daily and hourly costs by APS classification (for example, APS 1 to 6 and EL 1 to 2) across all entities and efficiency rates (how long it takes to complete tasks) across entities with similar tasks. This suggests an opportunity for collaboration between entities in benchmarking some costs of their regulatory activities and reviewing why some activities take longer than others. It is suggested that the Department of Finance examine opportunities explore how benchmarking of regulatory activities can be further encouraged and facilitated.

Recommendations

Recommendation no.3

3.61 The Australian Maritime Safety Authority:

- (a) as part of its planned review of its charging arrangements following the introduction of the National System, examines the use of tonnage-based proxies for its levies to enable charges to be closely linked to the level of efficient regulatory effort expended for the specific outputs;
- (b) develops a cost recovery model that aligns revenues of outputs within regulatory activities to the efficient cost of providing those outputs;
- (c) reviews charges for regulatory activities covered by the Regulatory Functions Levy and the Marine Navigation Levy to enable alignment of the costs and revenues under each levy arrangement;
- (d) examines ways to reduce the cost of providing its fee-based services; and
- (e) seeks a decision from the government on how the cost of its fee-based services should be met if it cannot fully recover the cost of these services.

Australian Maritime Safety Authority: Agreed.

3.62 AMSA's responses to each sub-recommendation are as follows:

- (a) *We will review the processes in relation to aligning the level of effort in regulatory activities to the levy charging structure, levy collection operations, and associated costs of administration.*
- (b) *AMSA is exploring options to improve cost recovery modelling techniques, including a review of allocation methodology across all activities, alignment of costs and revenue to individual outputs, and developing more accurate cost drivers for corporate functional costs.*
- (c) *AMSA will review the regulatory charging mechanisms as part of a broader discussion on the structure of levies. These discussions will also provide inputs for the upcoming review of the domestic commercial vessel regulatory charging activities in 2020–21. As part of this review, AMSA proposes to work with both the Department of Infrastructure, Regional Development and Cities, and the Department of Finance, on the maintenance and utilisation of regulatory charging reserves and incorporate these discussions into its industry stakeholder engagement strategy.*
- (d) *AMSA is in the process of investigating and understanding costs that underpin fee-based activities, as part of the process of continuous improvement to the costing model.*
- (e) *As part of the process in understanding costs for fee-based activities, should AMSA assess that industry cannot fully absorb fully the costs of fee-based activities, AMSA will seek policy decisions from government on how these activities may be funded.*

Recommendation no.4

3.63 The Department of Agriculture and Water Resources:

- (a) uses the current review of its charging arrangements to align the structure of its fees and levies with the Cost Recovery Guidelines; and
- (b) develops a cost recovery model that aligns the prices, expenses and revenues of outputs within regulatory activities to the efficient cost of providing those outputs.

Department of Agriculture and Water Resources: Agreed.

3.64 *The department agrees with Recommendation 4, and will continue to strengthen its approach to alignment of the prices, revenue and expenses to ensure that the department continues to effectively recover the costs of its regulatory functions.*

3.65 *The department advises that a program of work is already underway to review charging arrangements for the cost recovery of the department's export regulatory functions.*

3.66 *As part of this work, the existing cost recovery modelling approach was extensively updated and reviewed in 2017 and 2018, in tandem with discussion with our stakeholders about revised cost recovery arrangements.*

3.67 *The cost recovery arrangement reforms will continue to be included in the department's regular cost recovery and financial results reporting mechanisms. This program of work will include ongoing refinements to the pricing and cost recovery of our regulatory functions.*

Recommendation no.5

3.68 The Department of Health:

- (a) implements a consistent quality assured approach for the collection of staff effort data for use in the cost recovery model of the Therapeutic Goods Administration;
- (b) adjusts charges to reduce cross-subsidisation across industry sectors; and
- (c) further reviews the cross-subsidisation of fee-free services and seeks a decision from the government on how the cost of the services should be met.

Department of Health: Agreed.

3.69 *The department's financial performance for the TGA's cost recovery from 2011–12 to 2017–18 identified an over recovery of costs of \$28.8 million, or an average of \$4.1 million or about 3 per cent of TGA's budget. While most over recovery occurred in two sectors (prescription medicines and medical devices), under recovery was noted in Good Manufacturing Practice (GMP) and blood, blood components and biologicals (Blood) sectors. Most over recovery was largely a result of delayed expenditure because of later than planned implementation of major reform projects while the Medicines and Medical Devices Review was underway. TGA revenue resulting from underlying fees and charges continued to be mostly on budget. The recently revised GMP fee structure and reduced medical devices annual charges were implemented to address under/over recovery of costs and cross-subsidisation. These changes are showing the anticipated positive*

results. A review of fees and charges for the Blood sector has already commenced with a plan to implement any changes to fees and charges for the sector from 2020–21 to address under-recovery.

3.70 The TGA will require a significant future investment in upgrading ICT systems to ensure they are fit for purpose and support future regulatory and industry needs such as improving the traceability of medical devices. Funding will be sourced from these cost recovery provisions.

3.71 The report noted providing certain fee-free services by the TGA is inconsistent with the Cost Recovery Guidelines, however, provision of these services was found to be supported by regulation (which required Ministerial approval) and consistent with the original government policy decision that the TGA's regulatory activities be fully cost recovered. In accordance with the ANAO recommendation, the department will seek a decision from the Government on policy authority and appropriate funding for these fee-free activities.

4. Have the entities engaged stakeholders effectively in their cost recovery activities?

Areas examined

This chapter examines whether AMSA, Agriculture and Health have engaged effectively with stakeholders in the design, planning and implementation of their cost recovery activities.

Conclusion

Each entity regularly engages with stakeholders on cost recovery through industry consultative committees, but none have documented cost recovery engagement strategies. Health has been largely effective in engaging with stakeholders to develop and implement its TGA's cost recovery activities, and has regularly updated the TGA's Cost Recovery Implementation Statements to support this engagement. AMSA and Agriculture have focused on consulting on the introduction of new or revised cost recovery arrangements and have not always updated their Cost Recovery Implementation Statements to support engagement on cost recovery of existing regulatory activities.

Area for improvement

This chapter has one recommendation aimed at the three entities implementing stakeholder engagement strategies for their respective cost recovery arrangements (paragraph 4.10).

Have entities developed and implemented ongoing cost recovery engagement strategies?

None of the three entities have documented ongoing cost recovery engagement strategies. Rather, the entities have stakeholder engagement strategies for specific cost recovery activities and/or have drawn on broader engagement frameworks for the entity. The lack of documented ongoing cost recovery engagement strategies is reflected in little coverage of the issue in the entities' Cost Recovery Implementation Statements. Notwithstanding the lack of a documented strategy, Agriculture and Health have adjusted their consultative arrangements in response to stakeholder feedback. AMSA's stakeholder engagement has focused on implementing the National System and not directly on cost recovery of regulatory functions related to this audit.

Developing and implementing stakeholder engagement strategies

4.1 Effective stakeholder³⁵ engagement is one of the three cost recovery principles outlined in the Cost Recovery Guidelines. The Guidelines state (paragraph 30) that:

Stakeholder involvement will generally result in better design, planning and implementation of government activities. Successful stakeholder engagement is most likely to occur when it is well planned and when government entities enter into meaningful dialogue with stakeholders, consider their views and, where appropriate, take action.

35 Stakeholders include a range of people, groups and organisations, and in particular those subject to the cost recovery charges and their representatives.

4.2 The Cost Recovery Guidelines require an entity to include an engagement strategy on cost recovery in its Cost Recovery Implementation Statement (CRIS), but they do not specify what to include in the strategy. Table 4.1 presents the ANAO's high-level assessment for each entity against the key elements of the Cost Recovery Guidelines that an entity 'must' (mandatory) undertake and 'should' (best practice) consider in developing an approach to stakeholder engagement.³⁶

Table 4.1: ANAO high-level assessment of entity stakeholder engagement strategies

Key element from Cost Recovery Guidelines	AMSA	Agriculture	TGA
Entities should develop an ongoing engagement strategy in consultation with stakeholders (paragraph 31).	▲	▲	▲
The CRIS must include a stakeholder engagement strategy (paragraph 41).	■	■	■

Legend: ◆ = fully met; ▲ = partially met (including where there was no explicit strategy, but elements of a strategy or equivalent arrangements were in place); and ■ = not met.

Source: Cost Recovery Guidelines and ANAO analysis of entity arrangements and documentation.

Australian Maritime Safety Authority

4.3 The ANAO's assessment of AMSA's ongoing stakeholder engagement strategy (Table 4.2) is that AMSA does not have an ongoing stakeholder engagement strategy on cost recovery. AMSA should develop a stakeholder strategy, as required by the Cost Recovery Guidelines, and report on the strategy in annual updated CRISs.

Table 4.2: Ongoing cost recovery stakeholder engagement strategy — AMSA

Element from Cost Recovery Guidelines	Assessment
Entities should develop an ongoing engagement strategy in consultation with stakeholders. ▲	AMSA does not have a documented ongoing stakeholder engagement strategy for its cost recovered activities. However, its 2018–19 corporate plan identifies stakeholder engagement ('collaborating with our community') as a strategic enabler for the organisation. The plan identifies a need for AMSA to continue to review and improve its consultative arrangements, particularly with stakeholders in the National System, but does not indicate a need for improved consultation on cost recovery. AMSA advised the ANAO that stakeholder engagement for its cost recovered regulatory activities forms part of its overall stakeholder engagement and that it uses the <i>Australian Government Guide to Regulation</i> and the <i>Australian Government Best Practice Consultation Guidelines</i> to inform its approach to its consultations with industry. The consultation that AMSA undertook in relation to the National System reflected this approach.

³⁶ The Cost Recovery Guidelines state that entities 'should' develop an ongoing engagement strategy (paragraph 31 — better practice) but 'must' include a stakeholder engagement strategy in the CRIS (paragraph 41 — mandatory). Finance should reconcile this guidance in any review of the Cost Recovery Guidelines.

Element from Cost Recovery Guidelines	Assessment
The CRIS must include a stakeholder engagement strategy. ■	AMSA has published three CRISs relating to ship and seafarer safety, navigation infrastructure and environmental protection in the past four financial years — in 2015–16, 2016–17 and 2018–19. These CRISs included short sections on stakeholder engagement, but did not include a stakeholder engagement strategy, that is, planned engagement on cost recovery.

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: Cost Recovery Guidelines and ANAO analysis of AMSA documentation.

Department of Agriculture and Water Resources

4.4 The ANAO's assessment of Agriculture's ongoing stakeholder engagement strategy (Table 4.3) is that, while Agriculture has not had a comprehensive ongoing stakeholder engagement strategy on cost recovery in place for each year since 2015–16, it has engaged with industry on cost recovery through its industry consultative committees. It also commissioned reviews of several of its cost recovery arrangements, including a review of meat exports within the food exports program. It has also developed an engagement strategy for changes to its cost recovery arrangements that it plans to implement from 2019–20.

Table 4.3: Ongoing cost recovery stakeholder engagement strategy — Agriculture

Element from Cost Recovery Guidelines	Assessment
Entities should develop an ongoing engagement strategy in consultation with stakeholders. ▲	Agriculture has not had a documented ongoing stakeholder engagement strategy in relation to the cost recovered activities covered by the CRIS on food exports certification and has not updated its CRIS since 2015–16 to help facilitate ongoing engagement. However, the department: <ul style="list-style-type: none"> developed a stakeholder engagement and communication plan in 2015 when implementing a major change to its cost recovery arrangements; consulted industry about the terms of reference of the industry consultative committees; consulted industry on independent reviews of cost recovery related to the meat industry; and is currently engaging with industry through its industry consultative committees on the implementation of new cost recovery measures announced in the 2018–19 Budget and has obtained the Minister for Agriculture's agreement to an engagement strategy to support the implementation of cost recovery arrangements for the measures.
The CRIS must include a stakeholder engagement strategy. ■	Agriculture's most recent CRIS for the Food Export Program is for 2015–16. This included an overview section on stakeholder engagement and specific discussion around stakeholder engagement for the four components of the Food Export Program. The focus of the stakeholder engagement section in the CRIS was on stakeholder consultation that had occurred, rather than setting out a strategy for ongoing consultation on cost recovery.

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: Cost Recovery Guidelines and ANAO analysis of Agriculture documentation.

Therapeutic Goods Administration

4.5 The ANAO's assessment of Health's ongoing stakeholder engagement strategy for the TGA and how this is reflected in its CRIS is shown at Table 4.4. While the TGA does not have a specific documented engagement strategy on cost recovery, it applies the department's broader stakeholder engagement framework and has adjusted its consultative arrangements in response to stakeholder feedback.

Table 4.4: Ongoing cost recovery stakeholder engagement strategy — TGA

Element from Cost Recovery Guidelines	Assessment
<p>Entities should develop an ongoing engagement strategy in consultation with stakeholders.</p> <p>▲</p>	<p>Health does not have documented stakeholder engagement strategy specifically in relation to the TGA, but has a department-wide Stakeholder Engagement Framework that the TGA applies. The Framework outlines Health's stakeholder engagement process and other considerations to take into account when engaging with stakeholders. While the Framework does not mandate stakeholder engagement strategies for specific stakeholder engagement activities, the first two steps in the engagement process involve thinking strategically about the engagement and analysing and planning for the engagement. The ANAO identified examples of stakeholder engagement strategies on TGA issues, such as the implementation of reforms arising from the Medicines and Medical Devices Review.</p> <p>While Health does not have a documented engagement strategy on cost recovery for the TGA, it has adjusted its consultative arrangements in response to stakeholder feedback to ensure that industry has an adequate opportunity to engage with it, and does engage extensively with stakeholders (see Table 4.8). Nonetheless, there is scope for Health to develop a specific cost recovery strategy, policy or process that addresses how it will engage with stakeholders to identify opportunities for continuous improvement in terms of its engagement processes. Health has advised the ANAO that it will include details of its planned stakeholder engagement on cost recovery in future TGA CRISs.</p>
<p>The CRIS must include a stakeholder engagement strategy.</p> <p>■</p>	<p>The 2016–17 and 2017–18 CRISs included information about the TGA's approach to stakeholder engagement and on consultation that had occurred on the CRIS. However, these CRISs did not include an engagement strategy, which would have focused on planned future engagement on cost recovery.</p>

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: Cost Recovery Guidelines and ANAO analysis of TGA documentation.

Have entities actively engaged with stakeholders at each stage of the cost recovery framework and considered their views in developing and reviewing cost recovery stakeholder engagement arrangements?

Health has actively and regularly engaged with stakeholders on the TGA's activities through cost recovery policy development, implementation and review stages. AMSA and Agriculture have mainly consulted on new or changed cost recovery activities, although they do regularly engage with industry through their industry consultative committees. There is scope for all

three entities to implement performance measures for consultation on cost recovery to promote continuous improvement of cost recovery stakeholder engagement processes.

Engagement at each stage of the cost recovery framework

4.6 As a cost recovery principle, the Cost Recovery Guidelines state (paragraph 31) that stakeholder engagement should be applied ‘throughout all stages of the cost recovery process, from policy development through to implementation and review’. Table 4.5 presents the key elements from the Cost Recovery Guidelines that an entity ‘must’ (mandatory) undertake and ‘should’ (best practice) consider to achieve successful ongoing stakeholder engagement, and the ANAO’s high-level assessment of each entity.

Table 4.5: Stakeholder engagement at each stage of the cost recovery framework

Element from Cost Recovery Guidelines	AMSA	Agriculture	TGA
Entities should engage actively with stakeholders throughout all stages of the cost recovery process, from policy development through to implementation and review (paragraph 31).	▲	◆	◆
The CRIS: <ul style="list-style-type: none"> • should provide the basis for engagement (paragraph 39); • must include a summary of the most recent engagement (paragraph 104); and • should be checked by stakeholders before it is published (paragraph 121). 	▲	▲	▲
Entities should consider developing performance indicators to measure the effectiveness of stakeholder engagement (paragraph 31).	▲	▲	▲
Entities should revise their stakeholder engagement processes based on feedback (paragraph 31).	■	◆	◆

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: Cost Recovery Guidelines and ANAO analysis of entity documentation.

Australian Maritime Safety Authority

4.7 The ANAO’s assessment of the effectiveness of AMSA’s stakeholder engagement (Table 4.6) is that AMSA has not actively engaged with stakeholders on existing cost recovery activities since 2015–16, but has consulted extensively on cost recovery for the new National System. There is scope for AMSA to develop performance measures on stakeholder engagement on cost recovery, to be more responsive to stakeholder requests for information on cost recovery models and provide greater input to cost recovery processes, including through its CRIS.

Table 4.6: Stakeholder engagement at each stage of the cost recovery framework — AMSA

Element from Cost Recovery Guidelines	Reason for assessment
<p>Active stakeholder engagement</p> <p>▲</p>	<p>AMSA has a range of ongoing consultative bodies in place. In addition to the AMSA Advisory Committee, which is the principal advisory committee, there are 12 AMSA-run consultative bodies and a further 12 external consultative bodies in which AMSA participates, in relation to its regulatory responsibilities.</p> <p>AMSA consulted stakeholders in June 2015 on new and revised charges for marine services and ship registration, which came into effect in 2015–16. It published a discussion paper on its website and directly advised over 30 individuals and organisations about the consultation process. AMSA has not consulted stakeholders on cost recovery related to these services since 2015–16. Its focus has been on consultation relating to the National System.</p> <p>AMSA's website reports 27 stakeholder consultations between June 2016 and June 2018, mainly relating to changes in marine orders, 19 of which had a corresponding consultation feedback report, which outlined the nature of the consultation, the feedback received and AMSA's response. Of these 19 consultations, 18 (95 per cent) led to AMSA making changes in response to stakeholder input.</p> <p>AMSA's approach to consulting with stakeholders on the introduction of the National System was extensive and resulted in a decision by the government to delay the full introduction of cost recovery, and highlights the benefits of early and transparent stakeholder engagement.</p>
<p>Stakeholder engagement on the CRIS</p> <p>▲</p>	<p>The 2015–16 CRIS summarised the stakeholder consultation that occurred, including on new and revised charges for marine services and ship registration. One response was received and AMSA outlined its response to the stakeholder. AMSA has not altered its charges and has not consulted industry on the CRIS for these services since 2015–16.</p>
<p>Performance indicators to measure the effectiveness of stakeholder engagement</p> <p>▲</p>	<p>AMSA does not have performance measures to assess its stakeholder engagement activities on cost recovery. However, at the entity-level, AMSA's performance framework includes measures to assess the effectiveness of its engagement with stakeholders and how the organisation is perceived. AMSA uses three measures based on stakeholder feedback to monitor its overall regulatory performance and stakeholder engagement approach:</p> <ul style="list-style-type: none"> • the level of satisfaction with the service delivered by AMSA's call centre, including whether issues were resolved satisfactorily; • a Regulator Performance Framework Survey that gives stakeholders an opportunity to rate AMSA's performance as a regulator; and • the email campaign read rate regarding domestic vessel communication. <p>AMSA does not have specific measures of the effectiveness of stakeholder engagement for cost recovery activities.</p>
<p>Revise stakeholder engagement processes based on feedback</p> <p>■</p>	<p>AMSA's 2017 biennial stakeholder survey found dissatisfaction by some stakeholders with AMSA's level of engagement on cost recovery. Survey respondents indicated a desire for better industry input on cost recovery and better information on AMSA's cost recovery model. AMSA has not yet made changes to its stakeholder engagement processes in response to this feedback.</p>

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: Cost Recovery Guidelines and ANAO analysis of AMSA documentation.

Department of Agriculture and Water Resources

4.8 The ANAO's assessment of the effectiveness of Agriculture's stakeholder engagement (Table 4.7) shows that Agriculture has consulted extensively with industry through consultative committees and other arrangements, including on cost recovery issues, in developing its CRIS on food exports certification in 2015–16 CRIS and in progressing possible changes to its cost recovery arrangements, including those announced in the 2018–19 Budget. However, the department has not actively engaged with industry at each stage of the cost recovery framework since 2015.

Table 4.7: Stakeholder engagement at each stage of the cost recovery framework — Agriculture and Water Resources

Element from Cost Recovery Guidelines	Reason for assessment
Active stakeholder engagement ◆	Agriculture is currently engaging with industry on changes announced in the 2018–19 Budget and has engaged with industry on the reviews of its cost recovery arrangements, including of meat exports, which it commissioned. Agriculture regularly consults with industry stakeholders on its regulatory responsibilities, including on cost recovery issues, primarily through 13 industry consultative committees (and one industry sub-committee). Of particular relevance to cost recovery on the Food Exports Program are the Export Meat Industry Advisory Committee Finance Subcommittee, the Dairy Export Industry Consultative Committee and the Seafood and Egg Export Consultative Committee. The ANAO's analysis of the meeting minutes show that these committees have discussed a range of issues relating to their respective cost recovered activities.
Stakeholder engagement on the CRIS ▲	Consistent with the Cost Recovery Guidelines, each of the summaries of stakeholder consultation in Agriculture's 2015–16 CRIS on food exports certification outlined: who was consulted and when; their views; and how these views were considered. In relation to food exports, the department engaged with a range of industry and fee payer representatives through the sub-committees of five industry committees. During consultation, some food export industries expressed concern about making significant changes to the food export cost recovery arrangements, which had been substantially reformed in 2011. In this context, the department only proposed minor changes to the food export arrangements for the 2015–16 CRIS. Agriculture has not updated its CRIS since 2015–16.
Performance indicators to measure the effectiveness of stakeholder engagement ▲	Agriculture is subject to the Regulator Performance Framework and has developed measures to assess its performance against the Framework. A number of these measures are about stakeholder engagement, but do not specifically measure stakeholder engagement in relation to cost recovery. In 2016–17, Agriculture reported that it met the key stakeholder engagement performance measures, including that it: <ul style="list-style-type: none"> engaged with stakeholders on potential changes to regulatory policies, practices or service standards; consulted with stakeholders to reduce unnecessary compliance costs; provided its policy area and other agencies regular updates on stakeholder feedback regarding regulatory frameworks; and provided updates to its policy area on its regulatory performance.
Revise stakeholder engagement processes based on feedback	Agriculture is currently seeking feedback on the implementation of changes announced in the 2018–19 Budget and consulted industry on its proposed approach to these consultations. Agriculture also sought industry feedback

Element from Cost Recovery Guidelines	Reason for assessment
◆	on arrangements for consultation on changes in 2015–16 and on the terms of reference of industry consultative committees.

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Source: Cost Recovery Guidelines and ANAO analysis of Agriculture documentation.

Therapeutic Goods Administration

4.9 The ANAO's assessment of the effectiveness of Health's stakeholder engagement for the TGA (Table 4.8) shows that Health regularly consults industry about changes to the TGA's cost recovery arrangements and prices and makes changes to planned arrangements in response to industry feedback. It also regularly updates the TGA's CRIS, which facilitates consultation with industry on cost recovery. The development of performance measures related to the effectiveness of stakeholder consultations on the TGA's cost recovery arrangements would help to ensure ongoing assessment of the effectiveness of this stakeholder engagement.

Table 4.8: Stakeholder engagement at each stage of the cost recovery framework — TGA

Element from Cost Recovery Guidelines	Reason for assessment
Active stakeholder engagement ◆	<p>Health regularly consults stakeholders about proposed changes in charges through levies and fees. Primarily, consultation has been undertaken in February and March each year with nine peak industry bodies. In 2018, consultations were also conducted in December and included an additional four industry bodies. Health also uses other consultation methods, on a case-by-case basis, and other forums to consult and disseminate information regarding cost recovery activities. These include:</p> <ul style="list-style-type: none"> the TGA Consultative Committee for consultation with industry and non-industry bodies involved in the manufacture, use and consumption of therapeutic goods; industry working groups for prescription and non-prescription medicines; and TGA-Industry Working Group on Good Manufacturing Practice, for consultation on matters relating to good manufacturing practice. <p>In addition to the annual consultation undertaken on the CRIS, Health consults with stakeholders when significant changes are proposed in relation to charges, such as to Good Manufacturing Practice charges.</p> <p>Health also provides fee and levy payers with regular opportunities to provide feedback on its regulatory activities more broadly, and lists consultations and reviews on its website.</p>
Stakeholder engagement on the CRIS ▲	<p>The TGA's CRISs for 2016–17, 2017–18 and 2018–19 included information about stakeholder engagement. The level of information did not fully meet the requirements of the Cost Recovery Guidelines, because (with the exception of 2018–19), Health had not summarised the views of stakeholders and its response.</p> <p>No major objections were raised by stakeholders in relation to the proposed increases or new charges in 2016–17, 2017–18 and 2018–19. However, some stakeholders raised concerns about changes to Good Manufacturing Practice charges in the consultations on these changes. Including a summary of stakeholder feedback in the CRIS is a requirement of the Cost Recovery</p>

Element from Cost Recovery Guidelines	Reason for assessment
	<p>Guidelines and may assist Health to achieve more transparent cost recovery arrangements.</p> <p>Health advised that it may provide consultative committees with draft CRISs, but this would not normally occur during bilateral discussions on proposed changes to charges and that it is not practical to provide the CRIS to stakeholders before publication. In July 2018, Health noted that:</p> <p style="padding-left: 40px;">One peak body, representing a small segment of the medical device industry, suggested that we consult with stakeholders on the draft CRIS before the final CRIS is published. In a follow up meeting we had with the Department of Finance, they advised that while consulting on a draft CRIS was considered 'best practice', TGA's consultation processes on the cost recovery matters were considered satisfactory and consistent with its long standing practice.^a</p>
<p>Performance indicators to measure the effectiveness of stakeholder engagement</p> <p>▲</p>	<p>Health uses the Regulator Performance Framework key performance indicators to assess the performance of the TGA's activities subject to cost recovery. These indicators do not specifically relate to the effectiveness of stakeholder engagement on cost recovery, and there would be merit in the TGA developing such measures.</p> <p>In 2016–17, Health reported that it: held over 100 formal stakeholder events and numerous informal events; conducted 31 public consultations and received more than 1600 submissions; and addressed around 180,000 public and industry enquiries through its information lines.</p> <p>As part of its approach to assessing its performance, Health undertakes an annual survey of TGA stakeholders' views of its performance across a range of areas. One of those areas is about 'collaboration, consultation and feedback'. The 2017 survey found that Health had improved against the 2016 survey results in this area, although the survey identified opportunities for ongoing improvement.</p> <p>Ongoing areas for focus indicated by the survey included perceptions around the timeliness of consultation, listening to feedback, providing opportunities for input on key issues and decisions, and providing a range of feedback channels that both seek and share information and collaboration. In response, Health identified a range of actions to improve its stakeholder engagement. These actions included: better planning for Medicines and Medical Devices Review consultations; providing stakeholders with six weeks to respond to consultations; and better sharing across Health of information and insights gained from the TGA's stakeholder engagement activities.</p> <p>At the time of fieldwork for this audit, a draft report of the 2018 survey was available. The draft report showed that survey participants assessed the TGA as performing better compared to 2016 and 2017 in relation to 'collaboration, consultation and feedback'.</p>
<p>Revise stakeholder engagement processes based on feedback</p> <p>◆</p>	<p>The Regulator Performance Framework survey provides Health with an annual opportunity to seek feedback from the TGA's stakeholders on its approach to engagement. Of 25 consultations listed on the TGA website that occurred between 1 January 2017 and 30 September 2018, 14 (70 per cent) led to Health making changes as a result of the consultation.</p> <p>There is also evidence that Health seeks feedback about the TGA's consultation processes, although this appears to be more ad-hoc rather than embedded into stakeholder consultation processes. For example, in July 2018 Health approved changes to the TGA's consultation arrangements in response to industry feedback. These changes included:</p>

Element from Cost Recovery Guidelines	Reason for assessment
	<ul style="list-style-type: none"> • bringing forward the timing of its annual bilateral discussions from February/March to December of the preceding year to provide more planning time for the sponsors; • inviting other industry bodies to consultative meetings, as some smaller peak medical device industry bodies had advised that they had not been consulted on the TGA fees and charges; • providing a minimum 12 months' notice for changes other than indexation; and • enhancing communication to sponsors on fees and charges.

Legend: ◆ = fully met; ▲ = partially met; ■ = not met.

Note a: TGA submission to the Executive of the Health Products Regulation Group in the Department of Health, 9 July 2018, p. 2.

Source: Cost Recovery Guidelines and ANAO analysis of TGA documentation.

Recommendations

Recommendation no.6

4.10 The Australian Maritime Safety Authority, Department of Agriculture and Water Resources and the Department of Health:

- (a) implement ongoing stakeholder engagement strategies for their respective cost recovery arrangements in consultation with stakeholders;
- (b) include these planned engagement strategies in their draft Cost Recovery Implementation Statement each year; and
- (c) include performance measures for engagement on cost recovery in their Cost Recovery Implementation Statements.

Australian Maritime Safety Authority: Agreed.

4.11 *AMSA is exploring options in implementing a specific cost recovery based stakeholder engagement strategy before the publication of its annual CRIS.*

Department of Agriculture and Water Resources: Agreed.

4.12 *The department agrees with Recommendation 6 and will build upon the existing stakeholder engagement arrangements already in place for cost recovered regulatory functions.*

4.13 *The department agrees that stakeholder engagement details can be better documented in the CRISs, and is working to continue to improve the documentation of this engagement process as new CRISs are developed.*

Department of Health: Agreed.

4.14 *The department continues to improve its stakeholder engagement on the TGA's cost recovery, including adjusting its consultative arrangements in response to stakeholder feedback. This included holding bilateral meetings with peak industry bodies much earlier than in previous years, including three additional peak industry bodies as part of these bilateral meetings and releasing a public consultation paper on proposed changes to fees and charges. To further improve the stakeholder engagement on the TGA's cost recovery, the department will be implementing an ongoing stakeholder engagement strategy in addition to including further information in its CRIS, as recommended in the report.*



Grant Hehir
Auditor-General

Canberra ACT
14 May 2019

Appendices

Appendix 1 Entity responses



Australian Government
Australian Maritime Safety Authority

CHIEF EXECUTIVE OFFICER

Mr Grant Hehir
Auditor General
Australian National Audit Office
GPO Box 707
CANBERRA ACT 2601

Dear Mr Hehir

Thank you for the opportunity to respond to the Australian National Audit Office's (ANAO) proposed performance audit report on the *Application of Cost Recovery Principles* (received on 29 March 2019), pursuant to section 19 of the *Auditor-General Act 1997*.

The Australian Maritime Safety Authority (AMSA) welcomes and acknowledges the findings and recommendations presented in this report. The report has provided an important reflection on the approach to the cost recovery process and offered constructive comments on AMSA's cost recovery performance.

As part of continuous improvement, AMSA is committed to enhancing its cost recovery arrangements, as highlighted in the report, which will contribute to our regulatory compliance and strengthen our engagement with stakeholders to achieve our policy outcomes.

Our responses to the individual recommendations are included in the attachment.

Finally, I would like to express an appreciation to ANAO's staff for the professional manner in which this audit was conducted.

Yours sincerely



MICK KINLEY

23 April 2019

Att. (1)

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Australian Government
Department of Agriculture
and Water Resources

ACTING SECRETARY

Mr Grant Hehir
Auditor-General
Australian National Audit Office
19 National Circuit
BARTON ACT 2601

Dear Mr Hehir

Thank you for providing the Department of Agriculture and Water Resources (the department) with the opportunity to comment on the Australian National Audit Office proposed cross-agency audit report on the Application of Cost Recovery Principles.

The department agrees with the three recommendations that relate to this department. The department also notes the broader themes and findings contained in the report, which will support and inform our approach to the application of cost recovery.

The department remains committed to continuous improvement of the cost recovery arrangements in place for its regulatory functions. The recommendations made through this audit will assist us to continue to undertake this important work within the whole of government framework for charging and cost recovery.

The department's summary response, and specific responses to each of the recommendations that relate to this department, are enclosed for publication in the final Report (at **Attachment A** and **Attachment B** respectively).

I would like to thank you and the audit team for the collaborative and professional approach adopted during the audit process, and the audit team's willingness to engage with us. We look forward to the upcoming tabling of the final Report.

Thank you again for the opportunity to comment on the proposed report.

Yours sincerely

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30 April 2019

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Australian Government

Department of Health

Secretary

Mr Grant Hehir
Auditor-General for Australia
Australian National Audit Office
GPO Box 707
CANBERRA ACT 2601

Dear Mr Hehir

Department of Health response to the Proposed Audit Report – Application of Cost Recovery Principles

Thank you for providing the Australian National Audit Office's (ANAO) proposed report pursuant to section 19 of the *Auditor-General Act 1947* on the cross-entity audit of the Application of Cost Recovery Principles. I appreciate the opportunity to respond to the report. A detailed response to the individual recommendations is enclosed.

The following wording is provided for the Summary response:

The Department of Health (the department) welcomes the findings in the report and agrees with the recommendations relating to the TGA's cost recovery activities.

The audit found while each entity had scope to improve the effectiveness of cost recovery arrangements, it was pleasing to note the TGA's cost recovery policies and methodology are largely compliant with the Department of Finance's Cost Recovery Guidelines (CRGs). The department is fully committed to the effective implementation of the requirements set out in the CRGs and has already taken steps to address issues identified in this audit.

The department notes the ANAO has identified specific areas for further focus, including over recovery of costs, authority for fee-free services and the TGA's consultation strategy in the Cost Recovery Implementation Statement (CRIS). Most over recovery occurred in two sectors (prescription medicines and medical devices) as a result of delayed expenditure because of later than planned implementation of major reform projects while the Medicines and Medical Devices Review was underway. TGA revenue resulting from underlying fees and charges continued to be mostly on budget. The TGA will continue to review its fees and charges

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- 2 -

regularly to ensure they are aligned with revenue and costs as closely as possible for each sector. There is a need to provide for investments in updating ICT systems to ensure they meet regulatory needs. The TGA will continue to consult with the industry before any changes are made.

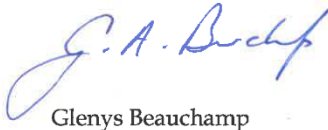
The report noted providing certain fee-free services by the TGA is inconsistent with the CRGs. In accordance with the recommendation in the report, the department will seek a decision from the Government for relevant authority for these services.

The department continues to improve its stakeholder engagement on the TGA's cost recovery, including adjusting its consultative arrangements in response to stakeholder feedback and including the planned stakeholder engagement strategy in the CRIS, as recommended in the report.

I would like to thank the Australian National Audit Office for its professionalism throughout the audit.

If you have any questions regarding the Department's response please contact Narelle Smith, Assistant Secretary, Corporate Assurance Branch on (02) 6289 5342.

Yours sincerely



Glenys Beauchamp

26 April 2019



Australian Government
Department of Finance

Rosemary Huxtable PSM
Secretary

Our Ref: EC19-000364

Mr Grant Hehir
Auditor-General
Australian National Audit Office
GPO Box 707
CANBERRA ACT 2601

Dear Mr Hehir

I refer to the Australian National Audit Office's (ANAO's) correspondence dated 29 March 2019 providing the proposed Audit Report *Application of Cost Recovery Principles* (the Report) pursuant to section 19 of the *Auditor-General Act 1997* and seeking the Department of Finance's (Finance's) response.

Finance's response to the Report is:

Finance agrees with the findings of the Report and notes the relevance of the key learnings to Commonwealth entities. The findings will support continuous improvement by entities in effectively implementing the cost recovery principles.

Finance's response to recommendation 2 of the Report is:

Finance agrees with Recommendation 2, which is being implemented as part of Finance's ongoing work to strengthen guidance in relation to charging across the Commonwealth.

Finance will continue to utilise budget processes and the biennial charging survey to support entities in complying with their requirements.

Thank you for the opportunity to respond to the matters raised in the Report.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'R Huxtable', written over a horizontal line.

Rosemary Huxtable
Secretary

17 April 2019

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Appendix 2 Issues to be examined in a future review of the Cost Recovery Guidelines

Audit report paragraph	Issue
2.3	Clarification of the use of the term in paragraph 33 of the Cost Recovery Guidelines, which requires entities and responsible ministers to obtain government approval for a new cost recovery 'model' or significant changes to a cost recovery 'model', and the cost recovery model used to calculate charges (Stage 2 of the Guidelines).
2.7	Guidance to entities on the timing of reviews of the risk assessments for their cost recovery arrangements.
2.13	Align the wording between paragraph 40 and paragraphs 124 and 125 of the Cost Recovery Guidelines to avoid possible misunderstandings about the timing of updates to the Cost Recovery Implementation Statement.
2.14	Guidance on ministerial approval of updates to a Cost Recovery Implementation Statement.
3.22 to 3.24	Requirement for entities to consider the need for action to prevent any systematic over- or under-recovery of costs, particularly at the program or sector level, as part of the annual Budget process.
3.45	Consideration of the best way of providing independent oversight of entity cost recovery models and the suitability of the models, commensurate with the materiality, complexity and sensitivity of the regulatory charging activity.
3.60	Consideration of how benchmarking of entity regulatory activities can be further encouraged and facilitated.

Appendix 3 Cost model evaluation framework

Criterion	Description
Cost allocation methodology	<p>Are the cost recovery and cost allocation methodology and business rules appropriately documented and do they include all hierarchies (for example, process, cost centres and cost elements), material cost elements, allocation rules, cost drivers, data sources and key assumptions (such as indexation or forecast volume data)?</p> <p>Does the cost recovery methodology explain the rationale for the selected cost drivers for each direct and indirect cost pool (that is, cost centre and cost element)?</p> <p>Are the source data for the cost drivers over the current and forward years readily available? Is an explanation of the expected workload provided (for example, renewal cycles, seasonal demand, peak demand, and the phasing of the transfer of functions from state-based agencies to a national agency)?</p> <p>Is the pricing strategy for fees and charges clearly defined and any material movements from the actual costs calculated in the cost model highlighted (e.g. policy to reduce the barriers to entry for small business)?</p>
Measurement of and attribution of costs to processes and outputs	<p>Does the cost model calculate the full cost of all fees and charges and any budget funded regulatory services?</p> <p>Do all outputs receive an equitable share of indirect costs?</p> <p>Are the cost attribution business rules consistently applied to all outputs?</p> <p>Are direct and indirect cost pools clearly defined?</p> <p>Has the business/service delivery model established to deliver the regulatory services been explained, including an explanation of any outsourced arrangements? In particular, have all processes in delivering the regulatory activity been documented and categorised as regulatory, regulatory support or enabling and appropriately attributed to an output? Descriptions of these categories are as follows:</p> <ul style="list-style-type: none"> • Regulatory — directly responsible for service delivery. • Regulatory support — support for the regulatory activity, such as risk analysis, legal and inquiry teams. • Enabling — typical enabling services include corporate services such as finance, human resource management and IT.
Expected use of drivers to help set charges	<p>Is the use of drivers to set fees and other charges reasonable? This includes the accuracy of staff effort and volume drivers, such as seasonal and peak demand and renewal cycles, and the use of cost pools, consultants, contractors and depreciation.</p> <p>Effort data that are based on management estimates are not evidence-based. Ideally, timesheet data capture should be used to validate all driver data.</p>
Technical	<p>Is the documented cost methodology applied in the cost model with the same standard terminology, master data and business rules for cost allocation?</p> <p>Does the cost model reconcile the nominated control totals (e.g. actual and budget results for a selected financial period) at each stage of the cost attribution process (i.e. input, process and output)?</p> <p>Is version control of the cost model maintained (e.g. last date of update, sign off, and locked cells or outputs)?</p> <p>Are the source data (such as financial, FTE, volume, driver and master data) included in appropriate formats and is clearly identified? Is the source of the data specified (for example, FMIS, HRIS, management estimate, timesheet and business systems)?</p>

Criterion	Description
	<p>Can the cost model be automatically updated by uploading/refreshing the source and driver data?</p> <p>Are the cost driver data regularly updated?</p> <p>Does the cost model have a back-end data base with all data fields to support analysis through drill down and slice and dice functionality?</p>
Reporting	<p>Are the financial and non-financial data presented in the CRIS (for example, fees and charges, revenue and expenses, and volume data) based on a specified version of the cost model (i.e. there is an audit trail)?</p> <p>Does the model provide the ability to track the degree of alignment between expenses and revenue and produce relevant and timely reports for the regulatory activity? Ideally the model should enable an entity to regularly monitor performance against budgeted expenses and revenues.</p> <p>Do the management reports enable a drill-down from outputs to processes and activities and business units, cost pools and FTE, forecast revenue and expenditure for the out years, exception analysis with prior periods and out years, and generate unit costs and prices for the fee schedule?</p>

Source: ANAO.