Australian Macadamia Society
submission to
Independent Pricing and Regulatory Tribunal
Review into the development of a funding framework for Local Land Services
NSW
June 2011

Background

The Australian Macadamia Society (AMS) is the peak industry body for the Australian macadamia industry. AMS membership includes over 80% of active growers and around 90% of production.

In NSW the industry is situated from the Tweed River down to Coffs Harbour. NSW produces around 65% of the national crop with approximately 550 growers with a median sized holding of 10 hectares.

The industry annually brings more than $280 million economic value to local communities including over $150 million in NSW alone. Around 70% of the crop is exported providing export earnings to NSW of over $100 million.

This submission is lodged on behalf of the NSW members of the Australian Macadamia Society, the significant majority of who currently pay LHPA rates.

Concerns with the current LHPA rating system

The letter from Minister Hodgkinson to IPART commissioning the review makes it clear service categories should be matched to the most efficient funding option and be imposed where the predominant benefit is captured.

The mandatory one size fits all approach of a notional carrying capacity that been the LHPA model is inefficient and inequitable. There still appear to be no strategic investment plans and cost benefit analysis that set out the work that needs to be done and the budget that would be
required for such work. Consequently the danger is that income will be generated and spent regardless of need or return on investment. Such an approach would not be tolerated in business or indeed most areas of government. As a monopoly service provider there is no market review of costs and charges for many of the services LLS will deliver and no competitive pressure to improve efficiency.

The current system is inequitable. Landholders under 10 hectares, poultry farmers and cane growers do not contribute. Plant industries contribute to a system that is principally geared to animal health and pest issues. Horticultural growers get no benefit from rangers, vets, TRS and stock monitoring yet, at the very least, contribute to the overheads and administration of these services. Special levies such as the locust levy mean that landholders in the northern rivers are subsidising farmers in locust affected areas.

The current system is archaic. The system reflects a rural environment the northern rivers have not seen for over 30 years with a significant livestock producers remaining and most farms horticultural or lifestyle. The new approach to equitable and transparent industry funding is that used for R&D and marketing levies through the RDC model. Contributing industries must be consulted, must have a positive vote by a majority of production and producers and must have an agreed strategic investment plan against which funds collected are spent. Any new funding framework must address these issues otherwise the problems that plagued the LHPA will carry over to the LLS.

**Issues for stakeholder comment**

1. **Cost recovery principles**
   In the main the AMS agrees with the IPART principles. However a few points should be made: The principles appear to assume that some compulsory levy or rating system is required. This should not automatically be applied to all landholders as this would be contrary to other principles.
   It is important that this is clearly acknowledged as an additional form of taxation on affected landholders. This taxation should not come without adequate representation. The AMS understands that the majority of LLS board membership will be appointments made by the Minister. This will leave, in most cases, three or less board members to represent the interests of a very diverse group of tax payers. This is not seen as adequate representation and until this issue is addressed no levies or rates should be imposed.
   Obviously the best way to ensure that costs are effectively managed and targeted is to maximize the use of fee for service. If the service is not needed or the costs are not deemed effective, the service will not be used. One of the important principles enunciated is that the
“the party charged should be able to capture enough of the benefits of the service to be prepared to pay for its provision”. This was clearly not the case with the LHPA as far as horticulture was concerned with the result that there were high levels of dispute, default and litigation and resulting inefficiencies and costs.

Some additional principles that should be considered:

- That the implementation of cost recovery for LLS is not used by the State Government to shift costs previously and legitimately borne by government to industry. There has been a long history of government shifting previously consolidated revenue funded costs to industry and this should not be allowed to happen here. This would particularly apply to services previously covered by NSW DPI. There is much reference to the policy outcomes sought by the NSW Government. This should not automatically imply that this is justification for charging rural land holders above and beyond their taxes.
- Where industries already have agreed funding mechanisms in place to cover the provision of certain services, no further cost recovery should be imposed. This would apply to components of advisory services, pest management and biosecurity. The macadamia industry already applies one of the highest statutory levy rates in primary production to its members to provide comprehensive extension and advisory support through HAL. Similarly the HAL levy funds significant pest and disease monitoring and management programs. Most horticultural industries already have cost sharing arrangements in place for biosecurity through Plant Health Australia. None of this should be duplicated simply to support the establishment of LLS.

2. Other jurisdiction models
The AMS strongly supports the Productivity Commission’s 2001 criteria for cost recovery models.

The Frontier Economics Report for DPI Victoria makes the important point that funding arrangements should only be used to meet gaps in Biosecurity arrangements not addressed by existing arrangements.

Industry specific R&D levies (in horticulture’s case through Horticulture Australia Limited, an industry owned company) pay for area wide plans and pest management. These can be;

- national and across all horticulture as in the case of fruit fly,
- specific to an individual industry as in the case of banana bunchy top
- specific to a region as with fruit spotting bug control for tropical horticulture
- crop and locality specific as in the case of nut borer for macadamias

The point is; this system is flexible, highly responsive to industry needs and funded in an equitable and transparent manner.
3. IPARTs approach; staged questions
The staged questions approach is sound. It is important to note however that “landholders” and “industry” are not homogenous sectors and within these groups there are often very different needs and requirements. The plant industries and landholders who do not run livestock cannot be included as beneficiaries of animal health based services. Nor should landholders who are part of industries that already provide comprehensive pest and disease monitoring and management levy based programs be treated the same as those requiring these service. The groupings of ‘landholder” and “industry” will need to be disaggregated when the staged question approach is used.

4. Determining the demand for services. Risk generators and beneficiaries
The process undertaken in boxes 5.2, 5.3 and 5.4 is clear although it will need to be more specific about which landholders and which industries. This cannot be emphasised enough. The current LHPA process has led to significant dispute, defaults and litigation due to the perception that rates were being imposed for services not needed or delivered. Horticultural and other cropping landholders will not use animal health related services. Plague locust services are not relevant to the northern rivers regions. Further information on specific industry needs for particular products and services could be sought from a variety of sources. Have DPI and LHPA kept records of who has used their services in the past?
Most industries that work with a Rural R&D Corporation have Strategic Investment Plans. The AMS can supply a copy of the Macadamia Strategic Investment Plan 2009 – 2013 on request. These identify areas of need and importantly preparedness to invest including biosecurity, extension and advisory and environmental stewardship.
It is essential that, as the LLS is intended to service all rural landholders and industries, rather than just the livestock industries that the LHPA focused on, all previous LHPA service and products be reviewed and not carried into the new organization without a clear business case for their continuation. A fee for service model for these elements would quickly establish the level of need and which sectors were prepared to pay for them.

5. Sliding scale for apportionment of costs
The sliding scale approach is simple and clear. It is however a rather blunt instrument to use at a regional level where the specifics of landholder demographics is much better understood and more important than at a national level. Also the service being offered by bodies like PHA are at a much more generic and strategic level and a broad bush sliding scale is more appropriate there than at regional LLS level.

6. A risk matrix for cost apportionment
The same could be said of the risk matrix approach. While it may have merit as a starting point and way of broadly categorising areas of activity for the LLS, it should not be used to determine the relative cost recovery obligations for specific landholders or industries. This approach as outlined in the issues paper appears to assume that all industries and all landholders will have similar benefit and risk creation profiles for the various services offered by the LLS. This is simply not so. To ensure equity and fairness, each category of private beneficiary would need to be divided numerous times (between animal and plant industries, between horticultural and broad acre cropping, etc) adding to complexity and cost. The three step process outlined could easily become a 6 or 7 step process.

If some version of the risk matrix approach is used, it would need to involve regional LLS Boards consulting and negotiating with affected landholders and industries to determine equitable % splits in each case. A one size fits all approach would lead to continuation of the inefficiencies and inequities that have been identified in at least 3 previous reviews of the LHPA.

7. Assigning weights
These same problems apply to weighting for sectors against impact; how specifically will the sectors and their weightings be determined?

8. Stakeholder Reference Panel outcomes
The variation in the three stakeholder reference panel allocations make it clear how regionally specific the risk generation and capture of benefit can be for many of the services the LLS intend to provide. As noted, it also reflects the makeup of the stakeholder reference groups. Almost no horticultural industries were represented in these groups, including the Coffs Harbour group. The need for further disaggregation of “industry” is clear through the varying responses for activities around animal health, tagging and stock routes to mention just a few.

The AMS is disturbed by the reference in Chapter 6, page 48 to government potentially fixing or restricting its cost share? How would such a decision fit with the principles outlines at the front of the issues paper? On what basis could government be allowed to fix its share yet industry and landholders be exposed to unlimited apportionment? This would make a complete mockery of the entire cost sharing framework.

9. Cost share discretion for LLS boards
These results would highlight the need for regional LLS boards to have some discretion as to the relative cost apportionment were it not for the fact that a majority of these boards will be Ministerial appointments. This is a critical issue as having unrepresentative government appointments making these decisions cuts across most of the principles outlined at the beginning of the Issues Paper. If the LLS boards are truly representative of those that will pay the costs, then discretion for these boards is a sound principle.
10. IPART approach to cost apportionment
As tools to form part of a flexible and targeted approach to apportionment of cost shares all the tools covered in the IPART issues paper are appropriate and useful. None however provide the solution in and of themselves. The principles on which the paper is founded are sound and should be adhered to. Each method has some role to play and could be used as part of an apportionment that takes into account:

- Existing industry and landholder (levy payer) arrangements for funding the specified activities through other structures and means
- The obligations the NSW Government already has to fund the activities in question through arrangements such as Plant and Animal Health Australia, commitments under projects funded through RDC (these often include significant and specific funding for extension and research adoption services to industry and regional groups), Primary Industries Ministerial Committee and other COAG agreements
- Opt out provisions where individual landholders or industry sectors can demonstrate that they do not need or will not use the service

One issue that has not been adequately considered in the issue paper is how the “industry” component of any cost apportionment would be collected. There is mention of industry levies. It is the AMS’ understanding that under the Constitution, mandatory State based levies on particular products that are traded nationally can be interpreted as an infringement of free trade across State borders and would, consequently, not be constitutional.

11. Information on appropriate split
As stated above, further information on specific industry needs for particular products and services could be sought from a variety of sources. Have DPI and LHPA kept records of who has used their services in the past?
Most industries that work with a Rural R&D Corporation have Strategic Investment Plans. The AMS can supply a copy of the Macadamia Strategic Investment Plan 2009 – 2013 on request. These identify areas of need and importantly preparedness to invest including biosecurity, extension and advisory and environmental stewardship.

12. What rating base
The notional carry capacity rating base is not transparent, it is inequitable and it is contrary to all the cost allocation principles that the Issues paper espouses. It should not form part of the LLS funding mix.
There appears to be an assumption in the Issues Paper that the current LHPA rating approach is the default and that the views of the current LHPA boards should carry weight in determining
the way forward. Both the Ryan and Bull reports found significant fault and shortcoming with
the management of rating by the LHPA and its predecessor and with the governance of the
boards. The fact that IPART is unable to determine the cost of each LHPA board’s collection
mechanism is just one indicator of how inadequate LHPA arrangements are.
Any funding mechanisms for the LLS should not use the LHPA model as either a default or a
starting point. This model has been shown to be inefficient, ineffective, inequitable and to have
caused significant challenge and litigation.
An area rating base is the most equitable as long as it is only applied to those costs and services
where it has been clearly established at the regional level that there is a significant benefit
and/or risk creation on the part of the landholders affected.
There should be an opt-out provision for any rate or levy where the affected party can
demonstrate sufficient lack of benefit or mitigation of risk creation.
Any general rate or environmental rate should be calculated at a level that will cover only those
costs that relate to the core functions and services meeting all of landholder needs. Public good
functions and their costs should be transparently covered by consolidated revenue funding from
the State Government. Private or specific industry sector benefit activities should not be funded
through general or environmental levies applied to all landholders. These costs should be
recovered by more targeted rates or fees.
Animal health and pest and insect levies should only be applied to those sectors and landholders
that directly create the risk or capture the benefit. There should be no cross subsidisation.

13. What fee collection system
The AMS does not believe the current LHPA collection mechanism works. The LHPA boards
appear to believe they have an entitlement to all funds and have prosecuted collection in an
aggressive, arrogant and ultimately counterproductive manner.
Local government collection mechanisms could be used with the support of relevant LGAs. At a
collection cost of 5% it is likely to be considerably more efficient than existing LHPA mechanisms
and also more cost effective than the Leviers Revenue Service that collects R&D and marketing
levies under the PIRD Act. LRS costs vary depending on the point in the supply chain at which
they are collected but as a rule, when collected directly from the levy payer (land holder) can be
in excess of 10%.

14. Exemptions and reductions as incentive to reduce risk
As covered elsewhere in this submission, there is a need for a funding mechanism that provides
clear exemptions where services are not required or no benefit is captured or no risk is
generated. This should be in the form of an opt-out clause for all fees, rates and levies.
The criteria for such exemptions set out in Box 7.1 are fair and reasonable. Determining the
applicability of an exemption should not be left to boards dominated by government appointees
or to any officer, board or committee where there is a potential conflict of interest to maximise income of the LLS. Ryan and Bull found this to be the case with LHPA application of rates. There should be the option of rebates or reductions in fees or rates applied to those seen as creating risk in a particular area of LLS activity where it can be demonstrated this risk has been mitigated to an appropriate extent. Similarly, exemptions, reductions or rebates should be applied where it can be shown the landholder or industry affected has met their obligations to contribute to outcome or risk reduction through other means. An example might be where a landholder has undertaken voluntary biosecurity risk mitigation or has contributed to natural resource management outcomes.

15. Lessons from other jurisdictions
The main lessons to be learned are from the funding approach used by the LHPCA. This system of rating based on a notional carrying capacity and applied to landholders without any consideration of their need for LHPCA services, their creation of the risks LHPCA sought to mitigate or the ability to capture the apparent benefits of LHPCA activity led to three reviews over 10 years and countless hours and thousands of dollars wasted in dispute, litigation and debt collection activities. Any new system needs to follow the principles set out in the Issues paper and not digress from these for political purposes or expediency.

**Conclusion**
The AMS position is:

1. The principles appear to assume that some compulsory levy or rating system is required. This should not automatically be applied to all landholders as this would be contrary to other principles.
2. Government appointment of the majority of LLS boards will leave, in most cases, three or less board members to represent the interests of a very diverse group of tax payers. This is not seen as adequate representation and until this issue is addressed no levies or rates should be imposed.
3. One of the important principles enunciated is that the “the party charged should be able to capture enough of the benefits of the service to be prepared to pay for its provision”. This was clearly not the case with the LHPCA as far as horticulture was concerned.
4. Some additional principles should be; cost recovery for LLS is not used by the State Government to shift costs previously and legitimately borne by government to industry: and, where industries already have agreed funding mechanisms in place to cover the provision of certain services, no further cost recovery should be imposed.
5. The AMS strongly supports the Productivity Commission’s 2001 criteria for cost recovery models.
6. The groupings of ‘landholder’ and “industry” will need to be disaggregated when the staged question approach is used.
7. All previous LHPA services and products be reviewed and not carried into the new organisation without a clear business case for their continuation. A fee for service model for these elements would quickly establish the level of need and which sectors were prepared to pay for them.
8. The risk matrix approach as outlined in the issues paper appears to assume that all industries and all landholders will have similar benefit and risk creation profiles for the various services offered by the LLS. This is simply not so.
9. Government should not be allowed to fix its share while industry and landholders are exposed to unlimited apportionment. This would make a complete mockery of the entire cost sharing framework.
10. Having boards with a majority of unrepresentative government appointments making funding decisions cuts across most of the principles outlined at the beginning of the Issues Paper.
11. The issue of how the “industry” component of any cost apportionment would be collected has not been well covered. Mandatory State based levies on particular products that are traded nationally may not be constitutional.
12. The notional carry capacity rating base lacks transparency and equity and is contrary to all the cost allocation principles that the Issues paper espouses. It should not form part of the LLS funding mix.
13. There should be no cross subsidisation

For further information, please do not hesitate to contact Australian Macadamia Society Chief Executive Officer Jolyon Burnett at the AMS office on (02) 6622 4933.

Yours sincerely

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