

The Auditor-General
Audit Report No.10 2000–2001
Performance Audit

AQIS Cost-Recovery Systems

Australian Quarantine and Inspection Service

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Canberra ACT
15 September 2000

Dear Madam President
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Australian Quarantine and Inspection Service in accordance with the authority contained in the *Auditor-General Act 1997*. I present this report of this audit, and the accompanying brochure, to the Parliament. The report is titled *AQIS Cost-recovery Systems*.

Following its tabling in Parliament, the report will be placed on the Australian National Audit Office's Homepage—
<http://www.anao.gov.au>.

Yours sincerely



P. J. Barrett
Auditor-General

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

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For further information contact:
The Publications Manager
Australian National Audit Office
GPO Box 707
Canberra ACT 2601

Telephone (02) 6203 7505
Fax (02) 6203 7798
Email webmaster@anao.gov.au

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Audit Team

Tom Clarke
David Spedding
Eve Martin
Alan Greenslade

Contents

Abbreviations	7
Glossary	8
Summary and recommendations	11
Summary	13
Introduction	13
Audit objective and approach	15
Conclusions	16
Key findings	18
Cost-recovery policy (Chapter 2)	18
Identifying costs (Chapter 3)	18
Recovering costs (Chapter 4)	20
Setting fees and charges (Chapter 5)	21
Managing cross-subsidisation (Chapter 6)	22
Consulting with industry (Chapter 7)	24
Recommendations	25
Audit findings and conclusions	27
1. Introduction	29
Australian Quarantine and Inspection Service	29
Management of cost-recovery	31
Previous reviews	36
The audit	37
Report structure	38
2. AQIS' Cost-Recovery Policy Framework	39
Identifying costs to be recovered	39
Managing cost-recovery outcomes	40
Setting fees and charges	42
Cross subsidisation	45
Articulation and documentation of policy	45
3. Identifying and Attributing Costs	46
Direct and indirect costs	47
Under-estimation of some direct costs	49
Staff costs	51
Attribution of indirect costs	58
Identifying capital costs	61
4. Recovering Costs	62
Cost-recovery performance	62
Recovery of costs in the year they are incurred	65
Under or over-recovery	67
Animal Quarantine Stations	71

5.	Setting Fees and Charges	75
	The nature of fees and charges	75
	Relationship between fees/charges and program costs	77
	Variation in fees for similar services	79
	Relationship between fees and charges for different activities within programs	81
6.	Managing Cross-Subsidisation	84
	Cross-subsidisation	84
	Cross-subsidisation between non-recoverable and recoverable programs	85
	Cross-subsidisation between recoverable programs	85
	Cross-subsidisation between clients	87
	Cross-subsidisation between locations	90
	Conclusion	91
7.	Consulting with Industry	93
	Industry views	93
	Industry consultative committees	94
	Case study: Non-meat EXDOC	95
	Appendices	99
	Appendix 1: AQIS organisation chart at 1 July 2000	101
	Appendix 2: AQIS' cost-recovery financial and information systems	104
	Appendix 3: AQIS recoverable programs trading results for 1998–99	107
	Appendix 4: Summary of AQIS fees and charges at 30 June 1999	108
	Appendix 5: AQIS' Industry Consultative Committees at 30 June 2000	110
	Appendix 6: Previous relevant reviews	111
	Appendix 7: Audit criteria	113
	Appendix 8: Decision tree on response to over or under-recovery	114
	Appendix 9: Cost drivers used to allocate AQIS' indirect costs 1998–99	115
	Appendix 10: Overhead costs attribution 1999–2000	117
	Appendix 11: Recoverable program budgets 1999–2000	119
	Appendix 12: AQIS recoverable program over-recoveries 1993–94 to 1998–99	120
	Appendix 13: IER, RR and II movements 1995–96 to 1998–99 (non-meat programs)	121
	Appendix 14: Legislative basis for AQIS' fees and charges as at 30 June 1999	124
	Appendix 15: Meat Inspection program expenditure and revenue 1997–98 to 1999–2000	126
	Appendix 16: Quarantine and Exports Advisory Council—Review and Evaluation of the AQIS Horticulture Exports program, June 1999	128
	Index	130
	Series Titles	131
	Better Practice Guides	132

Abbreviations

ABFC	AQIS Business and Finance Committee
AFFA	Agriculture, Fisheries and Forestry—Australia
ANAO	Australian National Audit Office
AQIS	Australian Quarantine and Inspection Service
BMS	Budget Management System
CSO	Community Service Obligations
EXDOC	Electronic Export Documentation System
FBT	Fringe Benefits Tax
FCA	Financial Control and Administration
FTE	Full Time Equivalent (Staff)
MASS	Management Accounting Support System
MID	Meat Inspection Division
MoU	Memorandum of Understanding
QEAC	Quarantine and Exports Advisory Council
QEC	Quarantine and Export Certification Divisions
QSP	Quality Software Products (Proprietary Software)
T&Os	Technical and Operational Services

Glossary

Charge (registration and quantity charges)	an impost on clients raised under taxing legislation. To qualify as a tax a charge must be a compulsory extraction by a public authority for a purpose, and not be a payment for services rendered. At least two acts are required, namely an act to impose the tax, and an act to authorise its collection.
Community Service Obligations	services that are provided for the good of the public, the costs of which are met by government.
Cost attribution: Full time equivalent (FTE) numbers	a method of distributing indirect costs to programs. Where costs are allocated on the basis of FTE (staff) numbers, each program's total FTEs are calculated as a percentage of the total FTEs for that indirect cost. It is this percentage of the cost that is attributed to the program.
Cost attribution: Total direct expenditure	a method of distributing indirect costs to programs. Total direct expenditure is the total expenditure of the program less its overheads. Where costs are allocated based on direct expenditure, each target program's total direct costs are calculated as a percentage of the total direct costs for all programs. This percentage is then applied to the indirect costs to attribute them to each program. This methodology assumes, for example, that a program with 50 per cent of the total direct expenditure within AQIS also incurs 50 per cent of the overhead costs.
Cost object	an activity or operation that consumes resources.
Cross-subsidisation	when one group of users pays for more than the cost of the services they receive, and the surplus is used to offset the cost of services provided to other users (who pay less than the cost of the services received).
Direct cost	expenditure that can be economically identified with, and specifically assigned to, a relevant cost object.

Downtime	the periods during paid working hours that recoverable program staff are at work but are not performing chargeable activities, such as performing inspections or serving clients. For example, when there are no clients to serve at the counter.
Fee-for-service	<p>an impost on clients for services rendered raised under fee-for-service legislation. To qualify as a fee-for-service, a number of criteria need to be met, including that:</p> <ul style="list-style-type: none"> • a specific service must be provided; • the service is rendered to or at the request of the party paying the account; and • the impost is proportionate to the cost of the service rendered.
Fixed cost	a cost which remains constant in a given operating range or as the cost drivers change.
Full time equivalent (FTE)	a measure of staffing in which employees are classified as either full-time or as fractions of a full-time equivalent.
Income Equalisation Reserve	an account in which a proportion of over-recovered funds are placed to buffer AQIS and industry from unforeseen events resulting in under-recoveries.
Indirect cost	expenditure, such as overheads and corporate expenses, which cannot be economically identified with a cost object and as a consequence, has to be attributed across a range of cost objects.
Industry Initiative account	an account in which over-recovered funds above the amount to be held in the Income Equalisation Reserve are placed, with the agreement of industry, for use in projects that benefit the industry, such as research, marketing or promotional activities.
Revenue Rebate account	an account in which over-recovered funds above the amount to be held in the Income Equalisation Reserve are placed, with the agreement of industry, pending their return to industry by temporarily applying a predetermined percentage discount on the level of fees applied for services performed by the recoverable program.
Variable cost	a cost that changes with movements in the level of output or as the cost drivers change.

Summary and Recommendations

Summary

Introduction

1. The Australian Quarantine and Inspection Service (AQIS) is part of the Department of Agriculture, Fisheries and Forestry—Australia (AFFA). It is charged with protecting Australia from exotic pests and diseases while helping the international movement of people and providing export certification for agricultural produce and other commodities. As such, its quarantine, export inspection, certification and food safety standards activities are essential to maintaining Australia's animal, plant and human health status and are important elements in the regulatory framework that governs our international trade.

2. AQIS has emphasised that it faces a number of challenges in the environment in which it operates, including the economic volatility of rural export industries that may be impacted by unpredictable events, such as droughts; floods; fires; frosts; pest and disease outbreaks; chemical residue and other food safety concerns; and rapidly changing world economic conditions, such as the Asian Economic crisis.

3. AQIS provides inspection services to clients from a broad commercial and private base, via programs delivered through locations across Australia and overseas.¹ In 1998–99, AQIS' expenditure was \$195 million and it employed 2034 staff (1861 in 1999–2000).

4. AQIS is responsible for quarantine policies and procedures relating to incoming passenger traffic, mail and proposed imports into Australia of animals, plants and their products and a range of other goods that have quarantine significance. AQIS estimates that in 1999–2000:

- 8.8 million international travellers entered Australia and 188 000 items were seized by AQIS from more than 1.9 million passengers at airports;
- 160 million mail articles arrived in Australia, of which some 14 million were parcels and small packets. Some 49 000 articles requiring quarantine action were seized; and
- AQIS supervised 11 600 first-port ship arrivals, and 58 000 first-port aircraft arrivals; and processed 962 000 cargo containers and 4.1 million airfreight consignments.

¹ AQIS has two outputs/outcomes—export certification and quarantine services.

5. AQIS' provision of export certification results in approximately \$10 billion a year of agricultural produce being certified for export as meeting importing countries' health and quarantine conditions. Commodities certified for export include meat, dairy, fish, grains, horticulture, wool, skins, hides and live animals.
6. AQIS has indicated that its market access negotiations resulted in 192 new commodity markets being opened up in the five years to June 2000, as well as improvements in access to 51 markets and maintenance of 107 existing markets that were under threat.
7. Under successive government decisions AQIS has been required to operate at 50 per cent cost-recovery from 1979, 60 per cent from 1 July 1988 and 100 per cent cost-recovery (for recoverable programs only) from 1 January 1991. In addition, since mid 1993, AQIS has been required to recover its full costs on a program-by-program basis, rather than across the organisation as a whole. In essence, this means that AQIS is not able to use a surplus from one program to offset a deficit in another. During 1998–99, AQIS earned \$141 million revenue from 12 cost-recovered programs.
8. About 90 per cent of the revenue for AQIS' recoverable programs is raised under fee-for-service legislation, with most of the remainder coming from establishment registration charges and quantity charges imposed under taxing legislation. This distinction is important in the context of examining AQIS cost-recovery systems.
9. Successive governments have also determined that some AQIS services should be provided free-of-charge. These are services that are viewed as community service obligations, with their costs being met by government. To fund these services, in 1998–99 AQIS received over \$50 million, which constituted about a quarter of its total revenue. The majority of this money funded the non-recoverable Policy and International Division, the Northern Australian Quarantine Strategy and redundancy-related payments associated with the Meat Inspection reform process. However, a small proportion was provided to the recoverable programs to offset costs specifically associated with operating as a government organisation. Subsidies of \$2.7 million were also provided to certain cost-recovered programs, including a component to minimise incentives for smuggling birds and plants into Australia.
10. AQIS' cost-recovery systems have been progressively developed over the last 20 years and have been continuously refined through experience and as a result of a number of internal and external reviews. As such, the systems are relatively mature. AQIS has operated on an accrual accounting basis for many years and, following some revisions implemented in July 1999 to the way it allocates overhead costs, AQIS is

now able to identify its full costs for each program with a reasonable degree of accuracy. AQIS does not consider it is necessary to identify and recover the full costs of each type of service within programs, as long as the total costs of the program are recovered.

11. AQIS has management information which identifies its revenues and costs at a program level, and which enables it to drill down to revenue details for individual service transactions at specific locations. Its systems, however, only provide information on costs at a more aggregated (cost centre) level within programs, with cost centres generally relating to locations rather than to types of services. Accordingly, its systems do not readily provide information on the actual costs of providing each type of service, to assist in setting fees. Instead, AQIS uses estimates of its costs, such as estimated staff usage, to discuss and agree fees and charges with industry.

Audit objective and approach

12. This audit was initiated following advice in June 1999 from the Joint Committee of Public Accounts and Audit that an audit of AQIS' cost-recovery systems was a Parliamentary priority. The objective of the audit was to assess the efficiency and effectiveness of the management of AQIS' cost-recovery systems and provide assurance to the Parliament that the cost-recoverable programs are identifying and recovering the full costs of services provided, without cross-subsidisation. The audit focused on the cost-recoverable programs in operation during 1998–99.² Particular attention was paid to the key areas of: AQIS' cost-recovery policy framework; identifying and attributing costs; recovering costs; setting fees and charges; managing undue cross-subsidisation; and consulting with industry.

13. The audit reviewed all twelve of AQIS' cost-recoverable programs, but focused predominantly on nine, that is, Meat Inspection; Quarantine Import Clearance; Airports; Horticulture Exports and Dried Fruit; Exports Fish and Other Processed Foods; Animal Quarantine Stations; International Mail; Live Animal Exports; and Exports Dairy. The criteria for the audit were based on those for the ANAO's Financial Control and Administration (FCA) Audit on the Costing of Services tabled in December 1998.³ In addition, the audit reviewed whether AQIS had implemented the recommendations included in the management letter from the ANAO to AQIS for that audit.

² A new financial management information system was introduced on 1 July 1999. Due to limited functionality, data for the 1999–2000 financial year was unavailable at the time of the audit.

³ Financial Control and Administration Audit on the Costing of Services (Audit Report No. 21 of 1998–99).

Conclusions

14. The ANAO concluded, overall, that AQIS' cost-recovery systems are mature and stable and, with some exceptions, have delivered near cost-recovery for the AQIS recoverable programs. Notwithstanding this, AQIS' cost-recovery systems contain a number of inherent weaknesses that potentially impair the efficiency and effectiveness of the management of those systems. In particular, as AQIS generally seeks to recover its costs at a recoverable program level, it is not able to sufficiently assure itself, or stakeholders, that the programs are identifying and recovering the full costs of each type of service provided, without not insubstantial cross-subsidisation for some services. More effective cost-recovery systems would seek to achieve a substantial degree of assurance in this regard, whilst recognising that there are practical constraints to this aim in an organisation providing a large number of different services.

15. During the 1990s, AQIS' cost-recovery performance against government requirements varied between programs and over years. Reporting to stakeholders on cost-recovery performance over the long-term has been variable in quality. Based on the data available, the ANAO concluded that, since the requirement for 100 per cent cost-recovery was introduced in 1991, AQIS has recovered about 97 per cent of its overall costs. Almost 98 per cent of overall costs were recovered in 1998–99. However, there have been significant under-recoveries, mainly in the Meat program. As well, in some other programs, AQIS has tended to recover more than its costs.

16. A large proportion of the total funds over-recovered by AQIS have been returned to industry during recent years, but the mechanisms used can be costly to administer and present difficulties in ensuring that those clients who contributed to any surplus receive an equitable share of the proceeds. This demonstrates the importance of AQIS regularly monitoring fee levels and promptly adjusting these where necessary, to minimise the likelihood of program over or under-recoveries. Return of surplus funds has, in some instances, been delayed for a number of years, which should be a matter of concern in a fully cost-recovered situation. AQIS advised that such delays were due to the industries concerned not being able to decide how they wanted the funds used. However, evidence in support of this view was not supplied. Over-recovered funds of around \$5 million were held by AQIS in three different industry reserve accounts at 30 June 1999.

17. In practice, AQIS' systems provide limited assurance of the apportionment of staffing, one of its biggest costs. Some 15 per cent of

staffing costs are attributed to recoverable programs on the basis of a subjective estimate. In addition, staff time spent performing various activities or serving various user groups within programs is not measured. AQIS does make some estimates for major client groupings within three of its programs, but these estimates are not subject to satisfactory verification procedures. Consequently, it has to be concluded that AQIS has limited ability to demonstrate that the fees it charges for particular services within programs relate reasonably to the actual costs of providing those services. Accordingly, the ANAO was unable to assess with any confidence how well the AQIS fees and charges reflected actual costs incurred.

18. The ANAO also concluded that these practices result in some avoidable cross-subsidisation between **clients** within some programs, although the extent is not readily quantifiable. Although AQIS generally seeks to minimise any cross-subsidisation between clients, it has data available that indicates some clients pay more in a fee than the cost to AQIS of providing the service, while others pay less than the cost. This raises issues of equity between clients as well as about transparency of fees and charges.

19. In addition to the cross-subsidisation between clients, the ANAO concluded that there had been some cross-subsidisation between **programs** and also between **locations**. The former arose principally from the method AQIS used for allocating overheads; AQIS has implemented measures to reduce such occurrences from 1999–2000 onwards.

20. The ANAO concluded that AQIS' consultative mechanisms provide a sound framework for the continuous improvement of open communications between AQIS and its clients.

21. This report contains a number of recommendations designed to assist AQIS to improve the efficiency and effectiveness of the management of its cost-recovery systems and to provide greater assurance to stakeholders that it is fully recovering its costs, without avoidable cross-subsidisation and charging fees that are fair and reflect, to the largest possible extent, actual costs incurred.

Key findings

Cost-recovery policy (Chapter 2)

22. Although there is a high-level Memorandum of Understanding with the Department of Finance and Administration which requires AQIS to recover fully the costs of each recoverable program, the ANAO found that AQIS' cost-recovery policies and practices at the operational level were not well promulgated within that latter organisation. For example, there is no authoritative guidance that identifies the costs to be recovered, the time period over which recovery is to be effected, and the method for setting fees and charges (including whether charges should be the same across Australia and the alignment of fees and charges with costs, both between programs and from one year to another).

23. AQIS considers that its cost-recovery policies are based on principles contained in legal advisings and reflected in a generally accepted culture of cost-recovery by management and staff of the recoverable programs. Notwithstanding this view, the ANAO found that a number of cost-recovery practices have evolved within AQIS, many of which are undocumented. In an organisation as diverse as AQIS, documentation for staff and clients of policy and practices on issues as complex as full cost-recovery is vital to ensure proper application, consistency and transparency of the process, and also assists in managing the risks associated with staff turnover.

24. In July 1998, in response to an ANAO audit on the costing of services,⁴ AQIS advised its intention to issue an organisation-wide charging policy document. However, this still has not been issued and there was no clear timetable for its availability.

Identifying costs (Chapter 3)

25. An essential element of an effective cost-recovery system is to be able to identify readily and accurately the costs to be recovered, ideally at any point in time, both from clients' and AQIS' own management effectiveness viewpoint. The ANAO found that, with minor exceptions, AQIS' systems seek to identify the full accrued costs of each recoverable program. AQIS collects costing information at a cost centre level within programs, but does not have accurate information on the costs involved

⁴ Ibid.

in performing each type of service within programs. Although AQIS considers that it is not necessary to cost-recover below the program level, for some programs, that is, the Meat, Quarantine Import Clearance and Grains programs, it estimates the costs attributable to major client groups based on estimated staffing allocations (in the absence of firm data, these estimates are based upon the program managers' knowledge of the area).

26. Staffing is the biggest cost component of the recoverable programs accounting for over \$100 million per annum. The ANAO found that AQIS apportions staffing costs to programs based on estimates of the time officers spend working on those programs. In practice, AQIS' systems provide limited assurance of the accuracy of its program estimates and the apportionment of the staffing costs for the 15 per cent of AQIS' staff who perform services for more than one recoverable program as the subjective staffing attributions are not supported by an effective assurance mechanism which monitors the sensitivity of estimates against cost outcomes.

27. In addition, staff time spent performing various activities or serving various user groups within programs is not measured. AQIS does make some estimates for major client groupings within three of its programs, but these estimates are not subject to satisfactory verification procedures. ANAO therefore considers that AQIS has limited ability to demonstrate that the fees it charges for particular services within programs relate reasonably to the actual costs of providing those services.

28. AQIS identifies its costs for each program through a customised costing methodology that includes direct costs, non-cash costs, and indirect costs. AQIS revised its methodology for attributing overhead (indirect) costs for 1999–2000 onwards, which the ANAO considers will result in more accurate cost attributions. The ANAO also found that, in 1998–99, a number of direct program costs totalling more than \$1.9 million were under-estimated, which contributed to the deficits incurred by some recoverable programs.

29. AQIS has recognised the need to have appropriate performance information to measure chargeable time, and its corollary—downtime. At the time of the audit, this measure was still being developed and results were not available for most programs. However, the indicators available suggested that the measures were not consistent between programs, making comparisons difficult, and that performance over time was variable. This area warrants continued management attention to provide better information on the efficiency of staffing allocations and to assist informed decision making regarding allocation of resources. Accountability, including transparency to clients and other stakeholders, would be enhanced by external reporting of this information.

30. AQIS internally funds its capital acquisitions, which in 1998–99 amounted to some \$5 million. However, the opportunity cost of this capital or notional interest on the funds employed is not identified and reflected in industry charges.

Recovering costs (Chapter 4)

31. Although AQIS reports on some aspects of its cost-recovery performance in its annual *Report to Clients*, more consistent reporting on the cumulative surplus or deficit and the actual percentage of costs recovered each year, both at a program level and for all recoverable programs, would improve accountability, assisting stakeholders to assess performance. AQIS has agreed that reporting to clients can be improved.

32. Changes in the structure of the recoverable programs over time have also made it difficult to ascertain whether AQIS has achieved full cost-recovery for each program over each of the last eight years, as required. Results were mixed, with variations from program-to-program and year-by-year. In total, AQIS appears to have recovered about 97 per cent of its overall costs over this period; almost 98 per cent of overall costs were recovered in 1998–99. However, the ANAO's analysis indicates that, over the last five years in relation to the non-meat programs, AQIS has over-recovered by an average of about four per cent per annum. The level of over-recovered funds held in reserves also evidences this.

33. Over-recovered funds of around \$5 million⁵ were held by AQIS in three different industry reserve accounts at 30 June 1999. The stated purpose of one account, namely the Revenue Rebate account, is to return over-recovered funds to industry in a timely manner through discounts or rebates on fees. The ANAO found that funds in this account had been retained for a number of years rather than being promptly returned by fee discount following over-recovery. The Revenue Rebate account totalled \$2.8 million at 30 June 1999.

34. AQIS advised that the delays in returning funds to clients are due, in part, to its reliance on industry bodies to determine the exact nature of how the returns will be effected. However, evidence in support of this view was not supplied. Review of the balances in the account is suggested as a matter of priority to ensure the revenue rebate policy objective is being achieved with least adverse impact on fee payers.

⁵ Excludes funds for the Ballast Water program of \$1.579 million also held in the Industry Initiative account.

35. The ANAO found that, unlike other recoverable programs, some \$1 million in over-recoveries generated during the five years to 30 June 1999 by the Animal Quarantine Stations has not been returned to industry, and has, instead, been treated as an increase in AQIS' equity. AQIS advised that this is because there is a diversified client base with no easily defined group to which funds could be returned. AQIS also advised that the over-recovered funds will be offset against a significant deficit incurred in 1993–94 and will also be used to offset future capital and maintenance costs incurred by the program. The ANAO considers that, as a general approach, this is not in accordance with sound cost-recovery practice, nor does it generate stakeholder confidence in the system.

Setting fees and charges (Chapter 5)

36. AQIS seeks to recover the cost of the various activities conducted by its recoverable programs through a mix of fees and charges. The distinction between fees and charges is important because their collection is subject to different legal principles. The ANAO found that the basis for imposing two AQIS 'charges' under fee-for-service legislation is uncertain, as they do not appear to relate to the provision of services and are revenue raising in nature. Action to resolve the uncertainties is recommended as a matter of priority at least in fairness to fee payers.

37. Although there is no written policy on the setting of fees and charges, AQIS' principle is for annual charges (such as registration charges) to recover fixed costs (Central Office and Regional Office costs) and fee-for-service revenue to recover variable costs (field costs). While this is a general principle, AQIS does not require its programs to strictly adhere to it where more appropriate arrangements are negotiated with industry.

38. For a variety of reasons, including the different cost structures within programs, and the different nature of products exported by various industry groups, there is variation in fees for similar services across the recoverable programs. For example, the equivalent rate for a half-hour inspection service ranges from \$35 in the Meat program to \$128 in the Live Animal Exports program. It was also noted that some fees were set above or below the estimated cost of the services provided in order to influence industry behaviour. For example, to encourage greater use, in 1998–99 the fee for issuing electronic export certificates was set at a rate below the cost of providing this service, while the fee for manually-issued certificates was set at a level that exceeded the cost. The fee for issuing a replacement certificate was set at a punitive level that was almost 20 times the fee imposed to issue the original certificate.

39. The ANAO considers that, while these practices may provide administrative benefits to AQIS, program management should consider, and keep under review, these decisions having regard to the cost-recovery principle that the fee charged should not exceed the reasonable cost of providing the service.

40. AQIS seeks to set fees-for-service at levels considered appropriate by AQIS and industry; they are not necessarily set with a view to match closely the cost of each type of service provided by a program. The cost of providing one service may be offset by revenue generated by another service within the same program in the same or another industry.

41. As AQIS collects costing information on a program and location basis, it does not have readily available data at an activity level within many of its programs that would enable assessment of the alignment between AQIS' costs and the many different fees it imposes. Further analysis of costs within programs is undertaken by program managers in consultation with industry, using estimates of costs based on the estimated staff utilised on various program activities. This approach is used to discuss and agree fees and charges with industry.

42. AQIS' approach means that the costs borne by individual clients are not necessarily the same as the cost to AQIS of providing the service. Misalignment between activity costs and revenue sources can result in inequitable fees and charges, as a recent joint AQIS/Industry review identified for the Horticulture Exports program.

43. AQIS explained that it seeks to minimise cross-subsidisation between user groups and that its approach recognises the significant cost burden that would be imposed by a system that identified costs for each type of service provided. However, the ANAO considers that appropriate information on the alignment of fees with costs is important in being able to demonstrate that fees bear a reasonable relationship with the costs of the services rendered. The limitations in AQIS' current approach to managing the risk of inequities arising between clients is illustrated in the above example and discussed further below.

Managing cross-subsidisation (Chapter 6)

44. AQIS seeks to prevent cross-subsidisation between programs (use of a surplus from one program to offset a deficit in another program). The ANAO found that AQIS generally has been successful in managing its programs in recent years to avoid direct cross-subsidisation between them. However, the methods used to attribute overheads in 1998–99 and in earlier years resulted in some cross-subsidisation of recoverable programs by non-recoverable programs. In 1998–99 the net cross-subsidy totalled about \$0.65 million. AQIS has revised the basis for allocating

overheads to all AQIS' programs for 1999–2000, which will significantly improve allocation of these costs. Further improvements should follow from a planned review of the allocations of costs for Technical and Operation services.

45. The method used to distribute the interest earned on funds held in AQIS' bank accounts (\$0.36 million in 1998–99) resulted in some programs with large industry reserve account balances subsidising other programs. AQIS advised that it has excluded funds held in industry reserve accounts from the process to distribute interest earned on funds held in AQIS' bank accounts as a disincentive for industry groups to leave funds in the reserve accounts for extended periods of time. This policy is currently under review.

46. Some avoidable cross-subsidisation within the AQIS recoverable programs was found to be occurring at a number of levels, although the extent was not readily quantifiable because of the general absence of data on the actual costs incurred to provide particular types of services. For example, Cargo Risk Management and Entry Management provide a disproportionate amount of revenue in the Quarantine Import Clearance program; and in the Animal Quarantine Stations program, revenue raised from importers of horses, cats and dogs subsidises other client groups.

47. AQIS' practice of limited measurement of the costs of its services and not aligning its fees and charges with its costs at this level means that it is only able to provide limited assurance to clients regarding cross-subsidisation. The ANAO noted AQIS' 1998–99 client satisfaction survey indicates considerable dissatisfaction with its fee and charge rates. The ANAO considers that more can be done to explain the basis for AQIS' fees and charges; more transparent costing information would assist AQIS in this process.

48. AQIS has emphasised that it considers that its current approach meets its legal requirements and is consistent with the approach recognised in the Air Services Australia v Canadian Airlines International Ltd High Court decision. Whilst recognising AQIS' view, the ANAO considers that good practice costing systems seek to identify revenue and costs for different services provided to clients for management purposes where it is cost-effective to do so. It is evident from a number of examples discussed in this report that AQIS has some data available which would assist it to better manage cross-subsidisation below program level. The ANAO considers that AQIS could extend this approach without necessarily incurring substantial additional costs, as well as considering the extent to which modern costing systems offer the opportunity to manage cross-subsidisation to a greater degree than is currently the case in AQIS.

49. AQIS seeks to operate on a system of nationally uniform fee and charge rates. Accordingly, differences between revenue and expenditure at locations will inevitably arise. The ANAO found that this was occurring in two forms within programs, namely, in setting fees for the same services based on national averages of existing fees, and in budgeting for deficit-making locations to be supported by surplus-making locations.

Consulting with industry (Chapter 7)

50. Industry has mixed views about AQIS' cost-recovery systems and is particularly concerned about AQIS' charge rates. The ANAO found that AQIS has developed generally appropriate industry consultative committees for its recoverable programs and that, overall, its consultative mechanisms provide a sound framework for the continuous improvement of open communications between AQIS and its clients.

51. In reviewing the effectiveness of AQIS' consultations with its clients, the ANAO also found that a number of affected industries expressed some dissatisfaction with AQIS' handling of the introduction of the \$4 million redevelopment of the Electronic Export Documentation System.

Recommendations

Set out below are the ANAO's recommendations with report paragraph references and AQIS' abbreviated responses. More detailed responses are shown in the body of the report. The ANAO considers that AQIS should give priority to recommendations 1, 2, 5, and 6.

Policy framework

Recommendation No.1
Para 2.27 The ANAO recommends that, to promote accuracy, consistency and understanding of AQIS cost-recovery, AQIS fully documents its cost-recovery policies and ensures that guidelines developed on budget systems and the budget process are current, for maximum effectiveness.

Response: Agreed.

Identifying costs

Recommendation No.2
Para 3.32 The ANAO recommends that AQIS consider the cost-effectiveness of introducing a system to enable it to determine, and regularly review, the proportion of time spent by staff working on each program, and the different types of activities within programs.

Response: Agreed.

Recovering costs

Recommendation No.3
Para 4.30 The ANAO recommends that, to improve transparency as part of its accountability obligations, AQIS include more comprehensive information in its annual *Reports to Clients* about cost-recovery program performance, including cumulative results in relation to under and over-recoveries.

Response: Agreed.

**Recommendation
No.4
Para 4.41**

The ANAO recommends that, in order to achieve the objective of cost-recovery, AQIS reviews more regularly its fees in relation to the costs incurred for the Animal Quarantine Stations program.

Response: Agreed.

**Setting fees
and charges**

**Recommendation
No.5
Para 5.8**

The ANAO recommends that AQIS review and resolve as necessary, the uncertainties concerning the basis for imposing the 'approved premises registration' imposts under the *Quarantine Act 1908* and the fish 'quantity charges' under the *Export Control Act 1982*. These matters should be kept under review on a regular basis.

Response: Agreed.

**Managing cross-
subsidisation**

**Recommendation
No.6
Para 6.34**

The ANAO recommends that AQIS align fees charged to particular clients with the costs associated with servicing those clients where it is cost-effective to do so. Where this is not feasible, the reasons should be made transparent to relevant stakeholders and kept under review.

Response: Disagree.

Audit Findings and Conclusions

1. Introduction

This chapter provides an overview of the Australian Quarantine and Inspection Service (AQIS) and its cost-recovery systems supporting the programs AQIS delivers. The audit objective, scope, methodology and criteria employed are also discussed.

Australian Quarantine and Inspection Service

Role and functions

1.1 The Australian Quarantine and Inspection Service (AQIS) is part of the Department of Agriculture, Fisheries and Forestry—Australia (AFFA). It was established in October 1986 by amalgamation of the Animal and Plant Quarantine branches of the Australian Agricultural Health and Quarantine Service, the Export Inspection Service (both within the then Department of Primary Industry), and the general quarantine function of the then Department of Health. Appendix 1 shows AQIS' organisational top structure at 1 July 2000, including the divisions examined during the audit.

1.2 AQIS' primary role is to contribute to and administer Australia's quarantine, agriculture and food export laws. The aim of these is to achieve and maintain access for Australian agricultural and food products to hundreds of markets around the world, and to preserve the pest and disease free status of Australia's own animal, plant and fish industries. AQIS' core services are quarantine, inspection and export certification and food safety standards activities.

1.3 The quarantine function relates to the protection of Australia from the entry of exotic pests and diseases arising from the movement of goods and people into this country. AQIS is responsible for quarantine policies and procedures and delivers services regulating incoming passenger traffic, mail and proposed imports into Australia of animals, plants and their products and a range of other goods that have quarantine significance. AQIS estimates that in 1999–2000:

- 8.8 million international travellers entered Australia and 188 000 items were seized by AQIS from more than 1.9 million passengers at airports;
- 160 million mail articles arrived in Australia, of which some 14 million were parcels and small packets. Some 49 000 articles requiring quarantine action were seized; and
- AQIS supervised 11 600 first-port ship arrivals and 58 000 first-port aircraft arrivals; and processed 962 000 cargo containers and 4.1 million airfreight consignments.

1.4 AQIS also provides inspection and export certification for agricultural produce and other commodities. Export certification and market access assistance by AQIS result in approximately \$10 billion a year of agricultural produce being certified for export as meeting importing countries' health and quarantine conditions. Commodities certified for export include meat, dairy, fish, grains, horticulture, wool, skins, hides and live animals.

1.5 AQIS' International Market Access Project supports the increase of Australia's access to export markets by reducing or eliminating technical barriers to trade (such as food safety standards). AQIS has stated that its negotiations resulted in 192 new commodity markets being opened up in the five years to June 2000, as well as improvements in access to 51 markets and maintenance of 107 existing markets that were under threat.

Recoverable and non-recoverable programs

1.6 AQIS and its predecessor bodies have provided a mix of cost-recovered and non cost-recovered services through a range of programs delivered in Australia and overseas. AQIS managed 12 cost-recovered programs during 1998–99, out of a total of about 30 business programs.⁶ In total there were 2034 AQIS staff in 1998–99, of whom 1741 or 85 per cent were in the recoverable programs.⁷

1.7 In 1998–99 AQIS' activities were funded through a combination of government appropriations for Community Service Obligations, and fees and charges imposed on users.⁸

Community Service Obligation activities

1.8 Successive governments have determined that some of AQIS' services should be provided free-of-charge with their costs being met by government.

1.9 To fund these services, in 1998–99 AQIS received over \$50 million, which constituted about a quarter of its total revenue. The majority of this money funded the non-recoverable Policy and International Division and the Northern Australian Quarantine Strategy. However, about \$10 million funded AQIS' surplus staff and redundancy-related payments

⁶ In 1999–2000 the number of recoverable programs increased to 13 with the commencement of the Organic Exports program.

⁷ Staff numbers are average in Full Time Equivalents (FTEs) for 1998–99, and include State/Territory public service staff contracted to provide AQIS services. There was a total of 1861 FTEs in 1999–2000.

⁸ All AQIS' revenue from fees and charges passes through the Consolidated Revenue Fund and an amount equal to the collections is appropriated to fund AQIS' provision of those services.

associated with the Meat Inspection reform process. A small proportion was provided to the recoverable programs to offset costs specifically associated with operating as a government organisation.⁹

Cost-recovered activities

1.10 Under various government decisions, AQIS has been required to recover the costs for most of its activities from users, beginning with 50 per cent cost-recovery from 1979, 60 per cent from 1 July 1988 and 100 per cent cost-recovery for recoverable programs from 1 January 1991. This audit focuses on the systems AQIS has developed to support the government requirement to recover fully the costs of its recoverable programs.

1.11 In 1998–99, AQIS earned over \$141 million in revenue. This was largely from fees and charges, but also includes some \$34 million from other sources, including the passenger movement charge and subsidies.¹⁰

1.12 The government requirement for full cost-recovery is underpinned by a 1994 Memorandum of Understanding (MoU) with the then Department of Finance and a cost-recovery policy framework. In this report we use the term ‘policy’ to refer to AQIS’ administrative policies and operational instructions to implement the government’s decision that AQIS operate on a full cost-recovery basis.

Management of cost-recovery

1.13 AQIS manages its cost-recovery in a devolved framework. Individual program managers are responsible for setting budgets and monitoring program performance against both the budget and the performance indicators in the program’s Business Plans, which cover a two to four year planning horizon. Proposed budgets for program areas are presented to, and approved by, the AQIS Business and Finance Committee (ABFC). Standardised financial reports on program

⁹ Community Service Obligation funds provided to non-recoverable programs are not recovered from industry. In 1998–99 AQIS allocated \$1.087 million non-recoverable Community Service Obligation funds to recoverable programs (\$0.774 million to overhead programs and \$0.313 million to operational programs). Activities related to the Quarantine Review process (Nairn) are jointly funded by Budget funds and cost-recovered funds (1998–99 \$20 million total funding, comprising \$10.3 million cost-recovered funding and \$9.7 million Community Service Obligation funding).

¹⁰ This includes a Government appropriation allocated to AQIS in respect of revenue collected from the passenger movement charge, to fund airport operations (\$18.9 million); subsidies of \$1.4 million for Meat, \$1 million for Post Entry Plant and \$0.3 million for Animal Quarantine Stations, representing a component to minimise incentives for smuggling birds and plants into Australia. The subsidy for Meat was phased out by 30 June 1999. It totalled almost \$38 million comprising: \$6.6 million in 1994–95, \$15.4 million in 1995–96, \$12 million in 1996–97 and \$3.6 million in 1997–98.

performance are also provided to program managers and the ABFC on a four-weekly basis. In addition, program managers provide quarterly reports on performance indicators to the ABFC and the Quarantine and Exports Advisory Council.¹¹

1.14 AQIS program managers and the ABFC conduct formal mid-year reviews of performance against budgets and, after consulting with the respective industry, adjustments are made as necessary to the program's budget, revenue or expenditure.

1.15 As at 30 June 1999, AQIS operated with over 150 different cost centres and around 500¹² revenue codes for its various fees and charges. Its systems enable it to analyse its revenue in considerable detail, including individual service transactions at specific locations, but only provide information on costs at a more aggregated (cost centre) level within programs, with cost centres generally relating to locations rather than to types of services.

1.16 AQIS operated on a single trust account from 1 July 1993 to 30 June 1997. Two separate Reserved Money Fund accounts were maintained from 1 July 1997, one covering the activities of the Meat Inspection Division (MID) and the other covering the remaining activities of AQIS (referred to as the Quarantine and Export Certification Divisions or QEC). However, these arrangements changed with the introduction on 1 July 1999 of devolved banking for Commonwealth agencies. Separate financial statements are prepared for each account and included in the *AFFA Annual Report*.

Budget and financial systems

1.17 AQIS uses a number of systems to manage its cost-recovery activities. A Budget Management System (BMS) has been used to prepare budgets covering the income and expenditure items for recoverable and non-recoverable program areas for several years. BMS was developed in-house and its design rules reflected AQIS' specific cost-recovery framework. Capital acquisitions are dealt with separately from BMS.

1.18 Prior to 1 July 1999, actual revenue and expenditure was recorded on a separate Management Accounting Support System (MASS) which

¹¹ An independent body appointed in 1997 by the then Minister for Primary Industries and Energy to provide advice on major quarantine and export certification policy issues and strategic directions for AQIS.

¹² Although AQIS had about 500 revenue codes, the actual number of different types of services provided is much less than this. For example, one type of service such as inspection of horticulture exports may have numerous codes covering various invoicing arrangements such as for the first half-hour, after first half-hour, daily rate, weekly rate, four-weekly rate, annual rate, together with several different overtime rates.

also contained the budget information transferred from BMS. MASS interacted with the Personnel and Human Resources system; AQIS' operational systems;¹³ and the Commonwealth Public Account.

1.19 MASS was decommissioned on 1 July 1999 following an AFFA Executive Board decision to amalgamate AQIS financial processing functions with those of the rest of the Department and to implement a new financial management information system called QSP.¹⁴ AQIS has decided to replace the BMS and will use a corporate budget system to be developed/purchased by AFFA. For the purposes of this audit, data was extracted from BMS and MASS only, as the QSP system had limited functionality at that time. Appendix 2 provides greater detail of AQIS' operational, financial and information systems, including its 1998–99 and 1999–2000 revenue systems.

Identifying costs

1.20 AQIS identifies its costs through a customised costing methodology. Budgets for the recoverable programs are prepared on a full accrual basis and include direct costs,¹⁵ non-cash costs,¹⁶ and indirect costs.¹⁷

Recovering costs

1.21 Under the MoU with the Department of Finance, AQIS is not required to pay a dividend but is required to recover its full costs on a program basis. In any system of full cost-recovery, inevitably, individual programs will generate revenue recovery that exceeds or falls short of the amount required to deliver services. This can occur as a result of, amongst other factors, the cyclical nature of the industries underpinning AQIS' recoverable programs.

1.22 Under-recoveries are expected by AQIS to be recouped through future revenue collection within the program. Over-recoveries are placed in reserve accounts. Table 1 shows the results of the recoveries for the programs in 1998–99, including amounts carried forward and transfers to and from reserves. Budget and actual trading results for 1998–99 are shown at Appendix 3.

¹³ The AQIS Revenue Unit generated invoices and collected moneys through 14 business systems in 1998-99.

¹⁴ QSP is a proprietary Quality Software Products system and will bring together eleven different financial management information systems across AFFA.

¹⁵ Such as: salaries, payments to suppliers, administrative and property operating costs, staff travel, Fringe Benefits Tax and consumables.

¹⁶ Such as depreciation and accrued long service leave entitlements.

¹⁷ Such as Corporate Costs, Financial Expenses, Overheads, and Technical and Operational Services.

Table 1
1998–99 program results (\$'000)

Recoverable program	Balance Carried Forward¹⁸	Expenditure	Revenue¹⁹	Surplus/ (Deficit) Before Transfers	Transfers from/(to) Reserves²⁰	Carry Over Balance²¹
Meat ²²	(208)	56 027	56 509	482	-	275
Quarantine Import Clearance	-	31 430	28 885	(2 545)	2 545	-
Airports	1 277	21 035	19 306	(1 729)	-	(452)
Grains Exports	-	5 583	6 842	1 259	(1 259)	-
Horticulture Exports & Dried Fruit	(68)	4 728	4 385	(343)	15	(396)
Seaports	-	4 051	3 478	(573)	334	(239)
Exports Fish & Other Processed Food	-	3 459	3 453	(6)	6	-
Animal Quarantine Stations	(7)	2 346	2 713	367	-	360
International Mail	20	1 916	2 162	246	(246)	20
Live Animal Exports	(233)	1 689	1 558	(131)	-	(364)
Post Entry Plant Quarantine	-	1 266	1 255	(11)	11	-
Exports Dairy	-	868	839	(29)	29	-
Other ²³	-	8 360	8 302	(58)	-	(58)
TOTAL	781	142 757	139 687	(3 070)	1 435	(854)

Source: AQIS.

¹⁸ Excludes amounts in reserve accounts.

¹⁹ Includes rebates paid from Revenue Rebate reserve.

²⁰ Excludes rebates paid from Revenue Rebates reserve.

²¹ Excludes deficits written off in Meat program of \$27.945 million and Imported Foods program of \$1.742 million.

²² The Meat program includes AQIS Training Services expenditure of \$1.387 million and revenue of \$1.422 million.

²³ Includes about \$5.83 million payment by Meat Inspection Division to Quarantine and Export Certification Division for corporate services provided. In addition, about \$0.8 million represents a surplus made on accrued long service leave when AQIS staff transferred to AFFA. A further \$0.8 million represents carried forward overspends in overhead areas.

Setting Fees and Charges

1.23 AQIS advised that its cost-recovery policies are based on six principles contained in a legal advice it obtained in 1992. These are discussed in Chapter 2.

1.24 In preparing budgets, program managers take into account the anticipated revenue from fees and charges, as well as any CSO funds, government subsidies and miscellaneous revenue. Most of the revenue for recoverable programs comes from fees and charges. AQIS applies these in line with the program's fees and taxing legislation to recover the costs of its operations. In this report we make the distinction that 'fees' refers to the imposts applied under the fee-for-service legislation and 'charges' refers to the imposts applied under taxing legislation, such as registration charges and quantity charges. However, in administering its recoverable programs, AQIS does not make this distinction.²⁴ As discussed at paragraph 5.6, the ANAO found that some of AQIS' 'charges' are recovered under fee-for-service legislation. During 1998–99 the total revenue generated by the AQIS recoverable programs comprised an average of about 90 per cent from fees and 10 per cent from registration and quantity charges.

1.25 The fees and charges used by each recoverable program reflect the user base, and may include a mix of fixed imposts, such as annual registration charges; quantity levies; documentation charges; and other variable imposts recovered on a fee-for-service basis. In September 1996, AQIS developed charging guidelines designed to promote consistent application of fees and charges across Australia.²⁵ Appendix 4 summarises the fees and charges in operation at 30 June 1999.

Managing cross-subsidisation

1.26 Under the MoU with the Department of Finance, AQIS is required to fully recover the costs of each recoverable program rather than across AQIS as a whole. In essence, this means that it is not able to use a surplus from one program to offset a deficit in another program.

²⁴ AQIS manages its revenues and costs at a program level. Data is collected that enables the separation of revenue into fees and charges, but in practice this is not routinely used for management purposes. Systems do not support the collection of information to enable the separation of respective costs between fees and charges. It was also observed that program staff and documents often interchange terminology when referring to fees and charges.

²⁵ AQIS Charging Guidelines for Quarantine and Inspection programs, 1 September 1996.

Consulting with industry

1.27 AQIS considers that it operates in partnership with industry and aims to provide adequate notice of proposed changes to program expenditures and fees/charges. There are Industry Consultative Committees for all but one of AQIS' programs (see Appendix 5). AQIS advised that each program consults extensively with its Industry Consultative Committee on program budgets, fees and charges and operating results. Program managers are responsible for ensuring that Industry Consultative Committees are aware and advised of any changes in the financial position of their program(s).²⁶

1.28 Full-year results for programs are published in the annual *Report to Clients*. Information is also provided directly to the respective Industry Consultative Committees.

Previous reviews

1.29 There have been a number of reviews over the years that have addressed AQIS' recoverable programs (see Appendix 6).

1.30 In May 1992 the Auditor-General reported the results of an efficiency audit of the Australian Quarantine Inspection Service Quarantine Division (Audit Report No.35 of 1991–92). More recently, a Financial Control and Administration (FCA) audit on the Costing of Services (Audit Report No.21 of 1998–99) included AQIS in an examination of the way public sector organisations process and use information about the cost of their activities.

1.31 The FCA audit covered 10 agencies and, in accordance with normal practice for audits of this nature, the tabled report did not identify the agencies or attribute specific findings to them. The emphasis of the audit was evaluating processes for the identification, capture, accumulation and reporting of cost information in certain key areas of each agency. With respect to AQIS, the evaluation included processes to determine fees and charges to monitor costs in the Seaports; Grains Export; and Post-Entry Animal Quarantine recoverable programs.

1.32 The FCA audit was thus a high level review. At this level of review it found that AQIS had satisfactory procedures relating to the accumulation, reporting and monitoring of cost information and assigning direct costs and allocating costs to the programs examined.

²⁶ Work Instruction May 1998, Adjusting AQIS Quarantine and Non-Meat Export Inspection Fees and Charges.

The audit

Audit objective and scope

1.33 This audit was initiated at the request of the Joint Committee of Public Accounts and Audit. The objective of the audit was to assess the efficiency and effectiveness of the management of AQIS' cost-recovery systems and provide assurance to the Parliament that the AQIS cost-recoverable programs are identifying and recovering the full costs of services provided, without cross-subsidisation. The audit focused on the cost-recoverable programs in operation during 1998–99 and was thus a more in-depth coverage than that undertaken in the above mentioned FCA audit.

1.34 The audit reviewed all 12 of AQIS' cost-recoverable programs, but focused predominantly on nine, that is; Meat Inspection; Quarantine Import Clearance; Airports; Horticulture Exports and Dried Fruit; Exports Fish and Other Processed Foods; Animal Quarantine Stations; International Mail; Live Animals Exports; and Exports Dairy. The nine were chosen based on their material significance and their coverage by previous audit reports.²⁷ The audit also addressed AQIS' action to implement the recommendations in the ANAO's management letter for Audit Report No.21 of 1998–99.

Audit criteria

1.35 The criteria for the audit were based on those for the FCA audit on the Costing of Services, expanded to take into account the nature of AQIS' cost-recovery programs. The criteria are at Appendix 7.

Audit methodology

1.36 The audit methodology comprised:

- background research, including previous audit reports, relevant review and evaluation reports; parliamentary committee inquiry reports; Australian and overseas guidelines;²⁸ and academic works on costing and cost-recovery;
- use of a consultant with recognised expertise in costing to assist with the development of the audit criteria;

²⁷ The FCA audit on the Costing of Services examined the Grains, Seaports and Animal Quarantine Stations programs.

²⁸ The main reference sources included the Department of Finance 1991, *Costing Guidelines* and Management Advisory Board December 1997, *Beyond Bean Counting: Effective Financial Management in the APS—1998 and Beyond*.

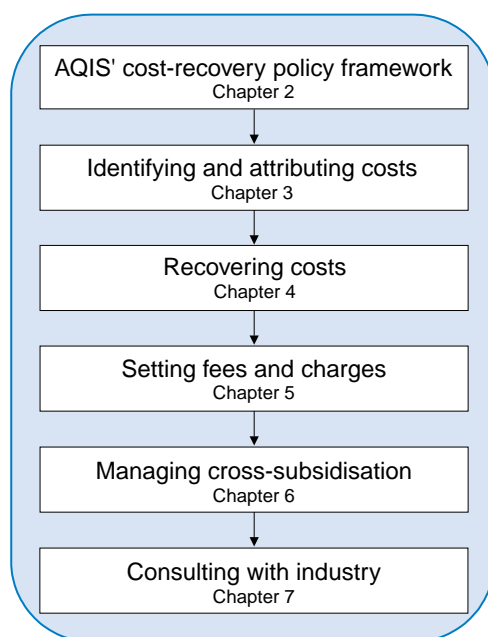
- fieldwork involving testing of the accuracy of costings and appropriateness of the basis for determining user fees and charges, file examinations, inspection of AQIS premises and operations in the New South Wales region and interviews with AQIS regional and central office staff;
- legal advice on issues relating to cost-recovery; and
- consultation with selected stakeholders, such as the Australian Meat Council, the National Meat Association; and a joint representative of the Import Clearance Industry and the Quarantine and Exports Advisory Council.

1.37 The audit was conducted in accordance with ANAO auditing standards. The audit commenced in August 1999, with fieldwork conducted through to December 1999. The cost of the audit was \$380 000.

Report structure

1.38 The report structure is summarised in Figure 1.

Figure 1
Report framework



2. AQIS' Cost-Recovery Policy Framework

This chapter provides an overview of the policy framework through which AQIS delivers its cost-recovered activities. The ANAO found that while AQIS has evolved cost-recovery practices, many of its policies are undocumented, increasing risks of misunderstanding and misapplication.

2.1 Clearly stated policies and procedures are an important element of a full cost-recovery environment, providing guidance to staff administering programs and performing operations in support of the cost-recovery objective.

2.2 AQIS' cost-recovery systems have evolved over the last two decades following the requirement for partial cost-recovery from 1979. This evolution is reflected in a generally accepted culture of cost-recovery.

2.3 This chapter seeks to draw out the key aspects of AQIS' cost-recovery policies and operational instructions with respect to:

- identifying costs to be recovered;
- managing cost-recovery outcomes, in particular under and over-recoveries;
- setting fees and charges; and
- managing any cross-subsidisation.

While AQIS' performance in relation to these aspects of cost-recovery is analysed in later chapters, this chapter makes findings in relation to the clear articulation and documentation of policy.

Identifying costs to be recovered

2.4 AQIS has evolved procedures that, amongst other things, seek to identify all recoverable costs. These procedures include the preparation of business plans and oversighting of the budget process and business performance by the AQIS Business and Finance Committee and collaboration with Industry Consultative Committees, as discussed in Chapter 1.

2.5 AQIS does not have a comprehensive policy document setting out the costs to be recovered in its recoverable programs; however, the 1994 MoU with the then Department of Finance (now Department of Finance and Administration) and the BMS training manual provide some guidance. The MoU requires that AQIS recover the full costs of its

recoverable programs. It describes 'full costs' in only general terms, however, it does specify that this includes:

...interest payable on moneys borrowed from the Commonwealth (this does not include working capital amounts), insurance premiums, depreciation and relevant employee on-costs such as workers compensation premiums and employer superannuation contributions.

2.6 The MoU does not address the method of recovery and the time period over which recovery is to be effected. Some provisions in the MoU are also out of date.²⁹

2.7 The training manual for the BMS provides program managers with guidelines on the various costs to take into account in preparing and entering a program budget into the BMS. However, some gaps were noted in the BMS training material, in particular for those program costs calculated by the Finance section, such as Fringe Benefits Tax (FBT); interest, borrowings and banking; bad and doubtful debts; and depreciation, although these types of costs are included in expenditure against all programs (see paragraph 3.13).

2.8 AQIS has decided to replace the BMS, and will use a corporate budget system to be developed/purchased by AFFA. The ANAO notes that, having regard to the above points, a comprehensive document on cost-identification in the new system will be required to support effective implementation of the system.

Managing cost-recovery outcomes

2.9 AQIS has an undocumented policy of recovering costs in the year that they are incurred (see paragraphs 4.8–4.13). The MoU provides an outline of the expected management of cost-recovery outcomes stating that:

*...charges will be set at a level which will avoid sustained over-recoveries. Where under/over recoveries become evident, subject to Government policy and legislative constraints, immediate action will be taken to adjust charges so that costs are fully recovered on a program basis.*³⁰

2.10 Although AQIS advised that it has had a policy for the management of over and under-recoveries since 1994, it was not until January 1999 that the policy was documented.³¹ AQIS' cost-recovery

²⁹ For example, the MoU refers to agencies that no longer exist, does not address treatment of interest earned on AQIS trust account balances after the first year (1993-94), and does not take into consideration changes to the Commonwealth public sector business environment such as the *Financial Management and Accountability Act 1997* and the introduction of devolved banking.

³⁰ Clause B12.

³¹ AQIS Business and Finance Committee Meeting No. 6/99, Agenda Item No. 1.3.

performance is discussed in Chapter 4 and Appendix 8 sets out the end of year decision process where a program has an unbudgeted under or over-recovery.

Under-recoveries

2.11 AQIS' policy is that under-recoveries are expected to be recouped through future revenue collection within the program. In the non-meat exports areas, for example, AQIS has a policy of triggering a fee/charge adjustment at the point at which it becomes apparent that there is likely to be a gap of 10 per cent or more between program expenditure and revenue by the end of the financial year.

Over-recoveries

2.12 On 30 June 1994, AQIS established what was then called an over-recovery liability account to hold funds that were over-recovered during the year, pending return to industry. At the end of the following year, this was split into three separate accounts, called the Income Equalisation Reserve, Revenue Rebate, and Industry Initiative accounts. These funds are accessible to the program that generated the over-recoveries and are earmarked for:

- buffering AQIS and industry from unforeseen events resulting in under-recoveries (Income Equalisation Reserve);
- temporarily reducing the level of fees/charges applied for services performed by the recoverable program (Revenue Rebate); and
- funding projects that benefit the industry, such as research, marketing or promotional activities, where the industry agrees with AQIS on this course of action (Industry Initiatives).

2.13 AQIS' policy is that where an over-recovery occurs, the surplus funds are first placed in the Income Equalisation Reserve. Initially, a limit of up to five per cent of the level of the program's annual expenditure was set; this was raised with the agreement of industry to 10 per cent from 1997–98. Over-recoveries above the amount retained in the Income Equalisation Reserve are placed in either the Revenue Rebate or Industry Initiative accounts, depending on industry views.

2.14 The January 1999 policy instruction states that amounts in the reserve accounts are industry funds, and that their return to industry is to be undertaken, as far as possible, in a timely manner.

2.15 The policy also specifies that where a deficit has been budgeted, the shortfall should be met in the first instance from the Revenue Rebate and Industry Initiative accounts, where available, and with the agreement of industry. This is to ensure the Income Equalisation Reserve account is available when there is an unplanned shortfall.

Setting fees and charges

2.16 As indicated in the previous chapter, AQIS advised that its cost-recovery policies are based on the six principles contained in a legal advising obtained in 1992, which states that:

The general principles to be applied in determining the level of a fee for service are as follows:

- (i) A charge for a service must not exceed a reasonable share by the 'client' in the total costs of administering the service system.*
- (ii) These total costs can include all direct and indirect costs reasonably attributable to the service system.*
- (iii) In calculating the 'reasonable shares' for 'clients' there is no need to make a precise calculation of the costs attributable to each individual: broad categories of user can be adopted, based on a reasonable commonsense commercial approach, and a common charge determined for each category. On such an approach, some cross-subsidisation of categories is unavoidable, in the sense that some persons would be charged less and others more than if precise apportionment of the costs of service were calculated. Such limited, purely incidental, cross-subsidisation would not result in the charges being taxes. On the other hand, charges for services could be taxes if, on a broad common sense approach, there is a cross-subsidisation of categories of service.*
- (iv) Costs associated with the formulation of policy, including the setting of standards, cannot generally be included in the costs to be recovered as a 'fee' from users of the service system. The High Court would, in general, be likely to regard the setting of standards as being for the general public benefit—contrast the issue of a licence or certificate, which is primarily for the benefit of the person applying for it.*
- (v) The costs relating to enforcement of standards against particular persons in breach, or suspected of being in breach, of the standards (such as surveillance or court proceedings) cannot be recovered from other users of the system. Routine monitoring (such as random testing of samples) is, however, part of the cost of providing the system, and can be included in a 'fee'.*
- (vi) Where part of the cost of a service system is recoverable under a taxing Act, the remainder can validly be recovered as a fee for service.*

2.17 As AQIS' systems provide limited costing information below program level (see paragraph 1.15), in applying the above principles, AQIS uses estimates of its costs, often based on estimated staff utilisation, to discuss and agree fees and charges with Industry Consultative Committees.

2.18 AQIS' charging guidelines provide instructions on how and when to apply particular fees and charges. AQIS advised that the current guidelines, developed in 1996, are in need of updating. A National Consistency Review Committee has been established by AQIS to address this issue. A template for revised charging guidelines was drafted and circulated in July 1999. The proposal is for program areas to complete the template for their program, which will ultimately make up the complete AQIS charging guidelines.

2.19 However, the current charging guidelines and the new template do not provide policy instructions in relation to the setting of fees and charges. In 1998 the ANAO recommended that this be addressed by developing a set of charging principles for use by the recoverable programs in the setting of their fees and charges.³² It was suggested that factors to be considered in setting fees and charges might include:

- circumstances in which fees and charges are set;
- the basis for setting different imposts (including the different basis for hourly rates such as for inspections, and flat rates, such as for certificates);
- outlining what costs are to be included in different fees and charges;
- market strategies (such as demand management and multi-tier pricing);
- providing for the charges to be reviewed; and
- competitive neutrality.

2.20 AQIS accepted the recommendation and advised that its fees and charges were guided by the following principles:

- Equity: charges are set to recover the full costs of providing inspection services to the relevant client group. These costs include all direct and indirect costs reasonably attributable to the activity involving those clients. Implicit is the concept of no cross-subsidisation between client groups;
- Efficiency: charging mechanisms will continue to be developed which enable efficient collection of revenue which recovers the cost of AQIS' operations at the point they can be readily identified and from the direct recipient of those services. These mechanisms will include the minimisation of the risk of 'bad debt' through collection of charges at the time of service delivery, where possible;
- Price stability: charges are set on the basis of achieving cost-recovery with the intention of minimising the frequency and amount of price variations; and

³² Management letter to AQIS for the FCA audit on the Costing of Services.

- Transparency: where possible, expenditure and revenue information is provided to industry representatives at an appropriate level of detail.³³

2.21 AQIS also advised that it would issue an organisation-wide charging policy document. However, the ANAO found that this has still not yet occurred and that there is no timetable for when the document will be available. The above guiding principles also have not been circulated within AQIS. AQIS commented, however, that they are well known within AQIS management, which ensures that they are applied.

Recovery at a program level

2.22 As previously indicated, under its MoU with the then Department of Finance, AQIS is required to set each program's fees and charges to recover fully the costs of that program. AQIS' policy,³⁴ consistent with Government policy, is that each program must recover its costs. While programs are therefore not required to align the amount set for specific fees and charges with the cost of providing the services to which they relate, AQIS does seek to ensure, as far as possible, that fees and charges equate to the cost of providing services.³⁵ The basic principle for program cost-recovery is that fee-for-service applies to the direct costs of providing services while charges in the form of registration or quantity charges are used to recover infrastructure costs. AQIS further stated that it consults extensively with industry in determining program budgets and setting fees and charges, and this process often results in variation from a strict application of the principle. This aspect of cost-recovery management is discussed at paragraphs 5.10–5.13 of this report.

Uniform fees policy

2.23 AQIS has a policy³⁶ to impose nationally uniform fees for particular services within each program. AQIS advised that this was consistent with implied government policy (in that it is similar to the policy of other Commonwealth agencies). AQIS also advised that it is consistent with legal advice that gives discretion to agencies to adopt either uniform or location-based fees;³⁷ reflects the additional costs that would be associated with implementing a general policy of location-based fees; and reflects the difficulties that would be involved in attaining industry agreement to discretionary fees based on location.

³³ AQIS response to the FCA audit on the Costing of Services, 17 July 1998.

³⁴ This policy is undocumented.

³⁵ This policy is undocumented.

³⁶ This policy is undocumented.

³⁷ AQIS obtained a legal opinion in 1992 that indicated there was no impediment to the setting of different rates of fees in different States, regions and localities to reflect more accurately the cost of providing services in those places. This advice was reconfirmed in a legal opinion provided for this audit.

2.24 The implications of this policy for client equity and transparency are discussed in Chapters 5 and 6.

Cross subsidisation

2.25 AQIS advised the ANAO that its systems are designed to reflect its policy of having no cross-subsidisation between programs. The MoU with the Department of Finance provides some guidance on cross-subsidisation, requiring each program to recover its full costs. In essence, this means that AQIS is not able to use a surplus from one program to offset a deficit in another program. However, AQIS does not have a policy on managing any cross-subsidisation that occurs within programs (addressed further in Chapter 6). AQIS advised that a formal policy is unnecessary as cross-subsidisation within programs is managed by each program manager and the respective Industry Consultative Committee.

Articulation and documentation of policy

2.26 AQIS has acknowledged that, notwithstanding the culture of cost-recovery, its key policies are not drawn together through, for example, a cost-recovery manual or other centralised collection of documents to provide support to the cost-recovery operations. The ANAO considers that limited documentation of core agency policies increases the risk of misunderstanding and misapplication. Better practice would include:

- ensuring policy guidance is appropriately disseminated;
- regularly maintaining and updating policy guidance to ensure consistency of current practices;
- ensuring that staff are aware of changes and refinements to existing policy;
- filling in gaps in the administrative policy environment; and
- recording of key government policy decisions driving administrative policies.

Clear documentation would also facilitate ongoing quality assurance and other reviews of the cost-recovery systems and procedures.

Recommendation No.1

2.27 The ANAO recommends that, to promote accuracy, consistency and understanding of AQIS cost-recovery, AQIS fully documents its cost-recovery policies and ensures that guidelines developed on budget systems and the budget process are current, for maximum effectiveness.

AQIS response

2.28 Agreed.

3. Identifying and Attributing Costs

This chapter examines the identification and attribution of AQIS' costs. The ANAO found that there are weaknesses in the identification of some costs.

3.1 Cost is a measure of the value of resources consumed in acquiring or delivering a product or service. The basic principle of cost-recovery is that all elements of cost should be identified and taken into account. The full cost of delivering a service is the sum of all costs, direct and indirect, incurred in delivering the service.³⁸

3.2 An essential element of an effective cost-recovery system is to be able to identify readily and accurately the costs to be recovered, ideally at any point in time, both from clients' and AQIS' own management effectiveness viewpoint. AQIS identifies its costs through a customised costing methodology that traces costs to programs rather than to the range of activities performed by the programs in delivering services.

3.3 The focus of the methodology is on costing at the program level and AQIS considers this approach to be the most cost-effective and efficient method available for an organisation operating in a cost-recovered environment and with a need to justify costs to the industries to which it provides services. However, in the Meat, Quarantine Import Clearance and Grains programs, AQIS further estimates program costs to a lower level, that is, some major client groupings, based on estimated staffing allocations within those programs (in the absence of firm data these estimates are based upon the program managers' knowledge of the area). For example, in the Quarantine Import Clearance program AQIS has revenue, expenditure and surplus or deficit figures for permit issuing, entry management, air and sea cargo and treatments/inspections groupings, which it also reports to industry.

3.4 The ANAO *Better Practice Guide—Building Better Financial Management Support: Functions, systems and activities for producing financial information* states that the choice of costing method, of which there are a number, *rests firmly with management*. However, it does identify Activity Based Costing as a better practice when used instead of, or in conjunction with, other methods in order to strengthen the accuracy of the calculated

³⁸ Australian National Audit Office November 1999, *Better Practice Guide—Building Better Financial Management Support: Functions, systems and activities for producing financial information*, p. 31.

costs and enhance the information for management. Activity Based Costing is directly applicable to the costing requirements of service and government entities and involves the attribution of resource consumption by activities and the allocation of activity costs to cost objects.³⁹

3.5 The ANAO noted that the then Department of Primary Industry stated in its submission to the Joint Committee of Public Accounts 1986 Inquiry into the Administration of Quarantine Services that ... *an activity-based costing system is to be introduced for the 1986–87 financial year*. Following the 1992 performance audit, AQIS indicated that new State reporting arrangements would provide information for determining cross-subsidisation between States for similar services.⁴⁰ However, to date AQIS has not introduced such a system and considers that the costs of doing so would outweigh the benefits. It is further noted, however, that AQIS has not undertaken any cost-benefit analysis to demonstrate this one way or the other.

Direct and indirect costs

Direct costs

3.6 Direct costs are expenses that can be economically identified with, and specifically assigned to, a relevant cost object (program).⁴¹ AQIS' direct cost attribution system is relatively straightforward, with salary costs forming by far the largest single item.

3.7 In setting budgets in BMS, AQIS program managers enter estimated staffing numbers (FTEs), from which the system automatically calculates a range of associated costs.⁴² AQIS advised that budget staff numbers were reviewed annually. Program managers and regional managers also received fortnightly reports at the end of each pay period detailing the staff numbers and salary costs attributed to each program. There is a requirement for these reports to be checked for accuracy with any inconsistencies to be rectified in a timely manner.

3.8 In addition to staffing related costs, program managers also directly entered into BMS any other budgeted program direct costs, such as administrative and property operating costs, staff travel, Fringe Benefits Tax (FBT) and consumables.

³⁹ *Ibid*, pp. 38-42 & 46.

⁴⁰ Audit Report No.35 of 1991-92, pp.102-103.

⁴¹ ANAO 1999, *Op Cit*, pp. 31 & 34.

⁴² Such as provisions for superannuation, higher duties, compensation and long service leave.

Indirect Costs

3.9 Indirect costs are expenses that cannot be economically identified with a cost object (program) and as a consequence, have to be attributed across a range of cost objects.⁴³ Indirect costs within AQIS include:

- corporate expenses that are charged to the organisation as a whole, such as insurance, Central Office rent, internal audit fees and corporate legal costs;
- financial costs, which cover interest, borrowings and banking charges and depreciation on capital items used by more than one program;⁴⁴
- overheads, which are those costs that cannot readily be identified with particular programs and commonly, comprise support services costs for the organisation as a whole. In AQIS, these comprise Finance, Human Resources, Information Technology and Regional Support; and
- Technical and Operational Services (T&Os), which cover the costs for services provided to particular programs within the Quarantine and Exports Division.⁴⁵

3.10 Unlike direct costs, AQIS distributes its indirect costs via a complex and varied methodology. The 'drivers' used for allocating AQIS' indirect costs in 1998–99 are detailed in Appendix 9 and included staff numbers, program expenditure, capital expenditure, computer system usage, and the number of computer workstations.

Proportion of direct and indirect costs

3.11 It is better practice to allocate as many costs as possible as direct costs, since this achieves the most accurate results in identifying costs.⁴⁶ Accordingly, the ANAO analysed the proportion of total costs which were direct costs for AQIS' recoverable programs. The results varied widely in 1998–99, as shown at Table 2, ranging from 92 per cent for the Meat program to 50 per cent for the Exports Dairy program, with an overall average of 83 percent.

⁴³ ANAO 1999, *Op Cit*, pp. 31 & 35.

⁴⁴ Program areas calculate and include in their budgets the depreciation charges for new capital items to be acquired during the year ahead. AQIS' Finance area centrally calculates the depreciation charges for existing capital items and enters details into BMS.

⁴⁵ T&Os include: Training and Quality Assurance; Public Awareness; Director of Quarantine Exports Operation Division; Border Branch Head; Animal and Plant Branch Head; Regional Managers; Registration and Documentation; Detector Dogs; EXDOC non-meat; Phytosanitary; Program Analysis and Support; and Establishment Register.

⁴⁶ ANAO 1999, *Op Cit*, p. 32.

Table 2**1998–99 direct and indirect costs per recoverable program**

<i>Program</i>	<i>Expenditure</i>	<i>Direct Costs</i>	<i>Indirect Costs</i>
	<i>(\$'000)</i>	<i>Per cent</i>	<i>Per cent</i>
Meat	56 027	92	8
Quarantine Import Clearance	31 430	77	23
Airports	21 035	74	26
Grains Exports	5 583	79	21
Horticulture Exports & Dried Fruit	4 728	71	29
Seaports	4 051	82	18
Exports Fish & Other Processed Foods	3 459	74	26
Animal Quarantine Stations	2 346	89	11
International Mail	1 916	68	32
Live Animal Exports	1 689	82	18
Post Entry Plant Quarantine	1 266	83	17
Exports Dairy	868	50	50
TOTAL⁴⁷	134 397	83	17

Source: ANAO analysis of AQIS data

3.12 AQIS advised that the specific variations between some programs reflect differences in the size of programs and their progress in implementing initiatives such as electronic commerce; competitive contracting and tendering; and third party inspection by non-AQIS staff where exporters implement certified quality assurance systems. AQIS does not routinely monitor the ratio of direct to indirect costs, however, AQIS advised that the cost of overheads attributed to AQIS' programs is monitored by the AQIS Business and Finance Committee.

Under-estimation of some direct costs

3.13 In 1998–99 a number of program costs were under-estimated, totalling over \$1.9 million, or about one per cent of total AQIS expenditure. These included FBT; interest, borrowings and banking; bad and doubtful debts; and depreciation. The ANAO was advised that program areas budgeted for these costs based on information received from the Finance Section. Table 3 shows the amounts budgeted, the actual expenditure and the variation between the actual expenditure and the budget for these items for the recoverable programs in 1998–99. The ANAO considers that the under-estimation of these costs compounded the deficits for some recoverable programs and reduced the surpluses for others.

⁴⁷ Excludes \$8.36 million 'other' expenditure (see Table 1).

Table 3

Comparison of 1998–99 budget and actual expenditure for selected items in recoverable programs

<i>Item</i>	<i>Budget (\$)</i>	<i>Actual (\$)</i>	<i>Variation (\$)</i>	<i>Variation per cent</i>
FBT	71 210	378 444	(307 234)	431
Interest borrowings and banking	45 500	211 941	(166 441)	366
Bad and doubtful debts	623 975	1 033 619	(409 644)	66
Depreciation	3 605 024	4 638 188	(1 033 164)	29
TOTAL	4 345 709	6 262 192	(1 916 483)	44

Source: AQIS BMS and MASS Reports.

3.14 AQIS advised that its 1999–2000 budget properly reflects the full costs for these types of expenditure items.

Free-of-charge services

3.15 Services such as accommodation are provided free-of-charge to the Airports program and the International Mail program, by some airports and Australia Post respectively.

3.16 The costs of these services were not consistently disclosed in the programs' financial statements and not included at all in the programs' budgets. The 1998–99 AQIS' financial statements included a note disclosing the Airports program's free-of-charge accommodation (\$0.55 million), but not that of the International Mail program. Neither program included free-of-charge accommodation in its 1998–99 and 1999–2000 budgets or in the results of the programs' operations published in the *AQIS Report to Clients*. AQIS advised that it will be disclosing these costs in its 1999–2000 financial statements.

3.17 Although AQIS' current practices do not affect the actual costs to be recovered, the ANAO considers that the fair value of provision of free-of-charge services should be identified and publicly reported. There is a risk that failure to make transparent the value of services provided free-of-charge to a program in their budgets and financial statements can distort the public and industry perceptions of the full cost of running the program.

3.18 The ANAO suggests that AQIS reflect the value of any services provided free-of-charge in program budgets and expenditure results to ensure that the full cost of recoverable programs is transparent.

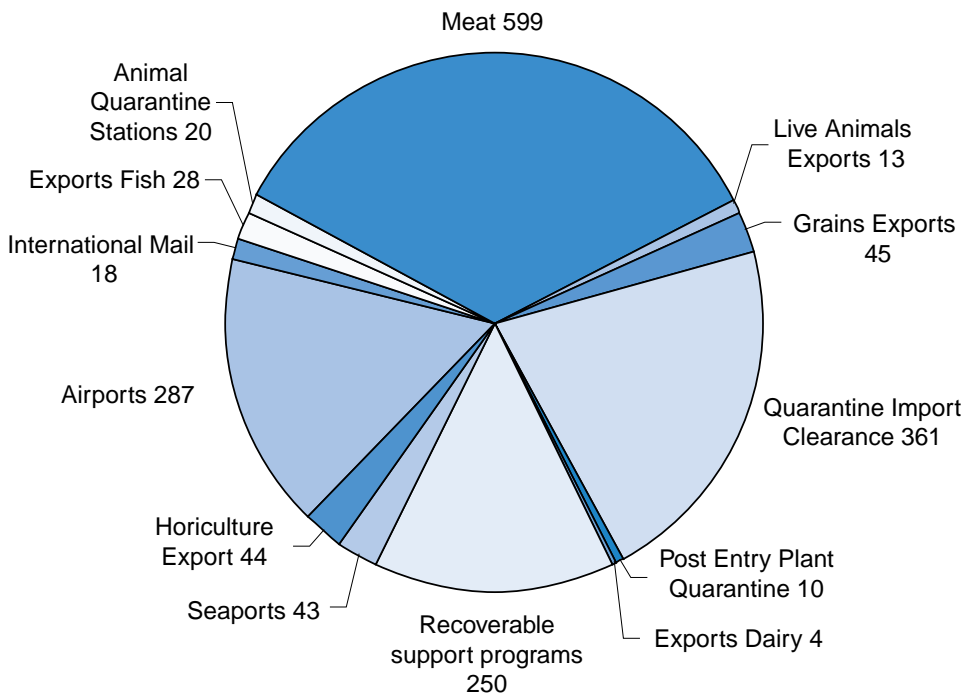
Staff costs

Staffing profile

3.19 Around 85 per cent of AQIS' staff were employed in the recoverable programs in 1998–99. The distribution of staff is illustrated in Figure 2.⁴⁸

Figure 2

Staff in recoverable programs (FTEs)—1998–99



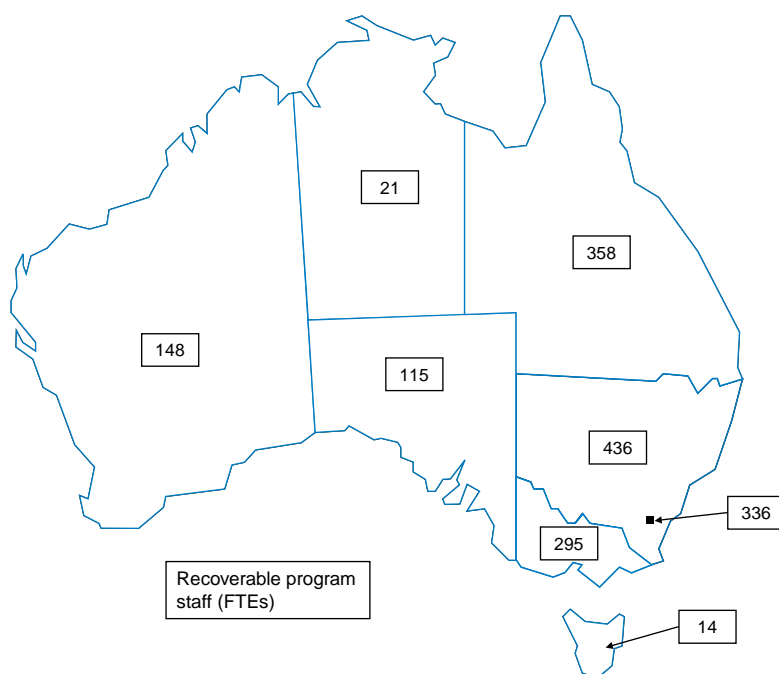
Source: AQIS.

3.20 AQIS delivered its recoverable programs in a range of locations across Australia. Figure 3 shows the location of staff in recoverable programs in 1998–99.

⁴⁸ Figures are average FTEs for the 1998–99 year. Total AQIS FTEs for 1998–99 were 2034, comprising 1723 in the recoverable programs and 311 in the non-recoverable programs. This includes 131 public service staff from Western Australia, Tasmania and Northern Territory contracted to provide services for certain AQIS programs. However it excludes contractors individually engaged by AQIS. There were about 310 Meat Inspection, Grains and Information Technology contractors employed during 1998–99, equating to around 97 FTEs.

Figure 3

Location of recoverable program staff across Australia—30 June 1999



Source: AQIS.

Apportionment of staff costs

3.21 About 70 per cent of AQIS' recoverable program costs relate to the employment of staff.⁴⁹ Accurate apportionment of staffing costs is therefore vital to ensuring that AQIS' programs bear the true cost of their activities, and that fees and charges associated with particular activities are set appropriately.

How AQIS apportions staff costs

3.22 Two methods are used within AQIS to record and attribute staff time to programs. AQIS' Information Technology staff use a task time recording system (EFFIT)⁵⁰ to enable the ready apportionment of the costs of maintaining and operating Information Technology systems and of developing new systems. By contrast, however, staff in the recoverable programs—the great bulk of AQIS' staff costs—do not record the actual time they spend performing various tasks. Instead, staffing costs are charged to recoverable programs based on the number of FTE staff attributed to them. In addition to allocation of staffing costs to programs, AQIS allocates staff costs to major client groups in the Meat, Quarantine Import Clearance and Grains programs using the same methodology.

⁴⁹ Based on 1998-99 salary and associated costs for recoverable programs, including contractors performing AQIS services.

⁵⁰ See Appendix 2.

3.23 AQIS advised the ANAO that recoverable program FTE staff numbers are set during the budget process and that fortnightly FTE reports are provided to both program and regional managers throughout the year. These reports provide detailed information on the number and cost of FTE staff attributed to a program for a pay period. Program and regional managers are responsible for reviewing the reports and preparing, as necessary, appropriate correcting journal entries to reflect actual staffing costs to program areas. This monitoring occurs at program level only, and not for major client groups within programs.

3.24 The ANAO found that practice in monitoring the fortnightly FTE attribution reports varies among AQIS managers. Most compare the total allocation with the budget allocation and only commence action to amend the attribution of staffing costs if a discrepancy is found, while some managers use the reports to check the attribution of each person listed. AQIS issued guidelines in 1996, which required the verification of each fortnightly report,⁵¹ but the ANAO found that all but one of the program managers surveyed were unaware of the guidelines, and all indicated that they did not verify each report.⁵² The ANAO suggests that to promote consistency of practices the guidelines be updated and reissued.

3.25 The ANAO noted that some effort on the part of program and regional managers was required to amend the attribution of FTEs where the reports were considered inaccurate. Requests for journal adjustments and location changes arising from the FTE reports are put to the ledger and systems areas through each branch's Program Analysis and Support Section (for central office staff), and each regional manager (for field staff). Data on the extent of such journal adjustments was not available to the audit.

Implications of AQIS' recoverable program staff apportionment method

3.26 AQIS considers that its systems accurately apportion the salary and associated costs incurred by staff working on its recoverable programs. However, the ANAO found that to function accurately, the system relies on program and regional managers routinely verifying the allocations with staff members, and practice in this regard was variable. Furthermore, there is presently no mechanism that enables staff who share their time between programs to determine the distribution of the time they spend on a program.

⁵¹ Minute to Program Managers and Area Managers 27 March 1996 *Responses to fortnightly FTE reports*. This Minute provided a timetable for checking FTE reports up to 30 June 1996.

⁵² Survey conducted of six AQIS program managers in October 1999.

3.27 Accordingly, the ANAO found that AQIS' systems provide limited assurance of the apportionment of the staffing costs for the 15 per cent of AQIS employees, and the majority of State/Territory employees working for AQIS, that share their time either across recoverable programs or between recoverable and non-recoverable programs.⁵³ The ANAO therefore concludes that, as presently operating, AQIS' systems do not provide assurance of the apportionment of staffing costs to the recoverable programs, as the subjective staffing attributions are not supported by a satisfactory assurance mechanism which monitors the sensitivity of estimates against cost outcomes.

3.28 This issue was also identified in the May 1992 Efficiency Audit conducted by the ANAO. The audit recommended that AQIS introduce time recording procedures whereby accurate details of time spent by inspectors and administrative staff on each program are recorded and analysed. It also suggested that these time records be periodically assessed through surveys and field testing to ensure their accuracy. AQIS responded at the time that its State reporting systems will require these steps, but it also raised practicality constraints on introducing detailed time recording as compared to using approximations such as sampling and estimation techniques.⁵⁴

3.29 As previously indicated, AQIS does allocate staff costs on an estimated basis to some major client groups in a few programs. However, this is not general practice and the groupings are at a high level, so there is limited information on the costs of various services for clients within programs. Furthermore, the allocations made are subjective and not subjected to verification processes, other than review on occasion by Industry Consultative Committee Charging Sub-Committees. The ANAO concludes that AQIS has limited ability to demonstrate that the fees it charges for particular services relate reasonably to the actual staffing costs of providing those services (about \$107 million in 1998–99), because staff time spent performing various activities or serving various user groups within programs, in general, is not measured or subject to a sufficiently robust estimation methodology.

3.30 It is a good business practice for any organisation operating under a cost-recovery regime to have systems in place to allocate accurately key costs such as staffing to recoverable activities. There are a number of mechanisms that AQIS could use to improve the accuracy of its staffing-related cost allocations. In addition to strengthening its current method, options range from introducing a periodic census conducted

⁵³ The ANAO's analysis revealed, for example, that 78 per cent of the Northern Territory's 28 AQIS payees work on more than one recoverable program. Some State/Territory employees are also shared between AQIS programs and non-AQIS (State/Territory) programs.

⁵⁴ Audit Report No.35 of 1991-92, p.103.

once or twice per year for four-week periods (as used by the Australian Customs Service⁵⁵ and is proposed for the AFFA Levies and Revenue Service),⁵⁶ to a full-time recording systems (as used by the AQIS Information Technology section). The choice of mechanism is a matter for AQIS, bearing in mind the relative costs and benefits. A census approach would be a low-cost option, but problematic for much of AQIS' business where there are strong seasonal factors. On the other hand a time recording system has the potential for providing much more comprehensive management information, but would be more costly and possibly more administratively complex.

3.31 The ANAO considers that AQIS should take a more formal approach to defining what costing information it needs at and below the cost-recoverable program level and comparing the costs and benefits of the various mechanisms available for the provision of that information.

Recommendation No.2

3.32 The ANAO recommends that AQIS consider the cost-effectiveness of introducing a system to enable it to determine, and regularly review, the proportion of time spent by staff working on each program, and the different types of activities within programs.

AQIS response

3.33 Agreed. AQIS considers that it already has a highly defensible cost-allocation system which it considers is supported by industry clients. The cost-effectiveness of introducing an alternate system will be reviewed in conjunction with industry.

Downtime

3.34 In a cost-recovery environment, where an organisation sets its staffing levels to meet peak workloads, there will inevitably be some periods when staff are not performing directly chargeable activities. This may be because they are on training, leave, or because there is temporarily no demand by clients for their services; it may also be due to travel to locations and management or preparation time. The cost of this 'downtime' is reflected in overhead costs. Downtime has a significant effect on costs and the calculation of fees and charges. Generally, where there is insufficient flexibility to reduce staffing rapidly in response to decreasing workload, the downtime factor will rise and the fees and charges paid by individual clients will increase.

⁵⁵ Australian National Audit Office, November 1999, *Better Practice Guide—Building a Better Financial Management Framework: Defining, presenting and using financial information*, p.59.

⁵⁶ AFFA Levies and Revenue Service Business Plan 1999-2000 to 2000-2001, p.13. Published in the *Levies and Revenue Service 1998-99 Year in Review*.

3.35 For example, the Meat Inspection Division budgeted for 50 per cent downtime for Area Technical Managers in 1998–99. This is consistent with the May 1992 efficiency audit report on AQIS, which identified that the average downtime for quarantine inspectors during 1990–91 was 50 per cent. This results in the average hourly service rate to industry being significantly increased to compensate for the downtime factor.

3.36 In the past AQIS has not consistently collected and reported information on performance in this area, although three programs did have a chargeable hours indicator. However, AQIS has recognised the need to have appropriate performance information to measure chargeable time, and its corollary—downtime. For the 1999–2000 year, AQIS introduced a mandatory performance indicator to provide data on chargeable activity to be reported quarterly to ABFC.

3.37 At the time of the audit this measure was still being developed and results were not available for most programs. However, the indicators available suggested that the measures were not consistent between programs, making comparisons difficult, and that performance over time was variable.

3.38 This area warrants continued management attention to provide better information on the efficiency of staffing allocations and to assist informed decision making regarding allocation of resources. The ANAO also suggests that accountability, including transparency to clients and other stakeholders, would be enhanced by reporting on the performance targets and the results in the AQIS annual *Report to Clients*.

Corporate on-costs of State/Territory employees

3.39 Under Commonwealth/State agreements, AQIS contracts-in the provision of services for certain AQIS programs.⁵⁷ In 1998–99 there was a total of 131.5 FTEs in Western Australia, the Northern Territory and Tasmania engaged under these arrangements.⁵⁸ These agreements were signed in 1992 and no longer reflect current practices. MoUs have therefore been drafted by AQIS to replace these agreements. There has been slippage in developing these MoUs, which were originally planned to be in place by the end of 1998.⁵⁹

⁵⁷ Programs include Quarantine Import Clearance; Airports; Seaports; International Mail; Horticulture Exports and Dried Fruit; Live Animals Exports; Animal Quarantine Stations; Post Entry Plant Quarantine; and Grains Exports.

⁵⁸ AQIS was unable to advise the ANAO of the actual number of AQIS and State/Territory staff shared between recoverable and CSO-funded programs, the total number of State/Territory staff and the number of State/Territory staff in each location. However, the relevant States and the Northern Territories advised the ANAO that there were 131.5 staff working for AQIS in 1998–99. In 1998–99 AQIS paid \$6.8 million to State/Territory governments in salaries, salary-related costs and corporate support for these staff.

⁵⁹ The MoUs with Western Australia and Tasmania were finalised in late 1999–2000, however, at the time of preparing this report, the MoU with the Northern Territory remained under negotiation.

3.40 Under the current agreements, AQIS pays the State/Territory for the direct cost of the employees engaged under these arrangements to provide AQIS services and also the relevant corporate on-costs charged by the State/Territory. Table 4 illustrates the State/Territory corporate costs incurred by staff in recoverable programs during 1998–99. It demonstrates that there is considerable variance in the State/Territory corporate on-costs paid by AQIS. In 1998–99 these costs averaged \$2697 per FTE in the Northern Territory, whereas the average in Western Australia was \$542 per FTE. Under the existing agreement, Tasmania does not charge any corporate on-costs for its staff performing AQIS services. The variations in the level of on-costs are consistent with previous audit findings. For example, in 1992 the ANAO found that some States were paid proportionately much greater degrees of corporate on-cost support than others.⁶⁰

Table 4

State/Territory on-costs of employees performing AQIS functions during 1998–99

Program	Tasmania		N. Territory		W. Australia		Totals	
	FTE	Cost (\$)	FTE	Cost (\$)	FTE	Cost (\$)	FTE	Cost (\$)
Quarantine Import Clearance	6	-	3	9 405	29	17 726	38	27 131
Airports	1	-	12	28 842	30	11 970	43	40 812
Other	-	-	2	8 778	8	2 727	10	11 505
Grains Exports	-	-	-	-	11	6 712	11	6 712
Horticulture Exports	3	-	1	1 881	5	3 285	9	5 166
Seaports	3	-	4	10 032	6	4 295	13	14 327
International Mail	1	-	-	627	2	855	3	1 482
Live Animals Exports	-	-	2	3 135	2	3 056	4	6 191
Post Entry Plant Quarantine	1	-	-	-	1	337	1	337
Total	14	-	23	62 700	94	50 963	132	113 663

Source: Cost figures based on period 14 reports for programs. FTE numbers provided by States/Territories.

Note: Numbers have been rounded. Other includes T&O functions and CSO funded positions.

3.41 The variations in on-costs provide potential for benchmarking between States and scope for deriving efficiencies, which AQIS may wish to pursue in the context of negotiating the MoUs with the States/Territories.

⁶⁰ Audit Report No.35 of 1991-92, p.18. The audit recommended that AQIS examine whether value for money was being received. AQIS responded that following a review in December 1990, the agreed on-costs for any State would reflect the actual costs of standardised components of on-costs. AQIS noted that on-costs will vary from State to State and therefore while there cannot be an all-embracing national standard there will be consistency and equity between States.

Attribution of indirect costs

3.42 The ANAO found that AQIS revised its methodology for attributing some of its indirect costs for 1999–2000. The ANAO considers that the new methodology will result in more accurate attributions of overhead costs to the recoverable programs.

Revision to cost ‘drivers’

3.43 AQIS attributes indirect costs using a range of ‘drivers’. These include generic drivers, such as staff numbers and proportional program expenditure, as well as more customised drivers such as capital expenditure, computer system usage, and the number of computer workstations. Appendix 9 summarises the drivers used to allocate indirect costs in 1998–99. Before 1 July 1999, AQIS did not allocate overheads to other overhead programs. However, following a review of its methods of allocating overheads, AQIS revised the basis for allocating overheads for 1999–2000 onwards to represent more accurately the usage of indirect services by program areas. Appendix 10 summarises the effect of the introduction of the inter-allocation of overheads and the revised drivers.

3.44 The combined effect of the changes resulted in significant reductions in the overhead allocations for the CSO funded activities and increases to the overhead allocations for the majority of the cost-recovered programs. As shown in Table 5, the programs that were most affected through increased allocations of overhead charges included International Mail; Live Animals Exports; Horticulture Exports; Grains Exports; and Quarantine Import Clearance. The programs receiving substantially reduced overhead charges included AQIS’ non-recoverable programs and the Meat program.

3.45 AQIS advised that its Business and Finance Committee provided program managers with 12 months notice of the change in overhead attribution methodology to ensure full consultation with industry and enable measures to be taken to reduce the impact of the proposed change. For example, by changing the method of collecting revenue, from a system based on sending invoices after the service was provided, to one that encourages the collection of payments up-front or at the time the service is provided.

Table 5

Net impact of overhead allocation changes by program 1998–99 (actual) to 1999–00 (budget)

<i>Program</i>	<i>Net change as a result of inter-overhead allocation (\$'000)</i>	<i>Net change as a result of changes to cost drivers (\$'000)</i>	<i>Total net change in overhead allocation (\$'000)</i>	<i>Percentage Change</i>
Meat	-	-618	-618	-17
Quarantine Import Clearance	-11	1 062	1 051	25
Airports	67	-90	-24	-1
Grains Exports	17	115	132	27
Horticulture Exports & Dried Fruit	7	157	164	32
Seaports	3	32	35	8
Exports Fish & Other Processed Food	2	-13	-11	-3
Animal Quarantine Stations	-	-17	-17	-12
International Mail	3	73	76	40
Live Animals Exports	1	68	69	35
Post Entry Plant Quarantine	1	6	7	4
Exports Dairy	-2	-2	-4	-6
Technical & Operational Services	-55	-44	-99	-6
Software Capitalisation	5	-105	-100	-61
Non recoverable programs	-36	-621	-657	-25

Source: AQIS papers.

Note: Numbers have been rounded.

Attribution of Information Technology costs

3.46 In July 1998 the ANAO recommended⁶¹ that AQIS consider strengthening the methodology used to distribute the costs of the mid-range computer system source pool by:

- attributing the mid-range system costs to program areas using a weighted average;
- reviewing the methodology for the allocation of Information Technology communication costs; and
- reviewing the method of allocating mid-range system costs from support services to recoverable programs.

⁶¹ Management letter to AQIS for the FCA audit on the Costing of Services.

3.47 AQIS implemented the recommended changes for its 1999–2000 budget.

Scope for improvement

3.48 Although AQIS conducted a review of its overhead cost drivers, the ANAO notes that AQIS had also planned to review the basis of allocation of its Technical and Operational Services costs during 1998–99, however, this had not yet occurred at the time of preparation of this report.

3.49 The ANAO considers that further refinements to the overhead cost drivers are desirable. For example, in premises shared by AQIS programs, the method of apportioning rent and property-operating expenses is determined by regional management. These costs are generally apportioned on the basis of staff numbers. It is recognised better practice in cost attribution to seek to apportion these costs in accordance with the area actually occupied by staff, since this provides incentives for managers to use accommodation efficiently or declare any that is surplus to requirements.

3.50 The ANAO noted that accommodation in the New South Wales Regional Office appeared to exceed requirements. AQIS advised that the accommodation surplus reflects the success of the organisation in reducing staff numbers and the difficulty in sub-leasing accommodation that was custom-built for AQIS' requirements, along with the cost of sub-dividing the accommodation to ensure security of AQIS' operations is maintained. The ANAO also noted that industry pays higher fees and charges to cover the costs of excess AQIS accommodation. AQIS commented that the choice of cost driver had no impact on the difficulties involved in subleasing the Sydney accommodation. However, the ANAO ascertained that there had been no attempts by AQIS to identify or sub-lease surplus space in the NSW regional office in recent years. The current lease expires in June 2001.

3.51 AQIS considers the approach for allocating accommodation costs according to staff numbers, is materially accurate since there is generally uniformity of accommodation across programs. AQIS therefore considers its current method is consistent with the ANAO's *Better Practice Guide Building Better Financial Management Support* which states that the cost of establishing the allocation base must be weighed against the benefit in terms of accuracy of the full cost of the objects being costed.

3.52 However, the ANAO found that AQIS has not analysed the benefits of alternative means of allocating accommodation costs. There is some evidence that other approaches may have different allocations,

since the ANAO observed that the accommodation space occupied by staff in each program varied across locations. Other approaches need not be administratively cumbersome, as the Victorian regional office has demonstrated by allocating its costs according to actual space utilised.

Identifying capital costs

3.53 The AQIS approved capital acquisition budget in 1998–99 was \$4.8 million. Under the MoU, AQIS funds its own capital acquisitions. Where its requirements for new capital items exceed its resources, AQIS can submit capital funding bids, along with those of other agencies, for consideration in the normal Budget process. All capital assets held by AQIS are depreciated in accordance with normal commercial practice and this cost is recovered from industry through annual depreciation charges.

3.54 The ANAO observed that the cost of the internal funding of capital acquisitions, such as the opportunity cost of its capital or notional interest on the funds employed, is not identified in AQIS' costing systems. The APS-wide introduction of capital usage charges may affect this matter. The ANAO suggests that AQIS examine this issue to ensure that the full cost of capital is identified and appropriately recovered.

4. Recovering Costs

This chapter examines whether AQIS recovers all its costs, in line with the government decision that it should do so. It looks firstly at the overall cost-recovery performance of AQIS and then analyses the results at a program level. The ANAO found that for a number of programs, revenues have exceeded costs in some years and that accountability could be improved through more comprehensive reporting of AQIS' cost-recovery performance. This chapter also reviews the mechanisms AQIS has developed for returning excess funds to the industries concerned.

Cost-recovery performance

4.1 AQIS has been required to recover from industry the full costs of its recoverable programs since 1 January 1991. Cost-recovery performance since then across all AQIS programs is summarised in Table 6. In total, AQIS appears to have recovered about 97 per cent of its overall costs over this eight-year period. In the first two years AQIS had a marked cost-recovery shortfall—of 10.5 per cent in 1991–92 and 8.8 per cent in 1992–93.⁶² Since 1993–94, when AQIS adopted full accrual accounting and restructured along policy and operational lines, cost-recovery results have presented a more balanced picture. Almost 98 per cent of overall costs were recovered in 1998–99.

Table 6

AQIS percentage of costs recovered 1991–92 to 1998–99⁶³

Year	1991–92	1992–93	1993–94	1994–95	1995–96	1996–97	1997–98	1998–99
Per cent	89.5	91.2	99.0	103.3	96.3	96.3	103.3	97.8

Source: AQIS.⁶⁴

4.2 Table 6 shows the overall result for AQIS, but combining the results for all programs can present a less than complete picture of AQIS' cost-recovery performance, because the figures net-off the various under and over-recoveries between the programs. For example, in 1993–94, although there was a one per cent total shortfall overall, for the first time recoveries exceeded costs in a number of programs. During that year a number of programs recovered more than 150 per cent of their costs.

⁶² AQIS *Report to Clients* 1991–92, p.8. Results for 1992–93 are from the 1993–94 Program Performance Statements, Primary Industries and Energy Portfolio.

⁶³ Based on operating results for recoverable programs after subsidies. Includes transfers from Revenue Rebate account and excludes transfers to and from other reserves. Under-recoveries before 1 July 1994 were Budget funded.

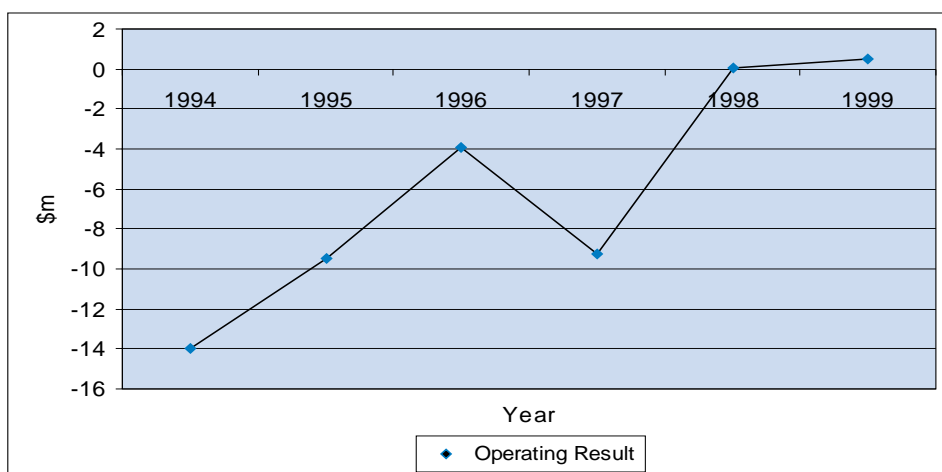
⁶⁴ The ANAO analysis is largely based on trading results published each year in the AQIS *Report to Clients*, taking into account a number of revised figures provided by AQIS. Results for 1992–93 are from the 1993–94 Program Performance Statements as no *Report to Clients* was published for that year. Results for 1998–99 were provided by AQIS as the figures published in the *Report to Clients* were estimates and did not reflect actual results.

4.3 The structure of the recoverable programs is determined by AQIS, in consultation with industry, and there have been a number of changes to the components of the programs over the years. For example, the Other Processed Foods program was recently amalgamated with the Exports Fish program. Such changes have not affected the total costs to be recovered, but do make tracking of the long-term cost-recovery performance of programs a difficult exercise.

4.4 The Meat program is the largest recoverable program, representing about 40 per cent of expenditure in 1998–99. The program has under-recovered its costs over the last six years by \$31.7 million (after government subsidies) or an average of \$5.3 million each year (see Figure 4). On the other hand, other programs combined have recovered an average of almost \$4.3 million per annum more than their costs over the same period (see Figure 5). Most of this over-recovery was attributable to the first two years' results. During the four years from 1995–96 recoveries exceeded costs by an average of \$2.2 million per annum or just over one per cent of 1998–99 expenditure.

Figure 4

Meat program operating results 1993–94 to 1998–99⁶⁵



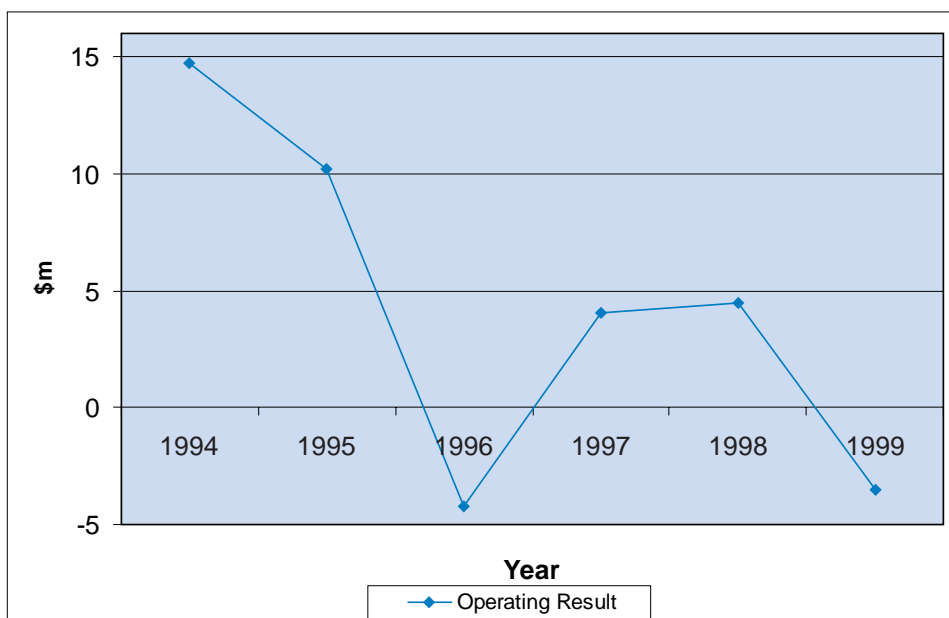
4.5 AQIS advised that the shortfalls and continuing losses in the Meat program until 1997–98 were largely a result of an inability to reduce costs due to rigid and archaic industrial relations arrangements, together with difficulties in addressing the industrial blockages or increasing fees and charges under then Government policies. Almost \$28 million in accumulated losses for the program were 'written off' in 1996–97 and 1997–98. AQIS also advised that, following the extensive reform program introduced by the Government in 1997, the Meat program has recovered 100 per cent of costs over the past two years.⁶⁶

⁶⁵ 1992-93 figures were not available. A deficit of \$11.022 million was incurred in 1991-92.

⁶⁶ The cost-recovery result over the two year period has been achieved with support of Government appropriations in the form of \$5 million in subsidies (phased out in 1999-2000) and \$25 million for redundancies and salary payments for surplus staff.

Figure 5

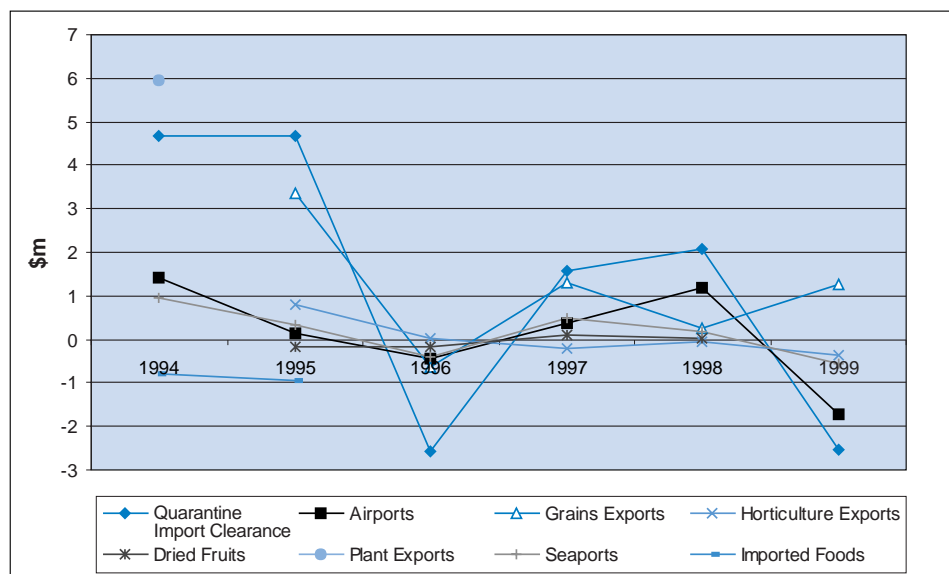
Non-meat programs total operating results 1993–94 to 1998–99⁶⁷



4.6 Operating results for the individual non-meat recoverable programs have varied from year-to-year (see Figure 6A and 6B).

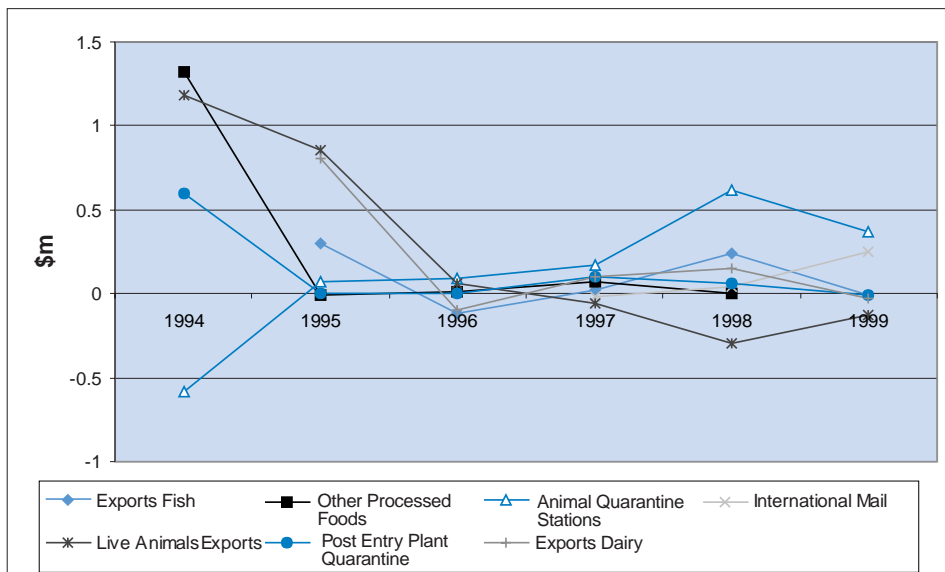
Figure 6A

Non-meat programs operating results 1993–94 to 1998–99⁶⁸



⁶⁷ 1992-93 figures were not available. The programs incurred a total deficit of \$3.6 million in 1991-92.

⁶⁸ In 1993-94 Plant Exports included Grains and Horticulture Exports. Imported Foods was combined with Import Clearance in 1995-96 and the accumulated deficit of \$1.742 million was 'written-off'.

Figure 6B**Non-meat programs operating results 1993–94 to 1998–99⁶⁹**

Source for Figures 4, 5, 6A and 6B: AQIS.

4.7 Figures 4 to 6B show operating results before transfers to and from reserves. As indicated in Chapter 2, since the first significant over-recoveries were made in 1994, AQIS has had a number of mechanisms in place to refund to industry any over-recoveries that exceed certain thresholds. These are further discussed below.

Recovery of costs in the year they are incurred

4.8 The AQIS cost-recovery system is designed so that all budgeted costs are recovered in the year in which they are incurred. Where actual costs exceed the level budgeted, the additional costs are usually recognised in the expenditure accounts for that same year and may result in a reduced program trading result.

4.9 Although overall there was general adherence to this principle, the ANAO found that in 1998–99 AQIS decided to defer the recovery of some \$0.377 million in overhead costs. However, overhead budgets for the following year were reduced by the same amount to effect recovery during 1999–2000. This deferral of recovery was because a number of programs were already running deficits and AQIS considered that it would

⁶⁹ In 1993–94 Processed Food included Fish, Dairy, Dried Fruit and Other Processed Foods. From 1998–99 Other Processed Foods was included in the Fish program. International Mail became a recoverable program from 1996–97.

have been unfair to load additional costs onto the programs that were outside the control of the respective program managers. As discussed in Chapter 7, some costs for the redevelopment of the EXDOC system⁷⁰ were also deferred.

4.10 The ANAO suggests that transparency and accountability would be improved for all stakeholders by including disclosure of decisions such as the deferral until future years of the recovery of some costs in AQIS publications of the financial performance of the recoverable programs, in order to ensure that the underlying level of program deficits is not understated.

4.11 AQIS advised that it considers such disclosure is unnecessary due to the immaterial nature of the adjustments and the discussion of these decisions with industry through the Industry Consultative Committees.

4.12 The ANAO also observed that programs are sometimes budgeted to over-recover costs in a year. This is with the agreement of industry, in order: to top-up the funds in the Income Equalisation Reserve; to recover prior year losses; or to meet anticipated cost increases. For example, the Quarantine Import Clearance program budgeted for a small surplus of \$0.14 million or 0.4 per cent in 1999–2000 in order to top-up its Income Equalisation Reserve; the Seaports program budgeted for a surplus of \$0.24 million or 5.9 per cent, in order to recover a 1998–99 deficit; and the Exports Fish program budgeted for a 3.8 per cent surplus in 1998–99, in order to spread the anticipated costs for the introduction of the EXDOC system over a longer period. (Appendix 11 shows details of 1999–2000 budgets for AQIS' recoverable programs).

4.13 AQIS obtained legal advice that questions the validity of setting fees within a cost-recovery environment that are designed to build up reserves or recover prior year losses.⁷¹ In particular, these practices raise a number of equity issues, as clients who use AQIS' services in any particular year may be subsidising past or future users. AQIS' considers, however, that a legal challenge is unlikely given that industry consents to these arrangements.

⁷⁰ Electronic Export Documentation system.

⁷¹ Legal advice was obtained by AQIS in 1992 and was reconfirmed in 1993 and again in 1994. Such practices are possible under taxing legislation, but there are practical limitations because AQIS would need to show that any over-recovery for a program arose purely from charges under taxing legislation and not from fees for services.

Under or over-recovery

Performance over time

4.14 Examination of operating results in isolation does not provide an accurate view on whether AQIS is under or over-recovering its costs in the long term, both in total and at a program level. Appendix 12 summarises the over-recoveries by program for the period 1993–94 to 1998–99. It shows that although AQIS has over-recovered more than \$39 million in the six years to 30 June 1999, much of this has also been returned to industry through a combination of offsetting deficits against Income Equalisation Reserves; Revenue Rebates; and Industry Initiatives. It also shows that, of the \$16 million over-recovered in 1993–94 from non-meat programs, some \$3.3 million was used to subsidise the Meat program.

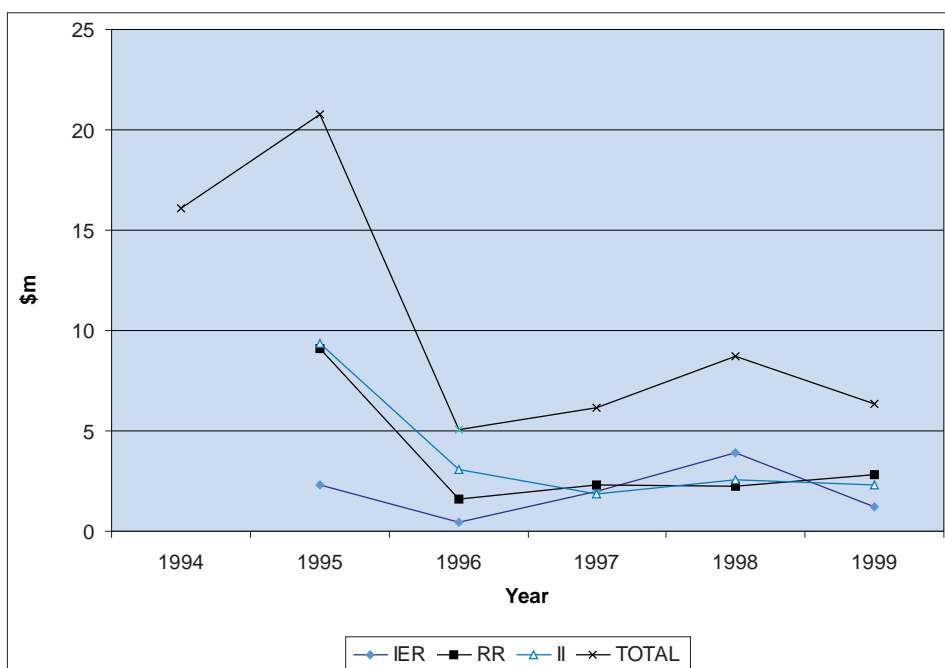
4.15 AQIS advised that the decision to subsidise the Meat program in 1994–95 with part of the surplus funded by non-meat programs was reached jointly by AQIS with the Department of Finance and Administration and endorsed by the Minister.

4.16 The administrative costs involved in returning over-recovered funds through Revenue Rebates or Industry Initiatives and by using over-recoveries to offset previous under-recoveries can be significant and depend on the method used. These costs are borne by industry, but have not been quantified by AQIS. The cost of managing over-recoveries highlights the importance of AQIS regularly monitoring fee levels and promptly adjusting these where necessary, to minimise the likelihood of program over-recoveries. There are also difficulties in ensuring that those clients who contributed to any surplus receive an equitable share of the proceeds. In addition, as discussed later in this report, there are delays in returning over-recovered funds to industry.

4.17 Although AQIS has a policy that a maximum of 10 per cent of annual program expenditure can be held in an Income Equalisation Reserve account, there were no limits on the amount of funds that can be held in the Revenue Rebate and Industry Initiative accounts. The ANAO noted that for some industries the total held in reserves was significant. For example, the amounts held at 30 June 1999 for the Grains industry totalled 30 per cent of annual expenditure and for Exports Dairy totalled 23 per cent. Figure 7 summarises the over-recovered funds held by AQIS from 30 June 1994 to 30 June 1999. It shows that results were mixed, with variations from program-to-program and year-by-year. Appendix 13 summarises the over-recovered funds balances and movements from 1995–96 to 1998–99 by recoverable program.

Figure 7

Over-recovered funds held by AQIS 30 June 1994 to 30 June 1999



Source: AQIS.

Note: Includes funds for the Ballast Water program for 1995–96, 1996–97, 1997–98 and 1998–99 of \$0.715 million, \$0.097 million, \$0.934 million and \$1.579 million respectively.

4.18 Over the last five years in relation to the non-meat programs, AQIS has over-recovered by an average of four per cent per annum. The level of over-recovered funds held in reserves also evidences this. Over-recoveries for the Grains program have averaged 26 per cent per annum over this period. The ANAO noted that AQIS has had legal advice that, if a program's revenue exceeds costs by more than 10 per cent there could be a difficulty in maintaining its status of fee-for-service 'cost-recovery'—it could be construed as a tax.

4.19 AQIS advised that the continued over-recoveries in the Grains program has been due to historical record high production and export of grain over the past three years⁷² and that in each of these years the original industry estimates have been exceeded.⁷³ AQIS also advised that:

The difficulties in establishing fees and charges to reach a zero outcome should not be underestimated. By their very nature, the programs that

⁷² Compared to the 10-year average of 14 million tonnes per annum.

⁷³ AQIS advised that the estimated volumes for 1997-98, 1998-99 and 1999-2000 were 21, 23 and 23 million tonnes respectively. Actual volumes achieved for these years were 23, 26 and 26 million tonnes respectively.

AQIS operates in key rural export industries are impacted by the extreme economic volatility that bedevils those industries. A range of factors can rapidly impact on trading activity which in turn impacts on AQIS' revenue base and its capacity to meet unavoidable, continuing costs. These include:

- national climatic influences (drought, flood) which are unpredictable and can have a severe impact;*
- regional climatic influences (frost, fire);*
- pest and disease outbreaks, for example, Anthrax in Victoria and New South Wales, Newcastle Disease in New South Wales;*
- world economic conditions, for example the Asian Economic crisis, can change rapidly;*
- food safety concerns and chemical residue concerns; and*
- world events, for example the outbreak of Bovine Spongiform Encephalopathy (BSE or 'mad cow' disease) in Europe.*

4.20 The ANAO recognises that AQIS' programs operate for industries subject to substantial uncertainty in export and import volumes. This reinforces the need for budgeting for cost-recovery to minimise other sources of forecasting error and for close monitoring and review, with appropriate response, of actual cost-recovery outcomes. In the example of the Grains outcomes, the ANAO notes that, on average over the three years, the percentage excess over estimate was 12 per cent per annum compared with the 30 per cent per annum over-recovery, suggesting that other factors contributed substantially to the over-recovery.

Revenue Rebates

4.21 AQIS' policy is that over-recovered funds belong to industry and that their distribution is to be undertaken, as far as possible, in a timely manner (see paragraph 2.14). The ANAO found that of the six programs that had Revenue Rebate balances at 30 June 1997, only Grains had paid out rebates over the following two years, although the total balance of funds held in reserves for Grains also increased by \$437,000 between 1997–98 and 1998–99 (see Appendix 13).

4.22 The ANAO concluded that Revenue Rebate balances are often retained for a number of years rather than being paid out promptly by means of fee discount following over-recovery, which should be a matter of concern in a fully cost-recovered situation. The total Revenue Rebate balance at 30 June 1999 for all programs was \$2.8 million.

4.23 The Quarantine Import Clearance program, for example, has had a \$1.3 million Revenue Rebate balance since 30 June 1998. AQIS advised that this was due to the AICCC [AQIS/Industry Cargo Consultative Committee] agreeing that, following the cessation of rebates to industry in 1996–97, the remaining over-recovered funds be held in an account for use on Industry Projects. The requisite transfer of balance of funds remaining in the Revenue Rebate to the account to the Industry Initiative account did not occur at that time. In reporting to the AICCC, however, AQIS has correctly reported the balance of the Industry Project Funds, irrespective of the description of the accounts.

4.24 In light of the issues stated above, AQIS indicated that it will now initiate the appropriate accounting adjustments to ensure balances of over-recovered funds are reflected in the correct accounts for which the funds are intended.

4.25 AQIS also advised that the delays in returning funds held in the Revenue Rebate account are due, in part, to its reliance on industry bodies to determine the exact nature of how the returns will be effected. However, evidence in support of this view was not supplied. The ANAO suggests that AQIS review the balances in its Revenue Rebate account as a matter of priority to ensure the policy objective is being achieved with least adverse impact on fee payers.

Reporting to stakeholders on cost-recovery performance

4.26 AQIS makes available cost-recovery performance information on its programs in the *AFFA Annual Report* to Parliament, the AQIS annual *Report to Clients* and directly to its Industry Consultative Committees.

4.27 The *AFFA Annual Report* discloses limited information about the performance of the individual recoverable programs. The annual *Report to Clients* does provide information for clients on income, expenditure and operating results for each program. However, it has not included the opening and closing balances of the reserve accounts and the cumulative surplus or deficit, nor consistently reported on the actual percentage of costs recovered, either at a program level or on an AQIS-wide basis, nor on how surpluses/deficits are employed. The ANAO found that a number of figures published in the *Report to Clients* over recent years differed from the figures provided by AQIS during the audit. In addition, the AQIS 1998–99 *Report to Clients* contains estimates of the income, expenditure and operating results for each program, even though the actual audited results were available well before the *Report to Clients* was printed.

4.28 The ANAO considers that the *Report to Clients* provides an opportunity for members of the public to compare the performance of the recoverable programs. More comprehensive reporting of the cost-recovery performance of the recoverable programs, including the

percentage of costs recovered and cumulative results in relation to under and over-recoveries, would assist in such comparisons. The ANAO understands that it would not be costly to produce this information. Reporting of cumulative cost-recovery results has also been discussed with AQIS in the context of appropriate disclosure in the AQIS financial statements.

4.29 In addition to the material published in its annual reports, AQIS provides financial information about the performance of each program to the relevant Industry Consultative Committee. The ANAO found that the consultative committees received regular reports on the program's expenditure and revenue position. However, the level of reporting on the balances and transactions in reserves varied from program to program. The reports to the AQIS/Grains Industry Consultative Committee contain comprehensive balance and transaction information, and the ANAO suggests that this be used as a better practice model for other programs.

Recommendation No.3

4.30 The ANAO recommends that, to improve transparency as part of its accountability obligations, AQIS include more comprehensive information in its annual *Reports to Clients* about cost-recovery program performance, including cumulative results in relation to under and over-recoveries.

AQIS response

4.31 Agreed that further information in relation to cumulative results and status of over-recovered funds will be included in the annual *Report to Clients*.



Animal Quarantine Stations

4.32 In examining all the AQIS recoverable programs, the ANAO observed that there were some differences from other programs in the way the Animal Quarantine Stations program was managed. Over-recovered funds have been treated as an increase in AQIS' equity and there has been no public reporting of the cumulative balances held

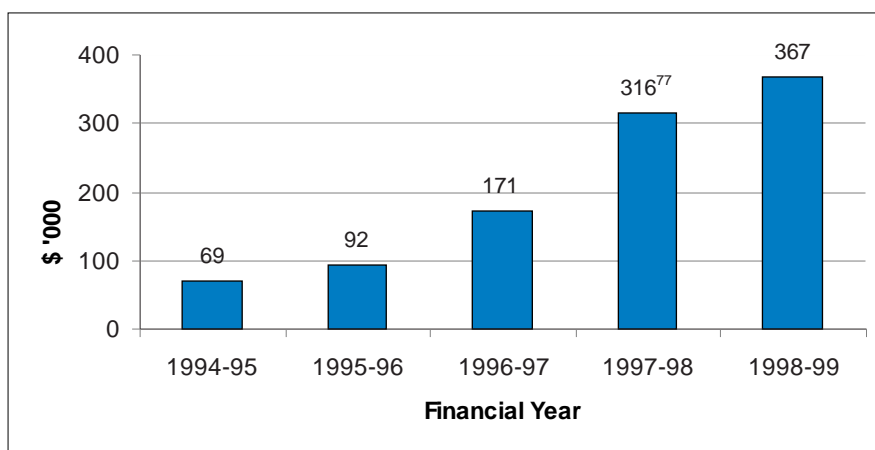
for the program. Unlike other recoverable programs,⁷⁴ there is no Income Equalisation Reserve for Animal Quarantine Stations and over-recoveries have not been returned to industry, as AQIS considers that:

*... due to the diverse nature of the client base it was not possible to return funds to an easily defined group and therefore no liability for over-recovered funds existed.*⁷⁵

4.33 For the five years to 30 June 1999, the program generated over-recoveries totalling some \$1 million. Although some fees were reduced during 1998–99, the program continued to make a surplus of \$0.367 million for the year, against a forecast deficit of \$0.138 million.⁷⁶ A further surplus of over \$83 000 was budgeted for the program for 1999–2000. Figure 8 summarises the annual over-recoveries made by the program for the past five years. The amounts represent a significant proportion of expenditure, for example, in 1997–98 and 1998–99 revenues exceeded costs for the program by 13.0 per cent and 15.6 per cent respectively. The accumulated funds now total 46 per cent of the program’s annual expenditure.

Figure 8

Over-recoveries made by the Animal Quarantine Stations program 1994–95 to 1998–99



Source: AQIS.

⁷⁴ In 1997-98 the Airports program also over-recovered \$1.265 million, which was also treated as equity. However, these funds were in effect rolled over into 1998-99 to offset a planned deficit.

⁷⁵ AQIS Business and Finance Committee 1/99, Agenda Item 5.

⁷⁶ AQIS assumed that the Asian economic crisis would lead to a significant reduction in importations, but this did not eventuate.

⁷⁷ The 1997-98 *Report to Clients* disclosed a surplus of \$0.577 million. The actual surplus was \$0.616 million before roll-over of \$0.3 million subsidy into 1998-99.

4.34 AQIS advised that:

... the build up in over recoveries has resulted from historical factors relating to the impact of changing import protocols on workloads. For instance, in 1994 the quarantine period for the importation of cats and dogs from rabies infected countries reduced from nine months to one month. Although fees had been increased in anticipation of a significant reduction in importations, there was in fact a huge increase in importations. AQIS is monitoring the appropriateness of program fees.

4.35 In February 1998 the then Minister was advised by AQIS that expenditure on repairs and maintenance at the facilities used by the program had been minimal during the last few years, that the infrastructure was in need of attention, and the Minister was requested to endorse the long-term retention of surplus funds within AQIS, for the use of the program. The Minister's Office sought advice from AQIS on whether such retention of these moneys was legally possible. In April 1998 the Minister was advised that AQIS proposed to spend the surplus on repairs and maintenance of Australia's post-entry animal quarantine facilities and that:

There would appear to be no legal impediment under the Quarantine Act 1908 or in AQIS' charter to the retention of these moneys for use in the upgrade of AQIS's post-entry quarantine stations. ...The only risk (judged to be remote) is that the fee might be challenged to be a tax as opposed to a fee.

4.36 AQIS advised the ANAO that the Minister approved the proposal but it has not been able to locate a signed copy of the approval evidencing this. Since then, the amount spent on repairs and maintenance has been relatively minor, and the program's accumulated over-recoveries have continued to grow. Good cost-recovery practice, including AQIS' practice in other programs, is for fees to cover all costs of the services provided, including any repairs and maintenance required. Repairs and maintenance usually represent a small percentage of total program costs and accordingly, reduction of a significant surplus could not reasonably be expected through this course of action.

4.37 During 1998–99 some \$0.125 million was spent by the program on capital items, mostly on a new equestrian surgery at the Eastern Creek Quarantine Station in Sydney. This represents about 10 per cent of the accumulated surplus.

4.38 AQIS advised that:

The issues of privatisation/commercialisation will impact on the program and have been under consideration for approximately 18 months. The effect should be known early in the next financial year. It is highly likely that the number of Government owned quarantine stations will be reduced. Significant money will be required to construct specialised facilities at remaining stations or to transfer these facilities from the ones being sold. These issues therefore mean that the program has been reluctant to spend all of the over-recovered money, given that it may be needed for this work in the near future.

4.39 AQIS has also recently advised that it has reviewed utilisation of the accumulated surplus. The program recorded a loss of \$0.584 million in 1993–94, which was not pursued in future years, mostly on the grounds that the deficit would be largely recovered from clients who had not used the program’s services when the loss was incurred. AQIS has now decided that the earlier deficit will be offset against the current surplus when the 1999–2000 financial statements are completed.

4.40 The ANAO concludes that clients using the animal quarantine stations, mainly dog and cat importers, have paid fees well in excess of costs for a number of years. The ANAO considers that, as a general approach, this is not in accordance with sound cost-recovery practice nor does it generate stakeholder confidence in the system. It appears there would be benefits in AQIS more quickly varying the fees charged where it becomes apparent that volumes of business will significantly exceed expectations, resulting in over-recoveries.

Recommendation No.4

4.41 The ANAO recommends that, in order to achieve the objective of cost-recovery, AQIS reviews more regularly its fees in relation to the costs incurred for the Animal Quarantine Stations program.

AQIS response

4.42 Agreed.

5. Setting Fees and Charges

This chapter examines the setting of fees and charges by AQIS' recoverable programs. The ANAO found that guidance to AQIS staff was inadequate and the fees imposed resulted in inequitable charges for some clients.

The nature of fees and charges

5.1 AQIS applies a mix of fees-for-services, and registration and quantity charges in each of its recoverable programs, in line with its goal of recovering the costs of its operations. Appendix 14 summarises the legislation under which AQIS' trading revenue is imposed and collected.

5.2 About 90 per cent of AQIS' trading revenue is collected from fees-for-services. The remainder is collected from registration and quantity charges that are raised under taxing legislation (except for two programs, as discussed below).

5.3 It has been established in the courts that for an impost to qualify as a fee-for-service, a number of criteria need to be met, including that:

- a specific service must be provided;
- the service is rendered to or at the request of the party paying the account; and
- the impost bears a reasonable relation to the cost of the service rendered. As a result of a High Court ruling issued in December 1999,⁷⁸ it is required that the impost represent an allocation, on a rational basis, to an individual user of a service (or network of services) of the costs of providing the service (or network of services) to all users of that service (or network of services).

5.4 For an impost to qualify as a tax it must be a compulsory extraction by a public authority for a purpose, and not be a payment for services rendered.⁷⁹ Section 55 of the Constitution requires that legislation imposing a tax deal only with that subject. Accordingly, at least two acts are required, namely an act to impose the tax, and an act to authorise its collection. The act authorising the collection of a tax is not constrained to deal with only the collection of that particular tax. Consequently, AQIS has consolidated the legislation authorising the collection of various charges into one act.

⁷⁸ The decision in *Airservices Australia v Canadian Airlines International Ltd* was handed down by the High Court on 2 December 1999. Decisions were handed down at the same time in *Airservices Australia v Monarch Airlines Ltd* and *Airservices Australia v Polaris Holding Company*, which raised the same issues and were heard concurrently.

⁷⁹ *Mathews v Chicory Marketing Board* (1938), 60 CLR 263 at 276.

5.5 The distinction between fee-for-service and taxing legislation is important to the management of AQIS' cost-recovery systems, because of the legal principle that a fee for a service must not be set with a view to exceeding the estimated full cost of providing that service to the user group for that service.⁸⁰ However, where AQIS imposes charges under taxation powers these are not required to be aligned with the cost of the service (if any) to which they relate. Accordingly, AQIS may set fees at a low rate by offsetting costs through higher registration charges. A fee for a service set at a rate which seeks to recover more than the actual cost of providing the service (or network of services) to all users of the service (or network of services) could be construed as constituting a tax.

Basis for imposing certain fees

5.6 Given the above considerations, it is a matter of good management practice to review the basis for imposing fees and charges from time-to-time and consider the implications for the agency as a whole. For example, normal AQIS practice is to impose registration charges and quantity charges under taxing legislation. The ANAO found, however, that two programs impose these 'charges' under fee-for-service legislation:

- the Quarantine Import Clearance program collected about five per cent of its revenue in 1998–99 (\$1.6 million) from 'approved premises registration' imposts collected under the *Quarantine Act 1908*; and
- the Exports Fish program collected about 16 per cent of its revenue in 1998–99 (\$0.5 million) from the fish 'quantity charge' collected under the *Export Control Act 1982*.

5.7 As discussed, the classification of an impost as either a fee-for-service or a tax is important because of the principle that a fee must be for a service and must not be set with a view to exceeding the estimated full cost of providing that service. Neither characteristic is required of a tax which, however, must be imposed under legislation dealing only with that subject. Advice received by the ANAO indicates the basis for imposing the above two 'charges' under fee-for-service legislation is uncertain as they do not appear to relate to the provision of

⁸⁰ See *Harper v Victoria* (1966) 114 CLR at 361, *General Practitioners Society v The Commonwealth* (1980) 145 CLR at 532, *Air Caledonie International v the Commonwealth of Australia* (1988) 165 CLR at 467 and *Airservices Australia v Canadian Airlines International Ltd* (1999) 167 ALR 392. Under AQIS' various legislation, its fees must be 'in connection with' the performance of services (*Export Control Act 1982*), be 'payable in respect of' services (*Quarantine Act 1908*) or be payable 'in respect of the provision of' the relevant services (*Imported Food Control Act 1992*). Subsection 36(2) of the *Imported Food Control Act 1992* provides that the amount payable in respect of a particular service must not exceed the direct and indirect costs that are properly attributed to the provision of that service, calculated in accordance with ordinary commercial principles.

services and are revenue raising in nature. Action to resolve the uncertainties is recommended as a matter of priority, at least in fairness to fee payers.

Recommendation No.5

5.8 The ANAO recommends that AQIS review and resolve, as necessary, the uncertainties concerning the basis for imposing the 'approved premises registration' imposts under the *Quarantine Act 1908* and the fish 'quantity charges' under the *Export Control Act 1982*. These matters should be kept under review on a regular basis.

AQIS response

5.9 Agreed. AQIS is currently reviewing this.

Relationship between fees/charges and program costs

5.10 In preparing budgets, AQIS program managers set all anticipated direct and indirect costs against the expected activity level of the program, and adjust fees and charges to reach a zero outcome (full cost-recovery without under or over-recovering). Fees and charges are endorsed by the ABFC and approved by the Minister. In most program areas, fees and charges are determined in consultation with relevant industry representatives, by taking into consideration existing fee and charge levels, the expected volume of chargeable transactions and expected costs for the forthcoming year.

5.11 AQIS advised the ANAO that the rationale underpinning its fee structure is that annual imposts such as registration charges are designed to cover program fixed costs, while fees-for-services cover program variable costs. It further advised that its registration charges cover central and regional office costs while its fees-for-services cover field costs. While this is a general principle, AQIS does not require its programs to strictly adhere to it where more appropriate systems are negotiated with industry. The ANAO found that AQIS has not defined the items to be treated as 'fixed' or 'variable' costs. In addition, AQIS' performance reporting for the non-meat programs does not present income and expenditure details that separate fixed costs from variable costs and separate annual charge income from fees-for-services.

5.12 AQIS does record raw data from which it is possible to ascertain the proportions of program revenue sourced from AQIS' fee-for-service and taxing legislation. As Table 8 illustrates, the proportions vary widely from program-to-program. AQIS advised that this variation was due to AQIS' policy of managing its cost-recovered programs as separate business units and industry's involvement in developing recovery mechanisms.

Table 8

Recoverable program revenue sources—fee-for-service and taxation legislation 1998–99 (Per cent)⁸¹

<i>Program</i>	<i>Fee-for-service</i>	<i>Registration charge (tax)</i>	<i>Quantity charge (tax)</i>
Meat	92	8	-
Quarantine Import Clearance	100	-	-
Grains Exports	61	1	38
Horticulture Exports and Dried Fruit	89	11	-
Seaports	100	-	-
Exports Fish and Other Processed Food	45	55	-
Animal Quarantine Stations	100	-	-
International Mail ⁸²	100	-	-
Live Animals Exports	100	-	-
Post Entry Plant Quarantine	100	-	-
Exports Dairy	48	11	41
AQIS Average	91	6	3

Source: ANAO analysis of MASS data.

5.13 The only recoverable program that does ascertain the mix between its fixed and variable costs is the Meat program. Figure 9 shows there is a gap between the program's registration charges and fees-for-service and its fixed and variable costs.

⁸¹ Excludes the Airports program, which received \$18.9 million in the form of a government appropriation of revenue, collected for the passenger movement charge and generated some \$0.49 million in fee-for-service revenue.

⁸² The International Mail program invoiced Australia Post for \$2.056 million for services delivered in 1998-99 and generated about \$0.1 million in fee-for-service revenue.

Figure 9

Meat program example

The Meat program aims to cover its fixed costs through establishment registration charges and its variable costs from fee-for-service charges. However, in 1998-99 the registration fee, government subsidy and other income was \$6.7 million against fixed costs of almost \$8.8 million. The shortfall (\$2.1 million) was subsidised by over-recoveries of fee-for-service income, as shown in Table 9. Appendix 15 shows detailed calculations of the relationship between the recovery of fixed and variable costs over the three years to 1999-2000 for the Meat program.

Table 9

Meat program 1998-99 comparison of fixed and variable costs and income (\$ million)

<i>Item</i>	<i>Budget</i>	<i>Actual</i>
Fixed costs	7.404	8.761
Registration Fees and other Income	6.105	6.702
Shortfall	1.299	2.059
Variable Costs	43.473	43.774
Fee-For-Service Income	44.133	45.812
Surplus	0.660	2.038

Note: A further surplus of \$0.47 million from EXDOC and miscellaneous document charges was also made. As indicated in Table 1, the 1998-99 total operating surplus was \$0.48 million.

AQIS advised that it had sought to align its Meat program registration charges with its fixed costs in 1997 but this would have resulted in significant increases in charges, a result that was unacceptable to both industry and the Government. Instead, existing charge levels were maintained and the Government provided direct subsidies to the program that were to phase out over the period of the meat industry reforms (see footnote 10 on page 31).

Variation in fees for similar services

Variation in fees between programs

5.14 For a variety of reasons, including the different cost structures within programs, and the different nature of products exported by various industry groups, there is variation between programs in the amount charged for similar services. For example, export certificates in the Meat program are \$13.65 compared with \$15 in Exports Dairy and \$40 in Horticulture. The equivalent rate for a half-hour inspection service ranges from \$35 in the Meat program to \$128 in the Live Animal Exports program. A summary of AQIS' charges by program is provided at Appendix 4. As there was limited data readily available on the actual costs of providing each service, the ANAO was unable to systematically analyse the nature of these differences further.

5.15 There is also variation in the costs built into various fees. Programs have built the cost of travelling to the client to undertake an inspection

into the service fee and, as a consequence, all clients are paying for the program's travel costs, regardless of their location. However, the ANAO noted that the Horticulture Exports program is proposing to charge separately for this cost element. Charging separately for travel is more equitable in that the fees imposed on individual clients more closely match the cost to AQIS for delivering the service. Although some clients in more remote locations may initially pay more than they currently do for AQIS' services, aligning fees with costs may stimulate the introduction of alternative delivery mechanisms and rationalise demand for inspections.⁸³ AQIS advised that its previous attempts to introduce travel charges have been resisted by industry and that its current attempt to introduce them for the Horticulture program is also meeting some resistance.

5.16 Variations between programs were also found in the basis on which quantity charges were applied. For example, the Exports Dairy program charged a flat fee-per-shipment regardless of the amount exported, meaning that high-volume exporters pay proportionately less in charges than low-volume exporters. On the other hand, the Grains and Exports Fish programs imposed uniform quantity charges.⁸⁴

Influencing industry behaviour through setting fee levels

5.17 AQIS sets some fees above or below the estimated cost of the services provided, in order to influence industry behaviour. AQIS advised that these practices are agreed with the industries which pay for the services. Examples are:

- during 1998–99, the electronic EXDOC system was budgeted by AQIS to be supplemented with \$0.26 million from excess revenue to be raised through a premium on the manually-issued certificates. In order to encourage industry to use the electronic certificates available through EXDOC, AQIS undercharged for these and overcharged for the manually-issued certificates (see paragraphs 6.24–6.25); and
- replacement certificates are \$150 for Exports Dairy and Horticulture, \$175 for Fish and \$270 for Meat. These amounts are up to 20 times the cost of the original certificate.⁸⁵ Other programs charge only the standard certificate fee for replacement purposes. AQIS advised that

⁸³ The Horticulture Export Program, for example, is proposing to introduce the travel charge in conjunction with other changes to the Program's service delivery arrangements, such as the adoption of compliance arrangements, utilisation of centralised inspection, and increased use of casual or contract staff.

⁸⁴ In addition, the Horticulture program proposed to introduce a quantity charge in 1999-2000.

⁸⁵ Replacement Certificates are required where the original is lost or, more usually, because the description and/or quantity of goods shown on the certificate do not match the type and quantity of goods received by the importing country.

the purpose of the punitive cost is to encourage exporters to provide accurate information when applying for export certification.

5.18 The ANAO considers that while these practices may provide administrative benefits to AQIS, program management should consider, and keep under review, these decisions having regard to the cost-recovery principle that the fee charged should not seek to exceed the cost of providing the service. Such consideration should include all relevant policy issues, such as those relating to small business.

Articulation of fee and charge setting policies and practices

5.19 Overall, the ANAO found that there were significant variations in the setting of fees and charges within AQIS. A comprehensive policy document (as recommended at paragraph 2.27) would provide a framework for the transparent and consistent setting of fees and charges and assist in providing more equitable outcomes for industry.

Relationship between fees and charges for different activities within programs

5.20 AQIS seeks to set fees-for-service at levels considered appropriate by AQIS and industry; they are not necessarily set with a view to match closely the cost of each type of service provided by a program. The cost of providing one service may be offset by revenue generated by another service within the same program. Accordingly, AQIS collects costing information on a program basis and by location (through a total of 430 cost centres). Consequently, it does not have readily available data at an activity level within many of its programs that would enable assessment of the alignment between AQIS' costs and the many different fees it imposes.⁸⁶ Further analysis of costs within programs is undertaken by program managers in consultation with industry, through the consultative committee mechanisms, using estimates of costs based on the estimated staff utilised on various program activities. This approach is used to discuss and agree fees and charges with industry consultative committees.

5.21 The ANAO found that this approach means that the costs borne by individual clients are not necessarily the same as the cost to AQIS for providing the service. Misalignment between activity costs and revenue sources can result in inequitable fees and charges. This is illustrated in the report of the Quarantine and Exports Advisory Council, summarised at Figure 10.

⁸⁶ This issue was also raised in the previous audits conducted by the ANAO in 1985 and 1992. The 1979 Senate Standing Committee Report on National Resources also recommended that a comprehensive functional breakdown of receipts and expenditure be maintained if the level of fees appropriate for cost-recovery is to be properly determined.

Figure 10

Horticulture Exports program example

The Quarantine and Exports Advisory Council (QEAC) June 1999 report of its 'Review and Evaluation of the Horticulture Exports program' found that the program has evolved fees that are inequitable because they do not match the program's costs. The report is summarised at Appendix 16. The Review found there was an absence of meaningful data underpinning the program's fee structure and performance resulting in a lack of financial management transparency and accountability. It also reported that there was an imbalance and inequity between those paying fees and receiving the services, with some clients paying very high proportional costs associated with AQIS' fees and charges while others do not contribute at all to the program's costs. This results from different clients using different types of services, the cost of which is not proportionate to the relevant fee or charge. Figures 10a and 10b summarise the sources of revenue and expenditure found in the program.

Figure 10a

Horticulture Exports sources of revenue 1 July 1998 to 4 June 1999

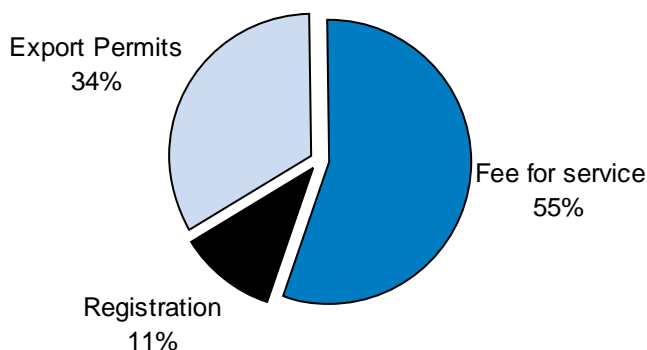
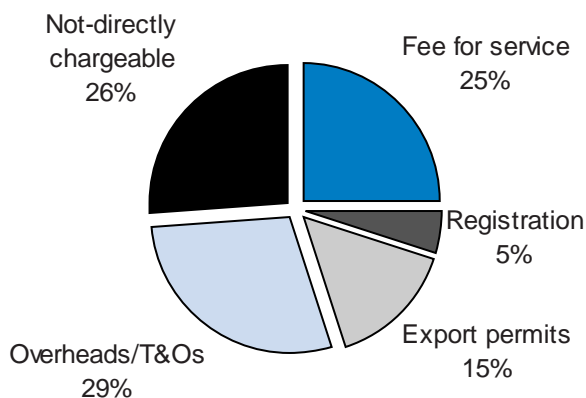


Figure 10b

Horticulture Exports types of expenditure 1 July 1998 to 4 June 1999



Source: Quarantine and Exports Advisory Council *Review and Evaluation of the Horticultural Exports Program*, p.21. Updated by the program to reflect period 13 data.

The Review recommended that the program's revenue base be revised and broadened. In November 1999 the AQIS Business and Finance Committee endorsed the AQIS response to the Review, which included the introduction of new fees and charges, and the revision of existing imposts. These are summarised at Appendix 16.

5.22 AQIS advised that, in conjunction with industry, it seeks to set fees and charges to minimise the possibility of cross-subsidisation between user groups and it has taken steps to minimise such misalignment with the instigation of a number of reviews of program charging mechanisms, including the review discussed above. It also emphasises that its approach to limited costing measures below program level recognises the significant cost burden that would be imposed by a system that identified costs for each type of service.

5.23 As indicated previously, the ANAO considers that appropriate information on the alignment of fees with costs is important in being able to demonstrate that fees bear a reasonable relationship with the costs of the services rendered. The limitations in AQIS' current approach to managing the risk of inequities arising between clients is illustrated in the example. Chapter 6 discusses further the opportunity to identify and manage costs through enhanced cost-recovery systems to minimise cross-subsidisation whilst having regard to cost-effectiveness considerations.

6. Managing Cross-Subsidisation

This chapter examines AQIS' management of cross-subsidisation in the recoverable programs. The ANAO found that it is present at a number of levels, although the extent was not readily quantifiable in some cases.

Cross-subsidisation

6.1 Under full cost-recovery, the revenue raised from fees and charges should offset fully the costs of service provision. Cross-subsidisation occurs when one group of users pays for more than the cost of the services they receive, and the surplus is used to offset the cost of services provided to other users (who pay less than the cost of the services received).

6.2 This issue is particularly acute in the cost-recovery environment, where clients have a legitimate expectation that the fees imposed on them represent the costs of the services that they receive.

6.3 The ANAO acknowledges that in any pricing regime, the price charged to an individual client is unlikely to match precisely the costs to the agency for providing that particular service. The ANAO also acknowledges that there are efficiency constraints on the precision to which fees are aligned with costs and cross-subsidisation is minimised. The issue for managers of cost-recovery therefore revolves around the extent to which an agency has managed its costing and fee-setting mechanisms to minimise, within cost-effectiveness constraints, the occurrence of cross-subsidisation.

6.4 The ANAO identified four areas where there are pertinent matters that AQIS has or should consider in the context of avoidable cross-subsidisation. These address balancing the allocation of costs and recoveries between:

- non-recoverable and recoverable programs;
- recoverable programs;
- clients; and
- locations.

These are discussed below.

Cross-subsidisation between non-recoverable and recoverable programs

6.5 As discussed previously, AQIS revised the methodology for attributing its indirect costs for 1999–2000 (see paragraphs 3.43–3.47). The methods used by AQIS to attribute overheads in 1998–99 and in earlier years resulted in cross-subsidisation of recoverable programs by non-recoverable programs totalling about \$0.65 million net in 1998–99. The ANAO considers the revised attribution methodology to be a significant improvement over previous practices, which had resulted in hidden cross-subsidisation of the recoverable programs by the non-recoverable programs. Further improvements should follow from a planned review of the allocations of costs for Technical and Operation services (see paragraph 3.48).

Cross-subsidisation between recoverable programs

6.6 As discussed earlier in this report, AQIS seeks to prevent cross-subsidisation between programs. The ANAO found that AQIS generally has been successful in managing its programs in recent years to avoid direct cross-subsidisation between them. However, as discussed below, there were some examples of minor cross-subsidisation occurring, between the Airports and Quarantine Import Clearance programs as well as a general risk of cross-subsidisation occurring from the allocation of interest earned on AQIS' bank accounts.

Airports and Quarantine Import Clearance

6.7 An AQIS review of the consistency of charging in the Airports program found evidence of cross-subsidisation of the Quarantine Import Clearance program. Airports staff in Brisbane were performing services and incurring expenditure for which Quarantine Import Clearance was receiving the associated revenue (about \$42 000 for six months or \$84 000 per annum). The ANAO suggested that AQIS review its processes to ensure that, where programs bear the cost of recoverable activities, they are also credited with the revenue generated by those activities.

6.8 AQIS considers that its review processes identify and remedy these sorts of issues and advised that Brisbane was the only airport where Airports program staff work for another program without compensation. AQIS stated that the issue has been addressed through an agreement between the two programs to code revenue to the Airports Program when undertaken by Airports staff.

Interest earned on bank account balances

6.9 During 1998–99, a total of \$0.36 million was earned in interest on funds held in the AQIS bank accounts. One-third was allocated to the Meat Inspection Division, about 15 per cent to corporate equity⁸⁷ and the remainder was allocated to all CSO and recoverable programs in proportion to expenditure.

6.10 The ANAO considers that the recoverable programs generate more than the share of interest credited to them as AQIS has consistently held sizeable amounts of over-recovered funds (averaging \$5 million per annum since 1993).⁸⁸ This indicates a risk that the recoverable programs may be cross-subsidising the non-recoverable areas of AQIS. In addition, the ANAO considers that the method used to distribute earned interest among the recoverable programs was inequitable. Some programs were credited with interest even where they do not have any funds in industry reserves, and consequently other programs with significant holdings have received a reduced amount of interest.

6.11 The ANAO is of the view that it would be more equitable if the interest earned on industries' over-recovered funds was credited in a transparent manner in proportion to each industry's share of the funds. AQIS advised that, in consultation with industry, it was re-examining the way in which it attributes the interest on funds held in its bank account. AQIS advised that it did not have investment powers prior to the introduction of devolved banking arrangements on 1 July 1999.

6.12 AQIS also advised that in January 1995 it received legal advice that it was not under any legal obligation to pay interest in respect of the amount to be returned to industry and such interest cannot be paid to industry unless the then Minister for Finance had given a valid direction under the then *Audit Act 1901* that it be so paid. Alternatively, AQIS could decide, as a matter of policy, to increase the amount returned to industry by an amount representing notional interest but this would depend on the availability of funds within the AQIS Trust Account.

6.13 In view of this advice, the minimal cash available to AQIS and as an incentive for industry to agree quickly on mechanisms to return

⁸⁷ AQIS operates a separate account called Corporate Equity through which it transacts, amongst other items, any gains or losses on disposal of assets that were acquired before the introduction of full cost-recovery. As the purpose of this account was stated by AQIS to be outside the cost-recovery environment, the audit did not include a review of this account, which had a balance of almost \$1 million at 30 June 1999.

⁸⁸ AQIS appears to have used over-recovered funds as working capital. AQIS advised that this was because it had inadequate capitalisation on start-up.

over-recovered funds, over-recoveries had not been included in any calculation of the attribution of interest to programs. AQIS advised that it has excluded funds held in industry reserve accounts from the process to distribute interest earned on funds held in AQIS' bank accounts as a disincentive for industry groups to leave funds in the reserve accounts for extended periods of time. The policy is currently under review.

Cross-subsidisation between clients

6.14 AQIS sets each fee and charge with a view to contributing to achieving the goal of full cost-recovery for each program, but not specifically to matching the cost of the relevant service (see Chapter 5). Inevitably, this fee and charge-setting practice will lead to cross-subsidisation between clients within a program, as some clients will pay more in a fee than the cost to AQIS of providing the service, while others will pay less than the cost. Some overall inequity in specific fees is therefore unavoidable, unless the program's client group is homogenous. In this circumstance, clients would use all of the program's services equally, and each would contribute an equitable overall proportion in revenue to the program, despite there being gaps between the fee for a specific service and its cost.

6.15 Many AQIS programs cover similar client groups and therefore the risk of internal cross-subsidisation is reduced, but not eliminated. AQIS does attribute costs below program level in some programs, but because its policy is to cost-recover at the program level, it does not systematically collect data on the actual costs of services for client groups within all programs. Accordingly, the ANAO was unable to quantify overall the degree of potential or actual cross-subsidisation.

6.16 Some AQIS programs cover many and varied clients that may not use all of the programs' services equally, thereby increasing the risk of cross-subsidisation, as the following examples illustrate. The examples also illustrate the potential benefits to AQIS and its clients where data for attributing costs below the program level are made available.

Quarantine Import Clearance program

6.17 The Quarantine Import Clearance program services clients who are importing processed foods, agricultural products, shipping and air containers, biological products, live plants and animals, machinery and equipment, sawn timber, logs and mouldings.

6.18 The program has tended to collect most of its revenue from the Cargo Risk Management and Entry Management systems, while these comprise less than half of the program's overall costs. In late 1998 the

program introduced the House Airway Bill fee and COMPILE⁸⁹ fee to recover costs not previously recovered from the aircargo industry and customs brokers respectively.⁹⁰ These costs were previously met through revenue paid by clients using other services provided by the program. However, in 1999–2000 the program still expects the range of fees paid by users of the Cargo Risk Management and Entry Management systems to supply 57 per cent of its revenue but only 44 per cent of its costs, generating a surplus of \$4.6 million. In part, this will subsidise the users of the program's Treatments and Inspection services, which are expected to run a deficit of some \$3.6 million. AQIS advised that some users of the Treatment/Inspection services were also users of the Entry Management services, thereby reducing the risk of overall cross-subsidisation for those clients. However, it was unable to quantify the extent of overlap between the two client groups.



Horticulture Exports program

6.19 The Horticulture Exports program covers agriculture exporters ranging from fresh fruit, to vegetables and cut flowers. A review of the program initiated by AQIS, as discussed previously, found that about 55 per cent of the program's revenue is from fees for services that account for only about 25 per cent of the costs. The review concluded that the fee structure is inequitable, leading to some fee payers contributing a disproportionate amount to the program's running costs while others have paid less than their fair share (see paragraph 5.21).

Animal Quarantine Stations program

6.20 The Animal Quarantine Stations program delivers quarantine station services covering many types of imported live animals including dogs, cats, birds, horses, cattle, pigs, rabbits, guinea pigs and bees. However, a costing review undertaken by the Program in 1998 revealed

⁸⁹ COMPILE is the Australian Custom Service entry management system that AQIS uses as part of its risk profiling and screening activities.

⁹⁰ AQIS Business and Finance Committee Meeting No. 7/99, Agenda Item No. 2.2.

that revenue raised from importations of horses, ruminants, cats and dogs was subsidising costs for other client groups such as bird and bee importers.

Exports Fish and Other Processed Foods program

6.21 The Exports Fish program has recently been combined with the Other Processed Foods program. AQIS advised that this was in recognition of the processing nature of both industries and the high degree of overlap between them. Other Processed Foods was formerly a small program covering the export certification of processed foodstuffs (such as canned fruits and vegetables) and non-prescribed goods (such as pizza) for export. The overall program therefore covers essentially unrelated industries and as such, there is a risk of cross-subsidisation between the industries unless the fees charged to each matches the costs of delivering the relevant services.

6.22 In view of AQIS' practice of recovering at a program level, the program was unable to demonstrate that the fees charged to each industry covered only the costs incurred by AQIS in servicing that industry. AQIS advised that the charges paid for export permits (essentially for other processed foods) were recently increased to ensure that they fully recovered the associated costs. The ANAO notes, however, that non-prescribed goods certificates were not adjusted at the same time, despite the program considering that historically the issue of these certificates has been cross-subsidised by around \$80 000 per annum. AQIS had calculated that a fee increase from \$30 to \$100 per certificate issued would be required to eliminate the cross-subsidy.

6.23 The ANAO also notes that the Dried Fruits program has been incorporated into the Horticulture Exports program from 1999–2000.

Meat program

6.24 Within the Meat program, there is evidence that users of the manually-issued certificate services have been subsidising users of the Meat EXDOC electronic certificate system. AQIS papers indicate that about \$0.26 million from the manually-issued Wool, Skins and Hides certificates (\$15 each) was used to provide supplementation to EXDOC during 1998–99. There were about 120 000 EXDOC certificates issued at \$13.65 each but, at the time AQIS set this price, it had budgeted that the certificates would cost \$15.82 each to issue.⁹¹ From 1 January 2000 following re-estimation of the costs involved, the fee for EXDOC certificates was reduced to \$12 and the fee for the manual certificates was increased to \$25.

⁹¹ AQIS Business and Finance Committee Meeting No. 12/98.

6.25 AQIS acknowledged that, within the meat program, the pricing structure for the issue of health certificates produces a surplus which is used to finance, in part, the fixed cost structure. The decrease in the cost of an electronic certificate reflected the sharing of fixed costs with other programs coming on to the EXDOC system and the increase in the price of manual certificates followed from an analysis with industry of the costs of providing manual certificates.

Cross-subsidisation between locations

6.26 AQIS seeks to operate on a system of nationally uniform fee and charge rates (see paragraphs 2.23–2.24), and accordingly, differences between revenue and expenditure at locations will inevitably arise. As discussed below, the ANAO found that this was occurring in two forms: averaging fees for the same service across locations, and deficit-making locations being supported by surplus-making locations.

Averaging fees for the same service

6.27 AQIS' charging guidelines aim to promote consistent application of charges across locations.⁹² However, there were instances during 1998–99 where the same service within a program had different charges depending on the location. For example, the Airports program conducted an initial review in June 1999 which identified that some types of charges were not applied consistently across all airports in Australia. This review determined that different Airports charged nil, \$10, \$13, \$20 or \$32 for the same heat treatments and \$13, \$50 or \$108 for the same Gamma Irradiation treatments.

6.28 AQIS has responded by setting new charge rates to be applied consistently at airports. Initially, the new charges have been set simply by averaging the existing charges, since AQIS does not have information on the actual cost of providing the services. A second phase of the review will determine the actual costs of providing the services to clients and ensure that this is reflected in the charges levied.

Support of deficit-making locations

6.29 The ANAO found that for the majority of programs some locations did not recover their full costs and were being subsidised by surplus-making locations. This was evident in the setting of budgets for programs, not just in the actual results. For example, in the Live Animals Exports program, five surplus-making locations subsidised four deficit-making locations. Similarly, in the Horticulture Exports program, some States were subsidising others. Table 10 shows the outcome of revenue and expenditure for selected States in the Horticulture Exports program.

⁹² AQIS Charging Guidelines for Quarantine and Inspection programs, 1 September 1996.

Table 10

Horticulture Exports program—outcomes by selected State 1997–98 and 1998–99 (\$'000)

	<i>Victoria</i>		<i>South Australia</i>		<i>Tasmania</i>	
	<i>97–98</i>	<i>98–99</i>	<i>97–98</i>	<i>98–99</i>	<i>97–98</i>	<i>98–99</i>
Revenue	1 257	1 558	253	227	129	140
Expenditure	924	1 088	373	469	396	254
Surplus/(Deficit)	333	470	(120)	(242)	(267)	115

Sources: 1997–98 Period 14 data used for the QEAC Review of the Horticulture Exports program and 1998–99 Period 14 data.

6.30 Inevitably, as discussed above, any national program such as AQIS' will result in differing balances of cost-recovery in different aspects of the program. When marked differences occur between locations, resulting in cross-subsidisation, transparency of these outcomes facilitates effective management and client focus. It also contributes to a management focus on discrepancies in costs and fees, contributing to more efficient management of resources.

Conclusion

6.31 The ANAO concluded overall that there was minor cross-subsidisation between AQIS' programs, there was some cross-subsidisation between clients, although in general this was not readily quantifiable, and that there was some cross-subsidisation between locations.

6.32 The risk of cross-subsidisation is inevitably a matter of considerable interest to clients. Any suspicion of cross-subsidisation may undermine client perceptions of the fairness of the fees and charges. AQIS' practice of limited measurement of the costs of its services and not aligning its fees and charges with its costs at this level means that it is only able to provide limited assurance to clients regarding cross-subsidisation. The ANAO noted AQIS' 1998–99 client satisfaction survey indicates considerable dissatisfaction with its fee and charge rates—69 per cent of clients feel that the rates are too high (see paragraph 7.5), although AQIS considers that this reflects in part that user charges *per se* are unpopular with clients. Notwithstanding the merits of this view, the ANAO considers that more can be done to explain the basis for AQIS' fees and charges; more transparent costing information would assist AQIS in this process.

6.33 AQIS has emphasised that it considers that its current approach meets its legal requirements and is consistent with the approach recognised in the Air Services Australia v Canadian Airlines International Ltd High Court decision. Whilst recognising AQIS' view, the ANAO

considers that good practice costing systems seek to identify revenue and costs for different services provided to clients for management purposes where it is cost-effective to do so. It is evident from a number of the examples discussed in this report that AQIS has some data available which would assist it to better manage cross-subsidisation below program level. The ANAO considers that AQIS could extend this approach without necessarily incurring substantial additional costs, as well as considering the extent to which modern costing systems offer the opportunity to manage cross-subsidisation to a greater degree than is currently the case in AQIS.

Recommendation No.6

6.34 The ANAO recommends that AQIS align fees charged to particular clients with the costs associated with servicing those clients where it is cost-effective to do so. Where this is not feasible, the reasons should be made transparent to relevant stakeholders and kept under review.

AQIS Response

6.35 Disagree. AQIS already has in place extensive consultative processes with industry groups which deal with issues associated with equity of fees. Most of AQIS' program industry consultative committees have charging or finance sub-committees which are responsible for the detailed analysis of program budgets and charging mechanisms including the alignment of fees with clients and cost-effectiveness of charging systems.

ANAO Comment

6.36 This recommendation is consistent with better practice cost-recovery systems, which seek to operate effectively and equitably. As discussed in this report, strengthened cost-recovery systems could improve the information available to AQIS for the consultative processes and provide greater management and stakeholder assurance on the alignment of fees with costs.

7. Consulting with Industry

This chapter examines AQIS' industry consultation mechanisms. The ANAO found that AQIS has established Industry Consultative Committees for all except one of its recoverable programs and that these were generally working well, however, indicators were also found that consultation concerning increases in the costs of a major project were not always timely.

Industry views

7.1 The ANAO acknowledges that AQIS operates in a regulatory environment in which the application of full cost-recovery may not always be popular. AQIS places considerable emphasis on developing and strengthening its relationship with its clients and has operated a client feedback program since 1994 that enables industry to report directly to senior management, with guaranteed confidentiality, about how AQIS performs its role.



7.2 AQIS has also been surveying its fee-paying clients since 1995. The 1998–99 AQIS *Report to Clients* presented a summary of the results of an independent client satisfaction survey conducted in early 1999 by a consulting firm. All clients were asked to rate their satisfaction with eight elements of AQIS' service covering:

- staff technical competence;
- staff professionalism;
- the extent to which business needs are taken into account;
- the extent to which AQIS adopts a team approach;
- value for money;
- whether expectations are made clear;
- AQIS' responsiveness; and
- AQIS' flexibility.

7.3 The report indicated that the overall level of satisfaction had increased for all industries over the previous two years. The net improvement rate (the difference between the percentage who said there was an improvement compared with those who said there was a deterioration) ranged from four per cent for live animal exporters to 31 per cent for air cargo clients.

7.4 It was also reported that 77 per cent of survey respondents felt AQIS was keen to promote a team approach (compared with 60 per cent in the previous survey). A further positive trend was that the percentage who believed AQIS provides adequate explanation of quality assurance had risen from 34 per cent to 54 per cent.

7.5 However, it was also reported that:

- 69 per cent of clients consider AQIS' charges are too high;
- 37 per cent of clients consider that AQIS' principal aim is to raise revenue;
- 54 per cent did not believe they can contact AQIS when they need to;
- 42 per cent do not agree that AQIS makes a positive contribution to their business;

and that the following trends needed attention:

- 50 per cent of clients feel that AQIS' staff are well trained (a fall from 61 per cent previously);
- 42 per cent feel that AQIS is consistent in rule interpretation (down from 56 per cent); and
- 42 per cent of clients consider inspections take too long (up from 25 per cent).

7.6 In response to the survey results, AQIS indicated that it would be paying particular attention to the trends in relation to staff training, AQIS' consistency of interpretation of rules and the time taken to perform inspections.

7.7 The ANAO's consultations with industry also revealed some concerns that there was a high level of indirect costs being charged to the AQIS recoverable programs (see paragraphs 3.9–3.12).

7.8 The ANAO noted that to date the AQIS surveys have not sought direct feedback from clients on their satisfaction with the level of consultation undertaken by AQIS.

Industry consultative committees

7.9 In 1997 the Government accepted the recommendation of the Nairn Review of Australian Quarantine that AQIS reform and expand its

industry consultative mechanisms.⁹³ The Review found that AQIS' Industry Charging Review Committees did not cover all industry groups and tended to centre on costs and charges of quarantine services, rather than broader aspects of quarantine policy development.⁹⁴

7.10 AQIS now has industry consultative committees for all but one⁹⁵ of its recoverable programs (listed at Appendix 5) and considers that it works in close collaboration with industry. All committees have had their terms of reference, scope and membership reviewed. Each committee now has representation from AQIS, the major client groups and industry peak bodies and is the principal advisory forum for policy, strategic issues, costs of the program and fees and charges.

7.11 The AQIS 1998–99 *Report to Clients* points out that the committees are proving highly successful for both industry and AQIS in improving consultation, input by stakeholders and clients to decision making, and priority setting. The committees have met regularly, usually three to four times per year. AQIS continues to review, in conjunction with industry, the composition and terms of reference of the committees.

7.12 The ANAO concluded that the revised consultative mechanisms were generally appropriate. Overall, they appeared to be working well and provide a sound framework for the continuous improvement of open communications between AQIS and its clients. In reviewing the effectiveness of AQIS' consultations with its clients, the ANAO did note that a number of affected industries expressed some dissatisfaction with AQIS' handling of the introduction of new technology, as discussed below.

Case study: Non-meat EXDOC

7.13 The ANAO reviewed the development of the non-meat EXDOC system as an example of AQIS' consultation with industry about major projects that will impact on the recoverable programs' costs and, therefore, their revenue requirements.

7.14 EXDOC is the AQIS Electronic Export Documentation System. It is designed to replace a number of manual transactions with electronic processing for documents and certificates. The system has been in place in the Meat Industry since 1992. In 1997 the decision was taken by AQIS to extend EXDOC to a number of non-meat programs, to commence by

⁹³ Australian Quarantine, *A shared responsibility. The Government Response*. August 1997 p.42.

⁹⁴ Nairn M.E., Allen P.G., Inglis A.R. and Tanner C., *Australian Quarantine a shared responsibility*. Department of Primary Industries and Energy, Canberra 1996, p.27.

⁹⁵ Industry Consultative Committees have been established for all programs except Animal Quarantine Stations because there is no easily identifiable industry for this program.

the end of 1998. AQIS considers this to be an important element in giving effect to the Government's commitment to implementing electronic commerce initiatives.

7.15 The ANAO noted some issues covering the management of the project and the adequacy of industry consultation, which have implications for cost-recovery. Estimates of the cost of the EXDOC non-meat development have escalated considerably from \$0.75 million at initial planning in 1996, to \$1.2 million in September 1997 and \$4 million in January 1999. Some \$2.7 million of this had been spent to 30 June 1999.

7.16 There has been no cost-benefit study for the extension of EXDOC to non-meat industries since a report completed in December 1997. The report of the study did not clearly show the costs of developing, maintaining and operating the system over its intended life. The capital cost used in the calculations appears to be \$1.2 million. The report showed (for an undefined 12-month period only), negative net benefits to industry at \$0.3 million, offset by projected benefits to AQIS of \$0.68 million. It is not clear whether industry was informed of the findings of the report at the time. Given the increase in the capital cost of the project since then, the costs would now appear to outweigh considerably the benefits.

7.17 The cost of the EXDOC non-meat redevelopment is to be recouped from the industries using the system, over a period of five years at an annual rate of \$0.2 million each from the Exports Dairy, Exports Fish, Horticulture Exports and Grains Exports programs.

7.18 In addition to the depreciation costs, there are ongoing system running and maintenance costs (such as for Information Technology staff) which are expected in 1999–2000 to be approximately \$1 million. These costs will be divided equally among the four programs.

7.19 Industry Consultative Committee minutes record concerns raised by industry about the huge increase in costs of the project without consultation by AQIS. One industry representative was also quoted as saying that the redevelopment was an 'extreme embarrassment' and that it was not a partnership, but a costly program that had been imposed on industry.

7.20 Although with the considerable delays in the project it must have been evident to AQIS for some time that costs were increasing, AQIS formally revised its estimate of the cost of the redevelopment to \$4 million in early January 1999. Table 12 shows the dates various industries were consulted about the more than threefold increase in the cost of the system.

Table 12

Dates when industries were consulted about EXDOC non-meat system cost increase to \$4 million

<i>Industry</i>	<i>Date Consulted</i>
Exports Fish	24 June 1999
Horticulture Exports	17 June 1999
Grains Exports	5 May 1999
Exports Dairy	14 April 1999

Source: AQIS Business and Finance Committee papers.

7.21 AQIS has agreed to industries' requests to defer the recoupment of depreciation charges and some \$0.52 million will be carried as a deficit by the EXDOC program area pending eventual recoupment of the full amount of depreciation charged in six years. AQIS intends to recover the full costs of the systems re-development, but this will be over a longer period than required under current AQIS cost-recovery practices.

7.22 The ANAO considers that this case study offers a number of lessons for AQIS in respect of keeping industry adequately informed about matters that affect the costs to be recovered from them by AQIS. The ANAO suggests that even at this late stage in the project, the conduct of a thorough cost-benefit analysis would be beneficial, in order to provide full transparency and accountability to industry.



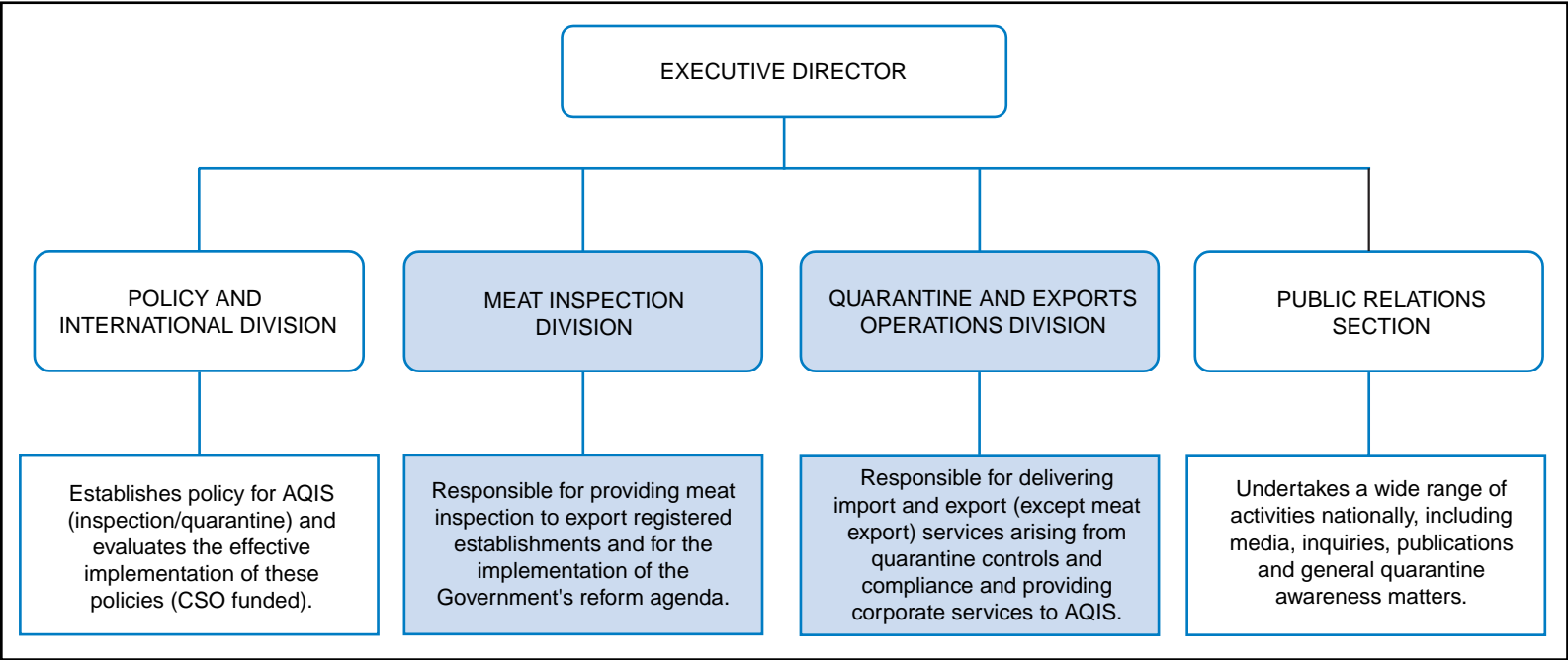
Canberra, A.C.T.
15 September 2000

P. J. Barrett
Auditor-General

Appendices

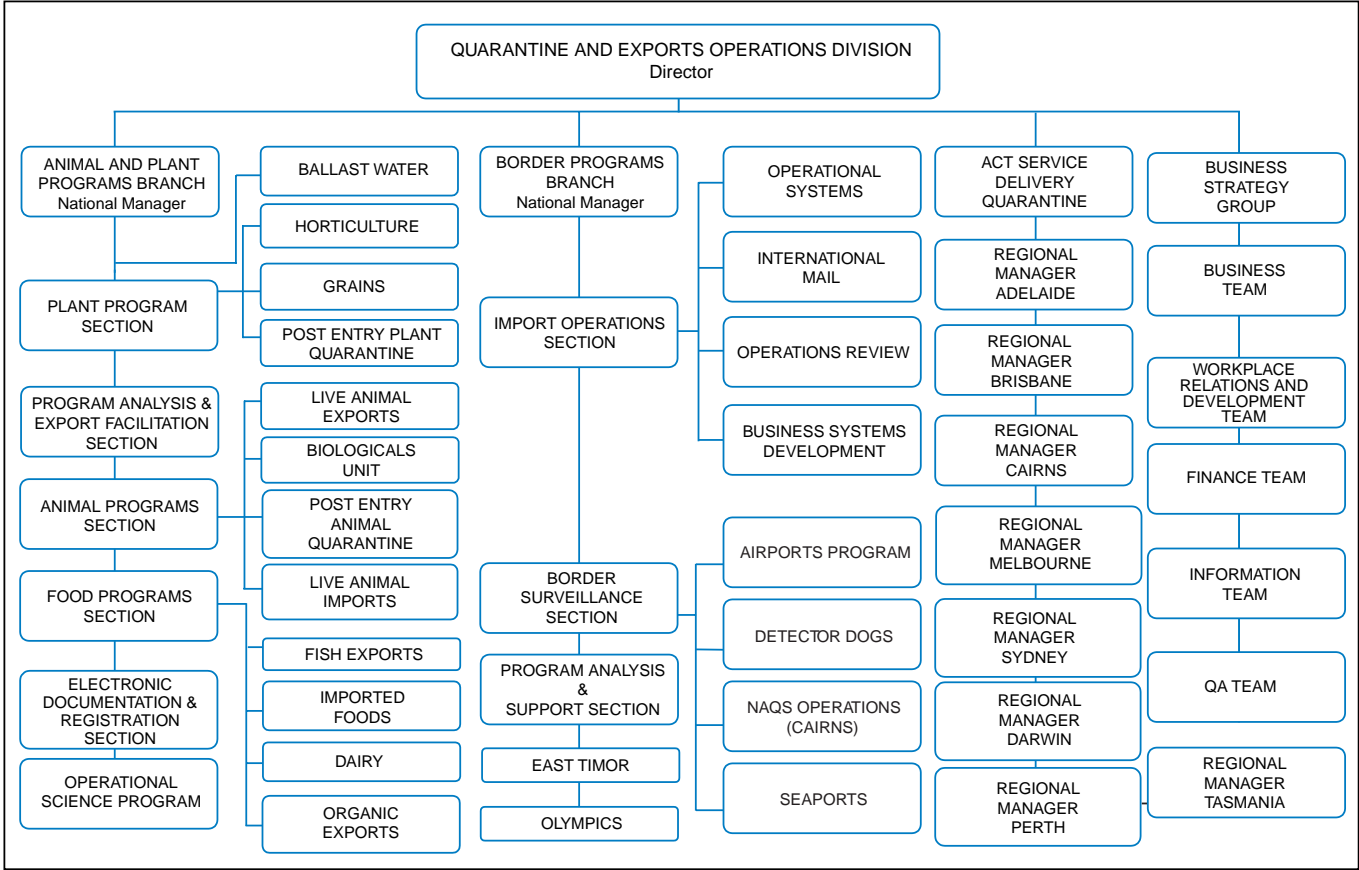
Appendix 1

AQIS organisation chart at 1 July 2000



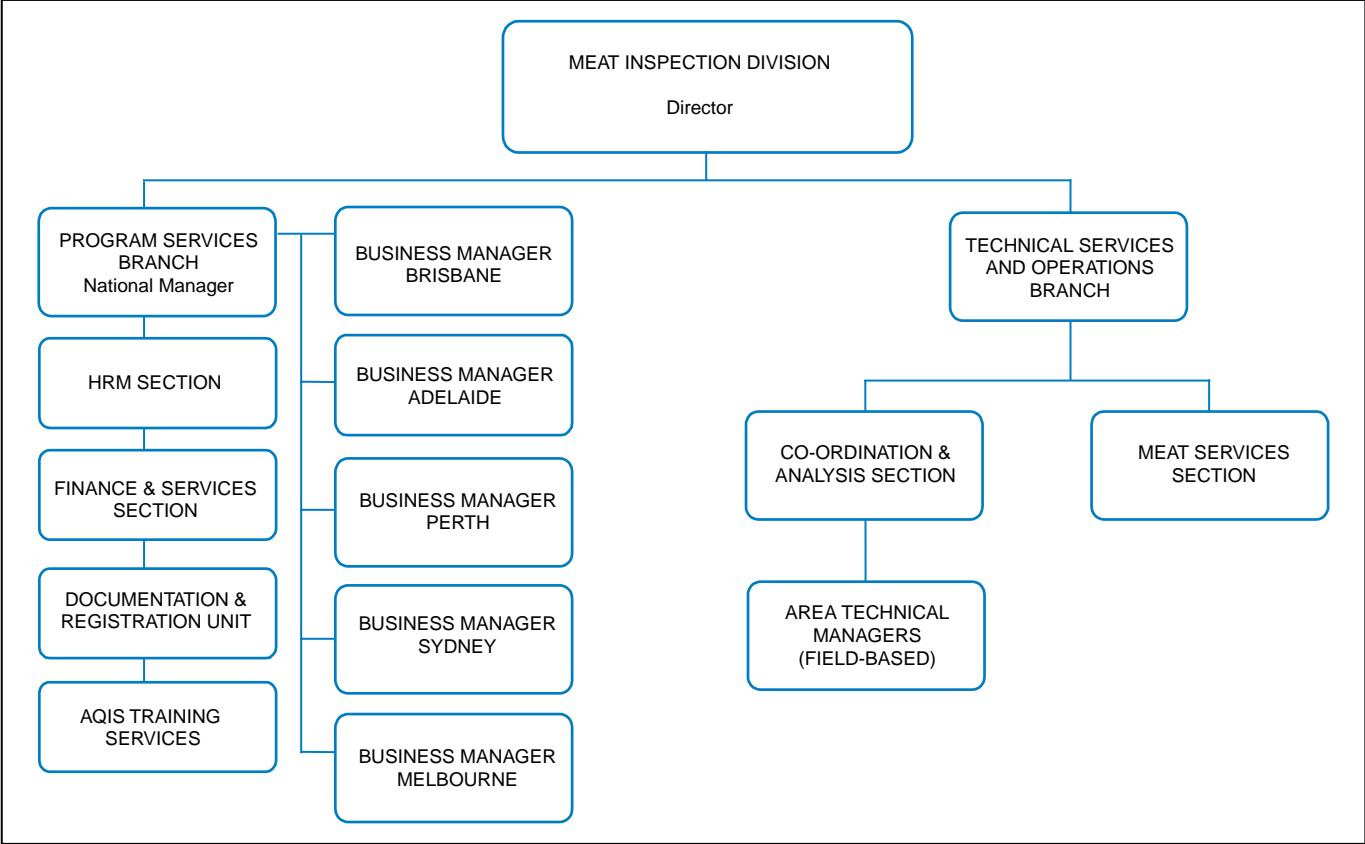
Appendix 1 cont'd

Top structure—AQIS Quarantine and Exports Operations Division



Appendix 1 cont'd

Top structure—Meat Inspection Division



Appendix 2

AQIS' cost-recovery financial and information systems

The **AQIS Import Management System (AIMS)** is an interactive database that processes all imported sea and air cargo that poses a potential health or disease risk to Australia. AIMS is used to profile, assign quarantine directions, apply fees and issue invoices as well as electronically release all imported cargo that is identified as being of quarantine concern.

AURION is a commercial human resource management system, which operates across AFFA.

The **Budget Management System (BMS)** supports the AQIS budget management process, records all aspects of the budget, automates the allocation of costs across and within programs and provides a large number of reports for budget management.

The **Electronic eXport DOcumentation (EXDOC)** system provides exporters of prescribed goods with a 'single window' facility to transact their export clearance business with AQIS and the Australian Customs Service. The system delivers documentation to meet stakeholder and overseas market access requirements.

EFFIT is a task time recording and software capitalisation system used by Information Technology staff that records the resources used for determining the allocation of the costs for systems development and other Information Technology operating and capital accounts.

The **Establishment Register (ER)** provides an electronic export establishment registration regime for export packers/processors of non-meat prescribed goods that meets AQIS' legislative needs and satisfies customer country requirements. The register interacts with EXDOC to ensure that export documentation is only provided for product eligible for a particular market.

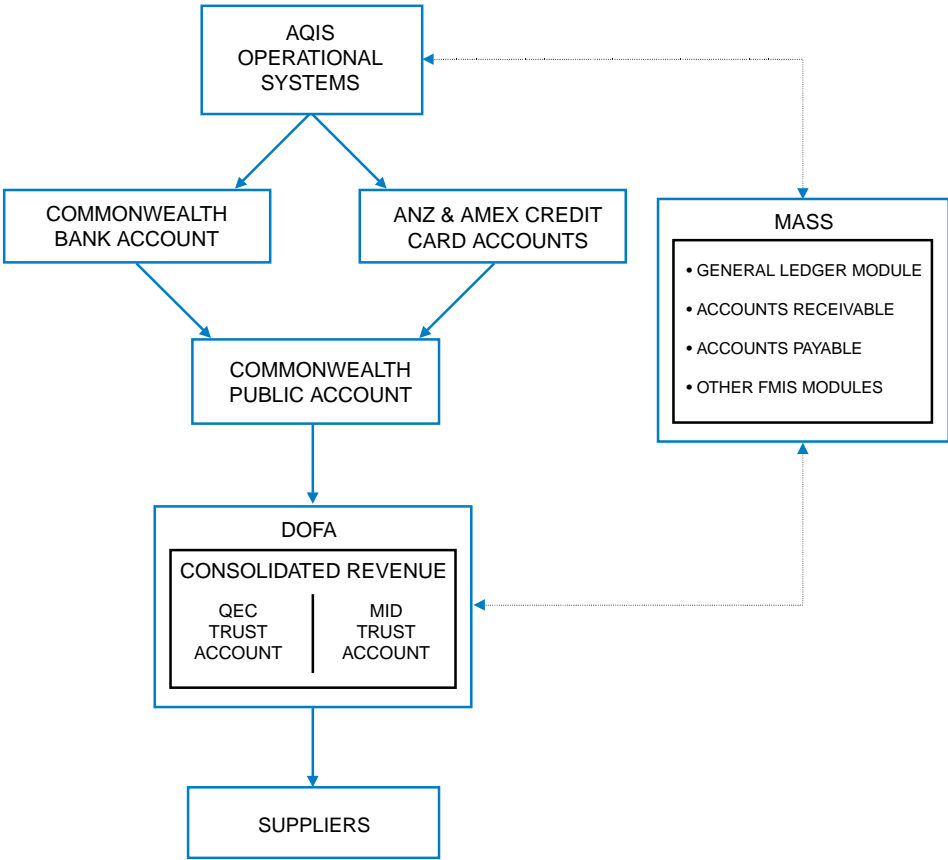
The **Import CONditions (ICON)** database is an Intranet query facility that enables AQIS staff to source a range of commodity related import information.

The **Management Accounting Support System (MASS)** consists of a number of modules such as accounts receivable, accounts payable, inventory control, fixed assets and general ledger which support AQIS' financial management. MASS was superseded by the AFFA-wide QSP Financial Management Information System in July 1999.

Appendix 2 cont'd

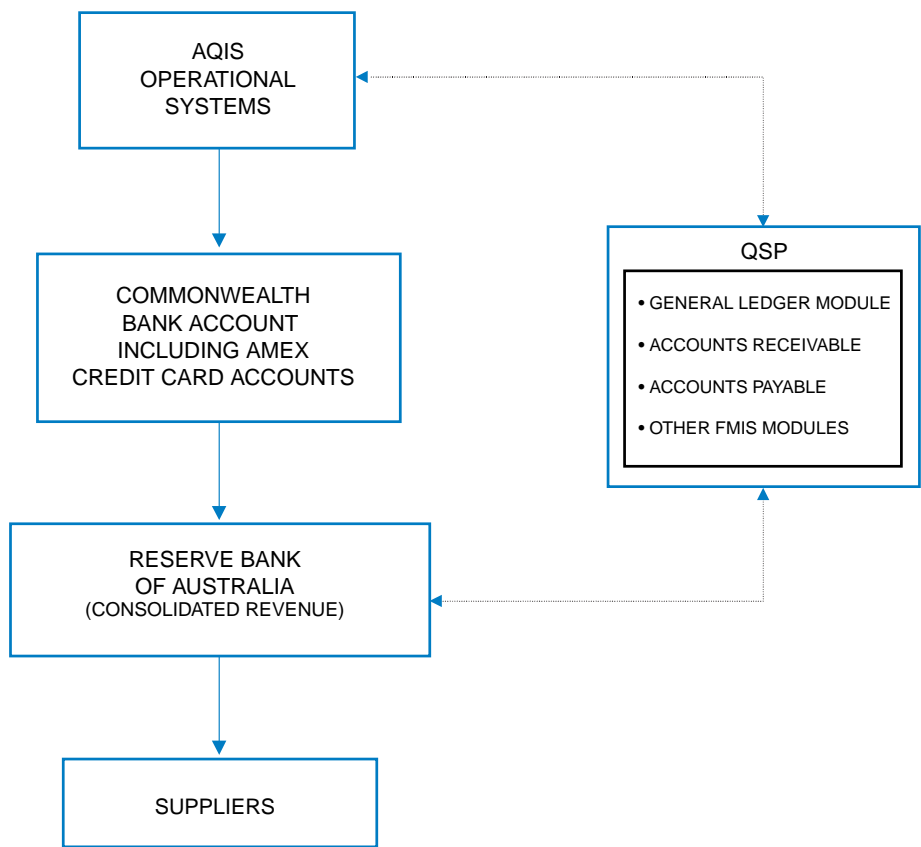
1998–99 Revenue systems

The figure below summarises AQIS' revenue systems in 1998–99.



1999–2000 Revenue systems

In 1999–2000 the revenue systems were changed to reflect devolved banking and the introduction of QSP. These are summarised below.



Appendix 3

AQIS recoverable programs trading results for 1998–99

(Before transfers to and from Income Equalisation Reserve, Revenue Rebates and Industry Initiatives)

<i>Program</i>	<i>Expenditure</i>			<i>Revenue</i>			<i>Surplus/(Deficit)</i>		<i>Percentage Cost-recovery</i>
	<i>Budget (\$'000)</i>	<i>Actual (\$'000)</i>	<i>Per cent</i>	<i>Budget (\$'000)</i>	<i>Actual (\$'000)</i>	<i>Per cent</i>	<i>Budget (\$'000)</i>	<i>Actual (\$'000)</i>	
Meat	53 801	56 027	4	54 535	56 509	4	734	482	100.9
Quarantine Import Clearance	30 884	31 430	2	30 460	28 885	(5)	(424)	(2 545)	91.9
Airports	20 129	21 035	5	19 193	19 306	1	(936)	(1 729)	91.8
Grains Exports	5 025	5 583	11	5 041	6 842	36	16	1 259	122.6
Horticulture Exports & Dried Fruit	4 606	4 728	3	4 699	4 385	(7)	93	(343)	92.7
Seaports	4 016	4 051	1	3 739	3 478	(7)	(277)	(573)	85.9
Exports Fish & Other Processed Food	3 401	3 459	2	3 528	3 453	(2)	127	(6)	99.8
Animal Quarantine Stations	2 348	2 346	0	2 226	2 713	22	(122)	367	115.6
International Mail	2 023	1 916	(5)	2 056	2 162	5	33	246	112.8
Live Animal Exports	1 706	1 689	(1)	1 959	1 558	(20)	253	(131)	92.2
Post Entry Plant Quarantine	1 283	1 266	(1)	1 223	1 255	3	(60)	(11)	99.1
Exports Dairy	1 042	868	(17)	810	839	4	(232)	(29)	96.7
TOTAL	130 264	134 397	3	129 469	131 385	2	(795)	(3 013)	97.8

Note: Excludes 'other' recoverable program income and expenditure. The Meat program includes AQIS Training Services expenditure of \$1.387 million and revenue of \$1.422 million.

Source: ANAO analysis of AQIS Business and Finance Committee papers.

Summary of AQIS fees and charges at 30 June 1999

[illegible]

Appendix 4 cont'd

Summary of AQIS fees and charges at 30 June 1999

Program	Fee-for-service					Levy or Volume Charge	Document Charge	Vessel Pratique	Establishment Registration Fees			
	½ Hourly	Daily	Weekly	Monthly	Annual							
International Mail	\$72 ^b											
Live Animal Exports	\$90 \$128						\$19, \$38, \$64, \$90, \$256, \$512, \$1 280			See Note d		
Post Entry Plant Quarantine	\$72											
Exports Dairy	\$60						\$10, \$15, Replacement \$150			\$800	\$1 750	\$3 100

- Notes: a) Electronic Certificate only (\$12 from 1 January 2000). Charge for manual certificate was \$15 in 1998–99 and \$25 from 1 January 2000.
- b) International Mail charges \$42 for treatment of commercial packages based on a standard quarter hour inspection charge of \$30 plus a \$12 handling charge.
- c) For Meat and Exports Fish programs, the registration charges represent the range of categories. There are several other charges that fit into the ranges shown.
- d) Live Animal Exports does not have documentation charges as such, but the cost is built into the present FFS charges. A review of the fee structure was conducted in 1999–2000.

Appendix 5

AQIS' Industry Consultative Committees at 30 June 2000

- * Quarantine and Exports Advisory Council
- * AQIS Airline Industry Consultative Committee
- * AQIS Industry Cargo Consultative Committee
- * AQIS/Grains Industry Consultative Committee
- * Australian Ballast Water Management Advisory Council
- * Biologicals Industry Consultative Committee
- * Dairy Export Industry Consultative Committee
- * Export Meat Industry Advisory Committee
- * Livestock Export Industry Advisory Committee
- * AQIS/Meat Industry Task Force
- * AQIS/Meat Industry Charging Review Committee
- * Seafood Export Consultative Committee
- * Horticulture Exports Consultative Committee
- * Imported Food Consultative Committee
- * Organic Produce Export Committee
- * Post-Entry Plant Industry Consultative Committee

Note: There is no Industry Consultative Committee for the Animal Quarantine Stations program.

Appendix 6

Previous relevant reviews

General

Australian National Audit Office, *Report of the Auditor-General on an Efficiency Audit: Administration of Quarantine Services*, (tabled November 1985).

Parliament of the Commonwealth of Australia Joint Committee of Public Accounts, *Administration of Quarantine Services*, Australian Government Publishing Service, (Report 257, 1986).

Australian National Audit Office, *Efficiency Audit: Department of Primary Industries and Energy, Australian Quarantine Inspection Service Quarantine Division*, (Audit Report No.35 of 1991–92).

Australian National Audit Office, *Financial Control and Administration Audit: Costing of Services*, (Audit Report No.21 of 1998–99).

Senate Rural and Regional Affairs and Transport Legislation Committee, *Australian Quarantine and Inspection Service*, May 1996.

Nairn M.E., Allen P.G., Inglis A.R. and Tanner C., *Australian Quarantine a shared responsibility*. Department of Primary Industries and Energy, Canberra, October 1996.

Australian Quarantine, *A shared responsibility. The Government Response*. August 1997.

Department of Finance and Administration, *Performance Audit of the Australian Quarantine and Inspection Service*, (Ernst and Young) 12 February 1998.

Meat Inspection Division

Industry Commission, *Meat Processing Volume 1 Report: Report No. 38*. 20 April 1994.

Industry Commission, *Meat Processing Volume 1 Appendices: Report No. 38*. 20 April 1994.

Coopers and Lybrand, Meat Industry Council and the Department of Primary Industries and Energy, *Business Review of the Export Meat Inspection Service*, May 1996.

Australian Quarantine and Inspection Service Reform, *Meat Inspection Program*, Steering Committee Report, November 1996.

Australian Quarantine and Inspection Service, *Follow-up Review of Meat Fee for Service System (MFFS)*, Internal Audit Report, 97–98 13 June 1998.

Appendix 6 cont'd

Quarantine Import Clearance program

Review of Quarantine Import Clearance Costings Structure and Cost-recovery Arrangements (Joint AQIS/Industry review).

Airports program

Review of Airports Program fees (nationally consistent treatment charges), July 1999.

Grains Exports program

Review of South Australian operations, March 1998.

Horticulture Exports program

Quarantine and Exports Advisory Council Review and Evaluation of the Horticulture Exports Program, June 1999.

Exports Fish program

Quarantine and Exports Advisory Council Review of the Export Fish Program, November 1999.

Animal Quarantine Stations program

Revision of Post Entry Animal Quarantine Program Fees, 17 November 1998.

Live Animal Exports program

Review of Financial Management (Joint AQIS/Industry review), September 1999.

Third Party Review (Joint AQIS/Industry review), Completed September 1999.

Export Dairy program

Evaluation of AQIS Export Dairy Program, 1996.

Appendix 7

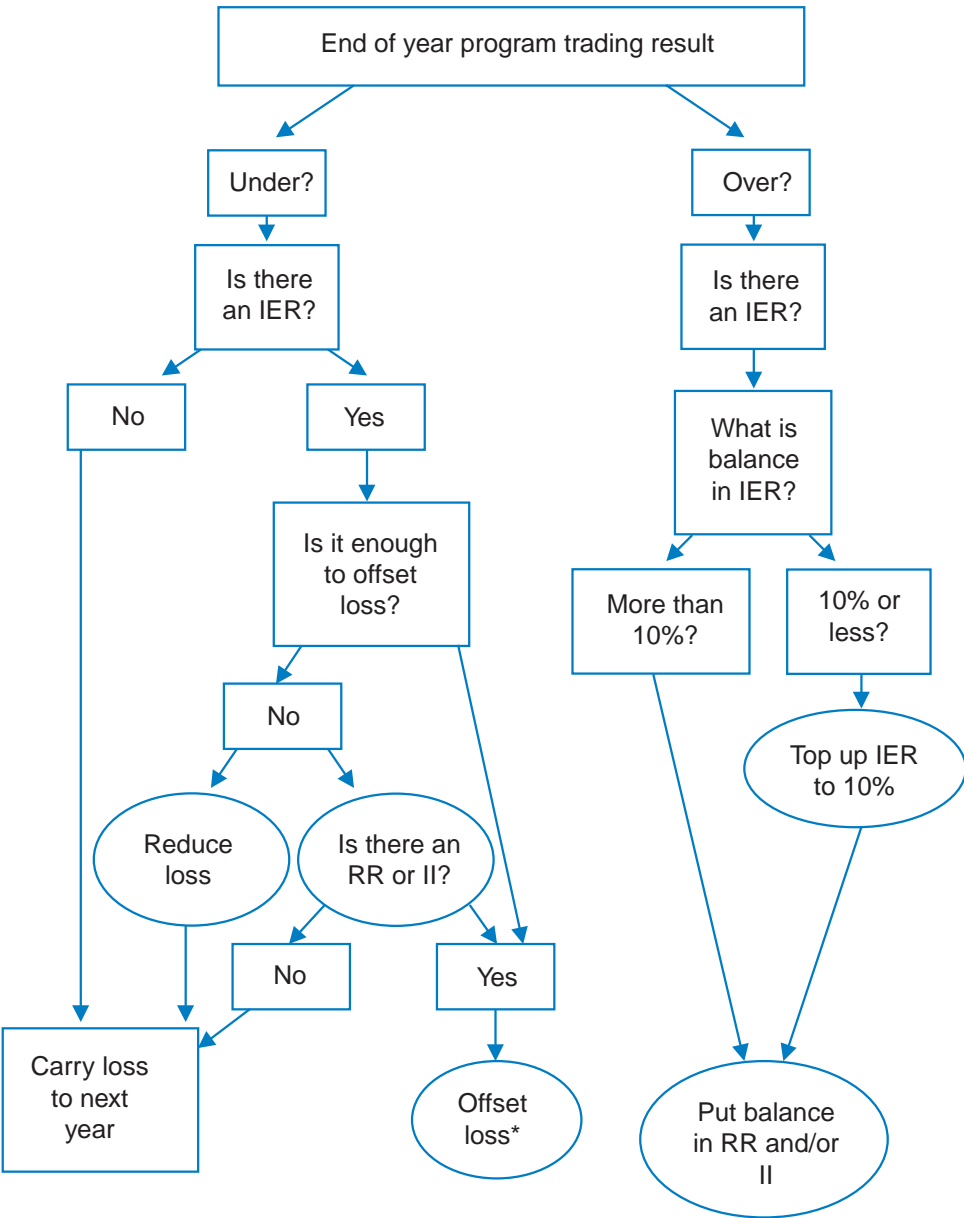
Audit criteria

After consultation and agreement with AQIS, the following criteria were adopted for the audit:

1. AQIS has identified and defined the cost object (entity, activity, program or output) to be costed (including that the boundaries of what is included or excluded are clearly documented, especially where a program also undertakes some appropriation-funded Community Service Obligation activities).
2. The costing methodology is clearly documented and available to all users. It is transparent and is understood and supported by all users.
3. AQIS has fully identified the direct and indirect costs incurred by each recoverable program.
4. AQIS has accurately allocated/attributed the direct and indirect costs incurred by each recoverable program.
5. The method used to assign direct and indirect costs was appropriate in the circumstances.
6. AQIS fully recovers the costs of its recoverable services through appropriate fees.
7. Costing information collected for the decision making and review processes is timely, accurate and sufficiently detailed for all users.
8. AQIS and/or each recoverable program periodically reviews its costing information.

Appendix 8

Decision tree on response to over or under-recovery



Source: Prepared by ANAO from AQIS over-recovery policy.

Notes: IER—Income Equalisation Reserve
RR—Revenue Rebate
II—Industry Initiative

* With the agreement of industry, if the RR or II is to be used to offset the loss.

Appendix 9

Cost drivers used to allocate AQIS' indirect costs 1998–99

Cost Item	Cost Driver
Corporate costs	
Insurance	FTE numbers ^a
Rent on the Edmund Barton Building (Canberra programs only)	FTE numbers
ANAO audit fees	FTE numbers
Internal audit fees	FTE numbers
Comsuper	FTE numbers
Corporate legal	Total direct expenditure ^b
Financial costs	
Ongoing depreciation	Managed by program managers, based on reports provided by the Assets area each quarter ^c
Capital depreciation (new capital acquisitions)	Based on approved capital budgets
Overheads	
Finance	Total direct expenditure
Human Resources	Total direct expenditure
Information Technology	Customised ^d
Regional Support	Total direct expenditure
T&Os	
Director Quarantine and Export Operations	Direct expenditure
Public Awareness	Direct Expenditure
Border Programs Executive	Canberra based FTEs across relevant programs
Animal and Plant Programs Executive	Canberra based FTEs across relevant programs
Program Analysis and Support (Animal and Plant Programs)	Canberra based FTEs across relevant programs
Regional Managers (Quarantine Co-ordinators)	Direct budgets of the operational programs on a region by region basis
Phytosanitary	Historical usage between the relevant programs
Quarantine Detector Dogs	Estimate of usage across the relevant programs
Registration and Documentation (non-meat)	Assumptions made at the beginning of the year regarding uptake by 'non-meat' programs of the EXDOC system
Electronic Documentation (EXDOC non-meat)	Assumptions made at the beginning of the year regarding uptake by 'non-meat' programs of the EXDOC system
Establishment Register	Analysis of total records updated in 1997–98 by program

continued next page

Quality Assurance	Central Office costs to Central Office programs; a weighted average of all Regional QA costs to Regional programs
Training	Program FTEs on a region by region basis
Meat Support program	Contract charge levied on the MID

Notes:

- a) Where costs are allocated on the basis of FTE staff numbers, the BMS calculates each target program's total FTEs as a percentage of the total FTEs for that corporate cost. It is this percentage of the cost that is attributed to the program.
- b) Total direct expenditure is the total expenditure of the program less its overheads. Where costs are allocated based on direct expenditure, each target program's total direct costs are calculated as a percentage of the total direct costs for all target programs. This percentage is then applied to the indirect costs to attribute them to each target program.
- c) Actual depreciation is charged to the programs each four-weekly accounting period. However, from 1 July 1999 AQIS adopted a monthly rather than four-weekly accounting period.
- d) Information Technology was divided into two source pools: office automation and mid-range systems. The costs of office automation were attributed on the basis of a flat fee for each personal computer or workstation. Mid-range systems were attributed according to systems use.

Appendix 10

Overhead costs attribution 1999–2000

For the 1999–2000 budget, AQIS decided to allocate overhead costs to overhead programs ('inter-allocation of overheads'), and to revise the drivers for attributing overheads to other programs.

Inter-allocation of overheads

While the net effect of the inter-allocation of overheads to the overall 1999–2000 overhead budget was zero, there were changes to individual overhead program budgets, both positively and negatively. The Information Technology programs had a combined \$480 000 reduction in the amount to be spread to the non-overhead programs, while the Finance and Business and Regional Support programs had increases between \$200 000 and \$265 000 in the amount to be spread. The table below shows the budgeted impact of the inter-allocation of program overheads to overhead programs.

Budgeted impact of inter-allocation of overheads (\$'000)

<i>Program</i>	<i>Direct Budget</i>	<i>Overheads Allocated</i>	<i>Overheads Received</i>	<i>Revised Budget</i>	<i>Net change in allocations</i>
Business Support Branch Executive	151	(6)	16	161	10
Finance and Business	1 450	(122)	325	1 653	203
Human Resources	648	(65)	71	654	6
Information Technology	4 404	(560)	76	3 920	(484)
Regional Support	2 164	-	265	2 429	265
Total	8 817	(753)	753	8 817	-

Source: AQIS Finance Section.

Revision of cost drivers

The following table summarises the changes to the drivers used for attributing AQIS' indirect costs to its recoverable and non-recoverable programs from 1 July 1999. It should also be noted that, from 1 July 1999, many of the overhead functions performed by AQIS' Business Support Branch were transferred to AFFA's Management Secretariat. AFFA's costs are to be charged back to AQIS and attributed as a corporate cost.

continued next page

Appendix 10 cont'd

Revision of overhead program cost drivers

<i>Program</i>	<i>1998–99 driver</i>	<i>1999–00 driver</i>
Business Support Branch Executive	Direct Expenditure	FTEs across all programs
Revenue	Direct Expenditure	Split into: Receipting—cheques processed Invoices—invoices raised weighted for manual input (weighting: 2 for manual invoice, 1 for automated) Debt recovery—FTEs working on debt recovery
Financial Operations and Services	Direct Expenditure	Split into: Travel—overseas trips Purchasing—purchase order lines processed Credit Cards—number of credit cards held by program Accounts Payable—invoice lines processed Assets Processing—Information Technology assets by program Property—properties by program Fleet—vehicles by program
Other Finance	Direct Expenditure	FTEs across all programs
Human Resources	Direct Expenditure	FTEs across all programs
IT—Office Automation	Number of computers	Number of computers
IT—Mid-range Systems	Use of databases	Use of databases
IT—Records and Mail	Part of IT allocations	FTEs across all programs
Regional Support	Direct Expenditure	Direct Expenditure

Source: AQIS Finance Section.

Appendix 11

Recoverable program budgets 1999–2000

<i>Recoverable program</i>	<i>Recoverable Expenditure (\$'000)</i>	<i>Recoverable Revenue (\$'000)</i>	<i>Surplus/ (Deficit) (\$'000)</i>	<i>Cost-Recovery (Per cent)</i>
Meat	49 723	49 843	120	100.2
Quarantine Import Clearance	34 510	34 650	140	100.4
Airports	19 756	20 242	486	102.5
Grains Exports	6 033	6 100	67	101.1
Horticulture Exports & Dried Fruit	5 373	5 641	268	104.9
Seaports	4 039	4 278	239	105.9
Exports Fish & Other Processed Food	3 875	3 875	-	100.0
Animal Quarantine Stations	2 222	2 305	83	103.8
International Mail	2 288	2 250	(38)	98.3
Live Animal Exports	1 798	1 986	188	110.5
Post Entry Plant Quarantine	1 384	1 384	-	100.0
Exports Dairy	1 081	880	(201)	81.4
TOTAL	132 082	133 434	1 352	101.0

Source: Meat—BMS. Non-meat programs—AQIS Business and Finance Committee Meeting No. 5/00.

Note: Some figures have been rounded.

Appendix 12

AQIS recoverable program over-recoveries 1993–94 to 1998–99 (\$'000)^(a)

	1993–94 Over- recovery	1994–95 Over- recovery	1995–96 Over- recovery	1996–97 Over- recovery	1997–98 Over- recovery	1998–99 Over- recovery	Total Over- recovery	1993–94 Transfer to Meat Program	Payments/ Rebates and Loss Offsets (b)	Over- recovered funds held at 30 June 1999 (c)
Quarantine Import Clearance	4 673	4 658	-	1 587	2 062	-	12 980	948	10 037	1 995
Airports	1 420	147	-	389	1 181	-	3 137	290	2 847	-
Grains Exports	-	3 358	-	1 295	274	1 259	6 186	-	4 499	1 687
Horticulture Exports	-	815	4	-	-	-	819	-	715	104
Dried Fruit	-	-	-	104	7	-	111	-	105	6
Seaports	971	329	-	484	178	-	1 962	196	1 672	94
Exports Fish	-	301	-	23	237	-	561	-	282	279
Other Processed Foods	1 319	-	7	73	4	-	1 403	364	962	77
Animal Quarantine Stations	-	69	92	171	616	367	1 315	-	-	(d)
International Mail	-	-	-	-	38	246	284	-	38	246
Live Animal Exports	1 179	852	63	-	-	-	2 094	239	1 855	-
Post Entry Plant Quarantine	597	-	-	99	65	-	761	122	550	89
Exports Dairy	-	804	-	98	147	-	1 049	-	851	198
Plant Exports	5 937	-	-	-	-	-	5 937	1 205	4 732	-
Meat	-	-	-	-	-	448	448	-	-	(d)
AQIS Training Service	-	-	-	-	44	35	79	-	-	(d)
Total	16 096	11 333	166	4 323	4 853	2 355	39 126	3 364	29 145	4 775

Source: Various AQIS sources.

Notes: a) Some of the above figures vary from those shown in a response by the Minister for Agriculture, Fisheries and Forestry to Senate Question No.610 (Hansard p.5183, 25 May 1999) and figures published in the respective AQIS annual *Report to Clients*. AQIS has agreed the above data are more accurate.

b) Includes total Revenue Rebates and Industry Initiatives paid plus amounts transferred from the Income Equalisation Reserve to offset program losses.

c) Excludes \$1.579 million for the Ballast Water program.

d) Over-recoveries for these programs were credited to equity.

Appendix 13

IER, RR and II movements 1995–96 to 1998–99 (non-meat programs)⁹⁶

Income Equalisation Reserve movements 1995–96 to 1998–99 (\$'000)

Program	1995–96			1996–97		1997–98		1998–99	
	Opening Balance	Movement	Closing Balance	Movement	Closing Balance	Movement	Closing Balance	Movement	Closing Balance
Quarantine Import Clearance	711	-619	92	1018	1110	1556	2666	-2545	121
Airports	146	-146	-	84	84	-84	-	-	-
Grains Exports	114	-114	-	256	256	255	511	47	558
Horticulture Exports	-	-	-	-	-	-	-	-	-
Dried Fruit	-	-	-	14	14	1	15	-15	-
Seaports	120	-120	-	156	156	178	334	-334	-
Exports Fish	146	-116	30	23	53	229	282	-10	272
Other Processed Food	-	-	-	2	2	3	5	-	5
Animal Quarantine Stations	68	-68	-	143	143	-143	-	-	-
International Mail	-	-	-	-	-	-	-	192	192
Live Animal Exports	98	63	161	-105	56	-56	-	-	-
Post Entry Plant Quarantine	-	-	-	58	58	-	58	-11	48
Exports Dairy	76	-76	-	37	37	28	65	-29	36
Other Plant	816	-669	147	-147	-	-	-	-	-
TOTAL	2295	-1865	430	1539	1969	1967	3936	-2704	1232

Revenue Rebate account movements 1995–96 to 1998–99 (\$'000)

Program	1995–96			1996–97		1997–98		1998–99	
	Opening Balance	Movement	Closing Balance	Movement	Closing Balance	Movement	Closing Balance	Movement	Closing Balance
Quarantine Import Clearance	5687	-4271	1416	-587	829	506	1335	-	1335
Grains Exports	-	-	-	1041	1041	-458	583	494	1077
Horticulture Exports	-	-	-	-	-	-	-	-	-
Dried Fruit	153	-153	-	-	-	6	6	-	6
Seaports	811	-811	-	47	47	-	47	-	47
Exports Fish	155	-155	-	2	2	8	10	-3	7
Other Processed Food	-	-	-	71	71	2	73	-	73
Animal Quarantine Stations	-	-	-	120	120	-120	-	-	-
International Mail	-	-	-	-	-	-	-	54	54
Live Animal Exports	1364	-1403	-39	37	-2	1	-1	-	-1
Post Entry Plant Quarantine	-	-	-	41	41	-	41	-	41
Exports Dairy	730	-674	56	-13	43	119	162	-	162
Other Plant	182	-18	164	-20	144	-144	-	-	-
TOTAL	9082	-7485	1597	739	2336	-80	2256	545	2801

Industry Initiative account movements 1995-96 to 1998-99 (\$'000)

Program	1995-96			1996-97		1997-98		1998-99	
	Opening Balance	Movement	Closing Balance	Movement	Closing Balance	Movement	Closing Balance	Movement	Closing Balance
Quarantine Import Clearance	1534	-216	1318	-55	1263	-151	1112	-573	539
Grains Exports	7246	-7246	-	-	-	156	156	-104	52
Horticulture Exports	528	259	787	-404	383	-85	299	-195	104
Seaports	42	25	67	-20	47	-	47	-	47
Live Animal Exports	19	142	161	-105	56	-56	-	-	-
Ballast Water	-	715	715	-618	97	838	934	645	1 579
TOTAL	9369	- 6321	3048	-1202	1846	702	2548	-227	2320

Source: AQIS.

⁹⁶ Although the Meat Industry Division has had over-recoveries, it does not operate IER, RR or II accounts.

Appendix 13 cont'd

Total over-recovery fund movements 1995-96 to 1998-99

<i>Program</i>	<i>1995-96</i>			<i>1996-97</i>		<i>1997-98</i>		<i>1998-99</i>		<i>1998-99 Expenditure</i>	<i>Total Reserves as Percentage of Expenditure</i>
	Opening Balance	Movement	Closing Balance	Movement	Closing Balance	Movement	Closing Balance	Movement	Closing Balance		
Quarantine Import Clearance	7 932	-5 106	2 826	376	3 202	1 911	5 113	-3 118	1 995	31 430	6.3
Airports	146	-146	-	84	84	-84	-	-	-	21 035	-
Grains Exports	7 360	-7 360	-	1 297	1 297	-47	1 250	437	1 687	5 583	30.2
Horticulture Exports ^a	528	259	787	-404	383	-85	298	-195	104	4 728	2.3
Dried Fruit	153	-153	-	14	14	7	21	-15	6		
Seaports	973	-906	67	183	250	178	428	-334	94	4 051	2.3
Exports Fish	301	-271	30	25	55	236	292	-13	279	3 459	10.3
Other Processed Foods	-	-	-	73	73	5	78	-	78		
Animal Quarantine Stations	68	-68	-	263	263^b	-263	-	-	-	2 346	See Note b
International Mail	-	-	-	-	-	-	-	246	246	1 916	12.8
Live Animal Exports	1 481	-1 198	283	-173	110	-111	-1	-	-1	1 689	-
Post Entry Plant Quarantine	-	-	-	99	99	-	99	-10	89	1 266	7.0
Exports Dairy	806	-750	56	24	80	147	227	-29	198	868	22.8
Other Plant	998	-687	311	-167	144	-144	-	-	-		
Ballast Water	-	715	715	-618	97	838	934	645	1 579		
TOTAL	20 746	-15 671	5 075	1 076	6 151	2 589	8 739	-2 387	6 353	76 371	

Source: AQIS.

Notes: a) In 1998-99 Dried Fruits was included as part of the Horticultural Exports program and Other Processed Foods formed part of the Exports Fish program.
b) AQIS does not consider that the Animal Quarantine Stations program has an industry body, therefore, although the program has shown IER and RR credits, it considers that this is inappropriate and these were reversed out the following years.

Appendix 14

Legislative basis for AQIS' fees and charges as at 30 June 1999

<i>Recoverable program</i>	<i>Fee-for-service legislation</i>	<i>Registration charges imposition legislation^a (tax)</i>	<i>Registration charges collection legislation (tax)</i>	<i>Quantity charges imposition legislation (tax)</i>	<i>Quantity charges collection legislation (tax)</i>
Meat	<i>Export Control Act 1982</i>	<i>Export Inspection (Establishment Registration Charges) Act 1985</i>	<i>Export Inspection Charges Collection Act 1985</i>	n/a	n/a
Quarantine Import Clearance	<i>Quarantine Act 1908 Imported Food Control Act 1992</i>	See Note b	n/a	n/a	n/a
Airports	<i>Quarantine Act 1908</i>	See Note c	n/a	n/a	n/a
Grains Exports	<i>Export Control Act 1982</i>	<i>Export Inspection (Establishment Registration Charges) Act 1985</i>	<i>Export Inspection Charges Collection Act 1985</i>	<i>Export Inspection Quantity Charge) Act 1985</i>	<i>Export Inspection Charges Collection Act 1985</i>
Horticulture Exports	<i>Export Control Act 1982</i>	<i>Export Inspection (Establishment Registration Charges) Act 1985</i>	<i>Export Inspection Charges Collection Act 1985</i>	n/a	n/a
Seaports	<i>Quarantine Act 1908</i>	n/a	n/a	n/a	n/a
Exports Fish & Other Processed Food	<i>Export Control Act 1982 Export Inspection (Service Charge) Act 1985</i>	<i>Export Inspection (Establishment Registration Charges) Act 1985</i>	<i>Export Inspection Charges Collection Act 1985</i>	See Note d	n/a
Animal Quarantine Stations	<i>Quarantine Act 1908</i>	n/a	n/a	n/a	n/a
International Mail	<i>Quarantine Act 1908^e</i>	n/a	n/a	n/a	n/a
Live Animals Exports	<i>Export Control Act 1982</i>	n/a	n/a	n/a	n/a
Post Entry Plant Quarantine	<i>Quarantine Act 1908</i>	n/a	n/a	n/a	n/a

Appendix 14 cont'd

<i>Recoverable program</i>	<i>Fee-for-service legislation</i>	<i>Registration charges imposition legislation^a (tax)</i>	<i>Registration charges collection legislation (tax)</i>	<i>Quantity charges imposition legislation (tax)</i>	<i>Quantity charges collection legislation (tax)</i>
Exports Dairy	<i>Export Control Act 1982</i>	<i>Export Inspection (Establishment Registration Charges) Act 1985</i>	<i>Export Inspection Charges Collection Act 1985</i>	<i>Export Inspection (Quantity Charge) Act 1985</i>	<i>Export Inspection Charges Collection Act 1985</i>

Sources: AQIS papers, program managers and legal section.

- Notes:
- a) A tax requires at least two acts of Parliament: an act to impose the tax, and an act to authorise its collection.
 - b) The Quarantine Import Clearance program's 'registration' impost was collected under fee-for-service legislation (*Quarantine Act 1908*).
 - c) The Airports program received the bulk of its revenue through Government appropriations of a portion of the passenger movement charge. The charge was imposed under the *Passenger Movement Charge Act 1978* and collected under the *Passenger Movement Charge Collection Act 1978*.
 - d) The Exports Fish and Other Processed Foods program's fish 'quantity charge' was collected under fee-for-service legislation (*Export Control Act 1982*).
 - e) This covers fees paid by mail recipients for treatments of seized items. However, the International Mail program received the bulk of its revenue from a fee-for-service invoice raised under an agreement between AQIS and Australia Post.

Appendix 15

Meat Inspection program expenditure and revenue 1997-98 to 1999-2000 (\$'000)

	1997-98 Outcome	1998-99 Outcome	1999-2000 Budget
Fixed Costs			
Expenditure			
- Central Office	4 554	3 564	3 069
- Area Offices	3 833	1 805	1 300
- Purchase of Support Services			
Finance	1 941	1 220	1 182
Information Technology	1 291	1 306	1 413
Human Resources	111	866	646
	<u>12 730</u>	<u>8 761</u>	<u>7 610</u>
Revenue			
- Subsidy	3 600	1 400	-
- CSO Funding	-	95	95
- Registration Charges	4 597	4 754	4 700
- Miscellaneous Income	252	289	250
- AMLC Licensing Income	-	164	140
	<u>8 449</u>	<u>6 702</u>	<u>5 185</u>
- Balance	(4 281)	(2 059)	(2 425)
Service Delivery			
Meat Inspectors			
- Expenditure	40 456	29 081	26 349
- Revenue	<u>44 935</u>	<u>31 176</u>	<u>27 369</u>
- Balance	4 479	2 095	1 020
Veterinarians			
- Expenditure	-	9 223	9 119
- Revenue	-	10 143	9 450
- Balance	<u>-</u>	<u>920</u>	<u>331</u>
ATMs			
- Expenditure	2 455	2 533	2 145
- Revenue	<u>1 941</u>	<u>2 163</u>	<u>2 150</u>
- Balance	(514)	(370)	5

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	1997-98 Outcome	1998-99 Outcome	1999-2000 Budget
Overtime			
- Expenditure	4 700	2 937	2 500
- Revenue	<u>4 401</u>	<u>2 330</u>	<u>2 750</u>
- Balance	(299)	(607)	250
EXDOC			
- Expenditure	2 304	2 104	2 000
- Revenue	<u>2 667</u>	<u>2 573</u>	<u>2 939</u>
- Balance	363	469	939
TOTAL			
- Expenditure	62 645	54 639	49 723
- Revenue	<u>62 393</u>	<u>55 087</u>	<u>49 843</u>
- Balance	(252)	448	120

Source: AQIS Meat Inspection Division.

Appendix 16

Quarantine and Exports Advisory Council—Review and Evaluation of the AQIS Horticulture Exports program, June 1999

The Horticulture Exports program ran at a cumulative deficit of \$726 000 between 1996-97 and 1998-99. The review found that the program was financially unsustainable and that the level of accountability to industry has been poor with mainly ineffective two-way consultation and communication. The role of the program was poorly understood by industry and there was scope to improve the program's processes.

Service delivery in the program was found to be:

- inefficient, as a result of the complexity of the program; the high proportion of low volume and irregular users of its services; and the large amounts of non-chargeable travel required of inspectors; and
- inconsistent in its service delivery with the intensity of inspection and the charges for similar inspection services varying among locations.

The financial position of the program has been affected by:

- inefficient financial management arising from its public service environment and the financial management skills of the program managers. Benchmarking of the program's cost-recovery system and service delivery against those of competing countries was recommended;
- the absence of meaningful data underpinning the program's fee structure and performance resulting in a lack of financial management transparency and accountability;
- a narrow revenue base that has created an imbalance and inequity between those paying fees to run the program and those receiving the service. Revision and broadening of the fee structure was recommended;
- the imbalance in the fee structure is compounded by the narrowness of the range of prescribed goods contributing to the cost of the program. Proclamation of all horticultural goods as prescribed goods was recommended;
- the program presently does not recover the true costs associated with all its activities. For example, 10 per cent of the program's expenditure is on the delivery of services at widely dispersed and remote locations with a cost-recovery mechanism that charges an average fee across Australia, regardless of the distance travelled to deliver the service;

continued next page

- an inefficient revenue collection system that relies on the preparation and despatch of invoices after service delivery rather than payment on-the-spot through electronic transaction facilities;
- a high debt level, which reflects the proportion of small, irregular and often seasonal clients. Nationally, 65 per cent of exporters use less than 10 inspections per year (three per cent of total services provided). Upgrading of the program's debt management system and introduction of differential electronic fee payment arrangements, with irregular users to pay upon service delivery and regular users to have commercial credit arrangements with AQIS, was recommended; and
- human resources management. High staff turnover will result in an increased demand on training and support services. Use of casual staff or relevant State Government employees was recommended, particularly in remote locations to improve the effectiveness and efficiency of inspection delivery and minimise travelling time.

In response to the recommendation to revise and broaden the program's revenue base, a subcommittee of the Horticulture Industry Consultative Committee (HICC) prepared a draft schedule of new fees and charges. Following consultations with industry it was proposed that:

- a volume charge be introduced to recover the programs overhead costs and market maintenance costs. The charge is to be based on a sliding scale (between \$1 and \$3 per tonne), differentiating between phytosanitary and non-phytosanitary markets;
- a travel charge be introduced based on the actual vehicle operating costs taking into account the number of vehicles, valuation and travelling time;
- EXDOC user fees introduced to reflect costs of providing services to regular (EXDOC) users and irregular (Non-EXDOC) users;
- registration fees rise by 135 per cent (to \$1500) for Fruit, Vegetable and Nuts premises, while a lower fee of \$650 for Nursery and Flower premises be introduced;
- fees-for-service and certificates be reduced by 41-47 per cent to bring them in line with commercial rates and other programs' rates; and
- a 1900 enquiries telephone number be introduced (the program estimates that 10-20 per cent of certain officers' time is spent providing advice to potential exporters and low-volume exporters).

In November 1999, the AQIS Business and Finance Committee considered and endorsed the AQIS response to the recommendations of the QEAC review and the HICC charging subcommittee.

Index

A

- activity 22, 43, 46, 47, 56, 69, 77, 81, 113
- Airports 13, 15, 29, 34, 37, 49, 50, 56, 57, 59, 72, 78, 85, 90, 106, 108, 112, 119-121, 123, 124
- Animal Quarantine Stations 15, 21, 23, 26, 31, 37, 49, 56, 71, 72, 74, 78, 88, 95, 106, 110, 112, 119, 120, 123
- audit on the Costing of Services 15, 18, 36, 37, 43, 44, 59

B

- Budget Management System (BMS) 32, 104

C

- capital acquisitions 20, 32, 61
- charge 13-15, 17-24, 26, 30-32, 35, 36, 38-44, 48, 50, 53, 54, 56-60, 62, 63, 66, 70, 76-86, 88-94, 96, 108, 110, 116, 124, 126, 128, 129
- charging guidelines 35, 43, 90
- clients 13, 16-20, 22-26, 36, 42, 43, 46, 50, 54-56, 62, 66, 67, 70-72, 74, 75, 80-84, 87-95, 120, 129
- Community Service Obligations 14, 30
- Corporate Governance 48
- cost centre 15, 18, 32, 81
- cross-subsidisation 15, 16, 17, 22, 23, 35, 39, 42, 45, 47, 83, 84-92

D

- Department of Finance 18, 31, 33, 35, 37, 39, 44, 45, 67, 111
- direct cost 19, 33, 36, 42-44, 47-49, 57, 58, 76, 77, 85, 94, 113, 115-117
- downtime 19, 55, 56
- Dried Fruit 15, 34, 37, 49, 56, 59, 65, 89, 106, 119-121, 123

E

- Electronic Export Documentation System (EXDOC) 24, 48, 66, 79, 80, 89, 90, 95-97, 104, 115, 127, 129
- Exports Dairy 15, 34, 37, 48, 49, 59, 67, 78-80, 96, 97, 106, 108, 119-121, 123, 124
- Exports Fish 15, 34, 37, 49, 59, 63, 66, 76, 78, 80, 89, 96, 97, 106, 108, 112, 119-121, 123, 124

F

- fee-for-service 14, 21, 35, 44, 68, 75-79, 108, 124
- fees 15, 17-24, 26, 30-32, 35, 36, 38, 39, 41-44, 48, 52, 54, 55, 60, 63, 66, 68, 72-84, 87-92, 95, 104, 108, 112, 113, 115, 124, 128, 129
- Financial Control and Administration (FCA) 15, 36
- financial costs 48, 115
- fixed cost 21, 77, 79, 90, 126
- free-of-charge services 50

H

- Horticulture Exports 15, 22, 32, 37, 49, 56-59, 64, 78, 80, 82, 88-91, 96, 97, 106, 108, 110, 112, 119-124, 128

I

Import Clearance 15, 19, 23, 37, 38, 46, 49, 52, 56, 58, 64, 66, 70, 76, 78, 85, 87, 106, 108, 112, 119, 120, 122-124

Income Equalisation Reserve 41, 66, 67, 72, 106, 114, 120, 121

indirect cost 19, 33, 42, 43, 47-49, 58, 76, 77, 85, 94, 113, 115-117

industry 15, 16, 20-24, 29, 31, 32, 36, 38, 39, 41, 42, 44-47, 50, 54-56, 58, 60-63, 65-72, 77-81, 83, 86-90, 92-97, 106, 110-112, 114, 120, 122, 123, 128, 129

Industry Initiative 20, 41, 67, 70, 106, 114, 120, 122

interest 20, 23, 40, 48-50, 61, 85-87, 91

International Mail 15, 37, 49, 50, 56-59, 65, 78, 106, 108, 119-121, 123, 124

L

legal advice 35, 38, 44, 66, 68, 86

legislation 14, 21, 35, 66, 75-78, 111, 124

Live Animals Exports 37, 56-59, 78, 90

M

Management Accounting Support System (MASS) 32, 104

meat 14-16, 19-21, 30-32, 34, 36-38, 41, 46, 48, 49, 51, 52, 56, 58, 59, 63-65, 67, 68, 77-80, 86, 89, 90, 95-97, 103, 104, 106, 108, 110, 111, 115, 116, 119-122, 124, 126, 127

Memorandum of Understanding (MoU) 31

N

non-cash costs 19, 33

O

other processed foods 15, 37, 63, 65, 89, 120, 123, 124

over-recovered funds 16, 20, 21, 67, 68, 70-72, 86, 87

overhead 14, 17, 19, 22, 23, 31, 33, 34, 48, 49, 55, 58-60, 65, 85, 115-118, 129

P

policy 14, 15, 18, 20, 21, 23, 25, 30-32, 39-45, 62, 67, 69, 70, 77, 81, 86, 87, 95, 114

Post Entry Plant Quarantine 49, 56, 78, 106, 119

Q

Quality Software Products (Proprietary Software) (QSP) 33, 104, 106

quantity charges 14, 26, 35, 44, 75-77, 80, 124

quarantine 13-15, 19, 21, 23, 26, 29-32, 34-38, 46-49, 52, 56-59, 66, 70-74, 76-78, 81, 82, 85, 87, 88, 90, 94, 95, 102, 104, 106, 108, 110-112, 115, 119-124, 128

R

registration charges 14, 21, 35, 76-79, 108, 124, 126

Revenue Rebate 20, 34, 41, 62, 67, 69, 70, 106, 114, 120, 121

S

staffing costs 17, 19, 52-54

State/Territory employees 54, 56

T

tax 14, 33, 35, 40, 42, 47, 66, 68, 73,
75-78, 124

Technical and Operational Services
(T&Os) 48

time recording system 52, 55

travel costs 80

U

uniform fees 44

user groups 17, 19, 22, 54, 83

V

variable cost 21, 77-79

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