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JOINT STANDING COMMITTEE ON DELEGATED LEGISLATION

COST RECOVERY GUIDELINES

TRANSCRIPT OF EVIDENCE TAKEN
AT PERTH,
ON WEDNESDAY, 19 MARCH 2003

Members

Ms M.M. Quirk (Chairman)
Hon Ray Halligan (Deputy Chairman
Hon Ljiljanna Ravlich
Hon Robin Chapple
Hon Alan Cadby
Mr R.N. Sweetman
Mr P.B. Watson
Mr T.K. Waldron

Committee met at 10.00 am

DOYLE, MR GRAEME
Director, Financial Policy,
Department of Treasury and Finance,
examined:

DUCA, MR ADRIAN
Assistant Director, Agency Resources,
Department of Treasury and Finance,
examined:

The CHAIRMAN: On behalf of the committee, I welcome you to the meeting. You have both completed and signed a document entitled "Information for Witnesses". Have you read and understood that document?

The Witnesses: Yes.

The CHAIRMAN: The proceedings are being recorded by Hansard and a transcript of your evidence will be provided to you. To assist the committee and Hansard, please quote the full title of any document to which you refer in the course of the hearing and please be aware of the microphones and try to talk into them. To start with, can you outline your respective roles because that might assist us in deciding how we should direct our questions?

Mr Doyle: As director of financial policy, I have responsibility for developing and implementing financial reforms and financial management policies for the public sector and government agencies and for developing and advising on financial legislation such as the Financial Administration and Audit Act and the associated Treasurer's Instructions. We give advice on the drafting of Bills to ensure they are consistent with that legislation, and we give advice to agencies and government on accounting policies such as pronouncements issued by the Australian Accounting Standards Board.

Mr Duca: I am responsible for a team within the budget area of agency resources at the Department of Treasury and Finance. I have direct responsibility for the budgets of a number of portfolios. My role is to work with agencies in developing appropriate budgets and to provide advice to the Treasurer on the budgets of agencies. Part of that role is to look at the raising of fees and charges by agencies, and that is probably why I am here today. There is also the expenditure side of the job as well. Basically, my role is to help agencies develop appropriate budgets and to provide advice to the Treasurer on the appropriate budget for a number of portfolios.

The CHAIRMAN: The committee is looking at fees and charges. We are particularly concerned that we must constantly examine in some detail the process whereby an agency or a local government arrived at a particular fee level. We believe there is not a lot of consistency in how that process takes place. We are canvassing ways in which maybe an overall scheme can be developed, so that the issue of whether something is a fee or a tax will arise less frequently and there will be no need for those of us who are not bean counters to frequently revisit the issue.

The committee forwarded to you the guidelines on costing and charging for public sector goods and services, which was prepared by the New Zealand Audit Office. Have either of you had occasion to look at that?

Mr Doyle: Yes, I have read through it. It is quite old now; it was written in 1989. However, the principles in the document are consistent with the principles in the Department of Treasury and Finance's "Costing and Pricing Government Outputs: Guidelines for use by agencies". The principles espoused in the New Zealand document are consistent with the way we advise agencies on guidelines for costing their services and applying user charges when full cost recovery is to be applied to those charges.

The CHAIRMAN: You have issued a similar publication; is that correct?

Mr Doyle: Yes, that is correct.

The CHAIRMAN: Have you noticed whether there is anything in the New Zealand publication that is not in your guidelines that you think is a good idea?

Mr Doyle: Our guidelines are much more comprehensive than the New Zealand ones and run to some 120-odd pages. They also address other issues such as competitive tendering and contracting. There is quite a lot of case study material in our guidelines as well. My view is that our guidelines are far more comprehensive than the ones provided by the New Zealand office.

The CHAIRMAN: I note that you have a number of copies of that report. Can you provide them to the committee?

Mr Doyle: Yes.

The CHAIRMAN: How long have those guidelines been in force?

Mr Doyle: The current edition was last updated in October 2001. That is the fourth edition. The first edition was issued in approximately 1994.

The CHAIRMAN: In addition to government agencies and statutory authorities, who else is provided with these guidelines or to whom are they intended to apply?

Mr Doyle: The guidelines are intended to assist agencies in costing their services; that is, to recover through fees by setting prices for the goods or services they charge for. That is their primary intention.

The CHAIRMAN: What about local governments? Do they do their own thing?

Mr Doyle: Yes. Our guidelines are directed at state government agencies.

The CHAIRMAN: Is there any general oversight of the setting of fees by Treasury?

Mr Duca: Agencies are required to review their fees and charges annually as part of the annual budget process. We have just gone through the current budget process. By about December, the agencies have made submissions about the fees and charges that they will raise. The Department of Treasury and Finance examines those submissions, provides recommendations to the cabinet expenditure review committee, and the expenditure review committee sits down with the responsible minister and approves or otherwise changes those recommendations. That is a normal part of the budget process, as are the submissions on expenditure, for example.

The CHAIRMAN: In other words, it is looked at from the perspective of an agency expecting to raise X amount of revenue by raising fees five or 10 per cent or by imposing a fee for X or Y service?

Mr Duca: Correct. We provide guidelines to the agencies. Basically, the standard that is applied is the Perth consumer price index based on the year September to September. Agencies are applying that at a current rate of 3.3 per cent. The advice is for agencies to at least keep up with inflation when appropriate to cost recover as much as possible. However, there are issues such as the community service obligation for a particular service. Those are the sorts of issues on which government makes decisions in terms of how much agencies intend to cost recover. On the expenditure side, the budget provides for those services anyhow, but it is up to agencies to recover as much as possible on what is seen as a good or a service.

The CHAIRMAN: As each process is undertaken, is there any sort of examination of whether the particular proposal complies with these guidelines, or is it more a big picture analysis?

Mr Duca: We do not go through it in detail with the guidelines, but we ask basic questions such as: are you attempting to fully cost recover; are you recovering at least CPI; are you trying to increase the scope; or are you raising new fees and charges? We ask some of those basic questions on which government expects some advice. However, we do not go through it in a lot of detail. Sometimes when we sit down with agencies and they ask us about their proposal, we use this document as the bible for how to approach fees and charges, because some agencies have a more advanced fees and charges regime. Also, some agencies have a greater capacity than other agencies. That is the nature of their work. You would not expect a pure public service agency to charge for a lot of its services, because in essence it is there to provide a service to the public. We expect other agencies that have a more commercial focus to take a more rigorous commercial approach to fees and charges.

The CHAIRMAN: A situation arose about eight months ago whereby we disallowed some fees for the registration of businesses because they were above cost recovery. That would be consistent with what you are saying; that is, Treasury does not go through these proposals with a fine toothcomb.

Mr Duca: That is right. However, when an agency seeks to make a major change of above 20 per cent in cost recovery in any year, the Cabinet is required to sign off on it. Anything under that and within cost recovery will go to the expenditure review committee and ultimately to Cabinet to sign off on.

The CHAIRMAN: Are you saying that an assertion by an agency that something is for cost recovery tends not to be examined?

Mr Duca: No.

Hon LJILJANNA RAVLICH: When you talk about full cost recovery, are you talking about 100 per cent or are you talking about 20 or 30 per cent, and therefore defining it as full cost recovery when in effect it is only full cost recovery when it is compared with an agency that has only one per cent cost recovery or something along those lines? What do you mean?

Mr Duca: It is really looking at the good or service that is provided, looking at the inputs to that and trying to recover at least the cost of those inputs. For example, under the reforms that have been introduced in the past few years, we apply a capital user charge. We expect full cost recovery to incorporate all of that.

Hon LJILJANNA RAVLICH: You have all the determinants of the full cost recovery of an output and they are pretty clear. I have some concern because, for example, there are a number of issues with the cost recovery model. First, consumers jack up and say that they already pay taxes so why should they have to pay for the cost of a report that used to be free. Secondly, from an agency point of view, you probably wonder at the end of the day whether they are any better off. For example, the Department of Fisheries is fairly advanced as an agency that recovers a high percentage of its costs. The bottom line is that it still must front Treasury and probably still has its hand out for an additional Treasury allocation. If that agency has a high level of cost recovery, where is the merit in the model? All government agencies seem to be asking for an increase when it comes to the budget allocation; yet, technically, the amount they recover in their cost component should be taken off the bottom line. They should go to Treasury every year and seek less money, but that does not seem to happen. Can you explain why that is not the case?

Mr Duca: It is an issue of excess demand over available resources. If providing agencies with an incentive to better manage their goods and services and the way they are funded is a way of meeting some of that excess demand, that is a positive. However, in the past few years we have found that there was excessive use of a lot of the free goods and services that were being supplied and there was no good accountability of the extent to which people were using them. If a service is free, people will get as much of it as they can. Obviously, it is up to government to decide where that balance lies; whether a fee or a charge needs to be raised, whether a community service obligation should be provided free or whether the community has a realistic expectation that it should pay something for the good or service. It is a grey area, but it is up to government and certainly the Department of Treasury and Finance to provide advice on that.

Mr Doyle: There are four main broad reasons that an agency would charge for a good or a service that is produced by government. The first is if it is economically responsible to do so to ration the demand for that particular good or service and, in some cases when there is competition in the private sector, to prevent distorted price signals. If a service was free in the public sector but had a cost in the private sector, that would cause excessive demand on the public sector for the good or service and would take up public sector resources. The second reason is if it is environmentally responsible to do so; for example, water issues. Obviously we have obligations to look after the environment. Social responsibility is another reason. In some cases it is unjust for the people whose choices lead to their not needing a particular good or service that is provided through the public sector. It would be fair for them not to pay for it through their taxes; for example, drivers licences, vehicle licences, etc. The other overarching broad reason is when it is fiscally responsible to do so to free up the finite nature of the public sector resources so that they can be directed towards the highest priority areas. Those four reasons are not necessarily divorced from each other. A particular good or service may fall across all those areas. It is a balancing act, as Mr Duca said.

Hon LJILJANNA RAVLICH: Has the Government or Treasury set a target at which it would like to pitch that cost recovery percentage mark? You have mentioned a figure of 20 per cent. As resources diminish within the public sector, there is less to go around and there is additional pressure on resources, I can see that you might work towards a target of 40 or 50 per cent. Is there a target and when do you anticipate reaching that target?

Mr Duca: No target has been set. We continually encourage agencies to review their cost recovery. If we had to set a target, because of the very diverse nature of agencies and the goods and services they provide, it probably would not be equitable. A number of people look at each agency’s individual circumstances. As I said before, for some agencies it makes much better sense to try to achieve full cost recovery. However, we are happy as long as we can see that other agencies are making an effort to at least keep up with the pace of inflation or to gradually cost recover, maybe at a slower rate over time. We do not have an overall target.

[10.20 am]

Mr Doyle: Pages 28 and 29 of the Western Australian costing and pricing guidelines make some statements about cost recovery and when it should apply. For example, the Government may set fees and charges at a level less than at cost recovery if there are positive externalities; for example, school fees. We will never fully recover costs of school fees. There may be some legislative restrictions in imposing full cost recovery. It may not be appropriate to charge full costs in some other circumstances due to the unique nature of the size of Western Australia. Unless there is a government statement or legislation saying that we should not cost recover, as Mr Duca said, we do encourage agencies to charge full cost recovery for their goods and services.

Hon ALAN CADBY: It could be seen that in a cost recovery model, we are supporting inefficiencies of agencies. If that is the case, what incentives do agencies have to become more efficient if they get the money irrespective of their costs?

Mr Duca: As part of the budget process, agency expenditure is reviewed, compared and benchmarked aside from the cost recovery aspect of that expenditure.

Hon ALAN CADBY: Benchmarked against what or whom?

Mr Duca: We measure against prior years and interjurisdictional benchmarks. There are a number of ways in which that is done. Every agency is unique. We cannot compare the performance of the Police Department of Western Australia exactly with that of the Police Department in Victoria. However, we get some sort of basis for asking questions. The agency would point out differences.

For example, travel factors in Western Australia might be an issue. We rely a lot on the Productivity Commission reports that are produced annually. Your point is valid in that if agencies were automatically allowed to retain their revenues without any scrutiny, that would not be equitable. However, agencies continually argue - excess demand over available resources - their capacity to meet that excess demand. If they can use the funding generated from cost recovery or if they keep pace with inflation that is a lesser demand placed on government from the central pot. We take all those things into account when assessing each agency.

Hon ALAN CADBY: Where is the incentive for an agency to become more efficient so that more money goes to core business rather than being tied up in administration.

Mr Duca: Invariably much of the money retained goes back into expanding the scope of the service or growing a related service. Every year some new fees and charges are raised because a new service is identified. The incentive is there for agencies to say that to the extent they can cost recover, they can put the money back into the business to provide a better service or quality, or more of the same.

Hon ALAN CADBY: Does Treasury have a role in looking at the efficiency of a department?

Mr Duca: Yes. We work with them all the time. As part of the budget papers you will see that we have performance measures to work with agencies and to try to encourage them and ask questions about their meeting their targets. We ask them about the targets and how they are developed. We go into their businesses and examine what they are doing. The incentive is there to the extent that they can justify those measures and demonstrate that the achievement of targets is valid. That is good. In areas in which we find inefficiency we ask the expenditure review committee whether the Government wants to keep purchasing the inefficient service. There are areas in which services have been withdrawn or the Government says it no longer wants to purchase a service. That is our role. It is an ongoing process. It happens once a year with every budget but it is a 12-month process. We continually review agencies' performance.

Hon ALAN CADBY: Have you identified agencies that are inefficient?

Mr Duca: They are continually identified as part of the budget process. I am not referring to an agency, but part of an agency. Agencies have divisions that have different outputs. We question why certain outputs cost more than others, and we undertake benchmarking. The agency must respond. As part of the budget process the chief executive officer and the minister must address why an agency is inefficient.

Mr Doyle: We ask why a particular service costs as much as it does. If an agency is charging for a service we ask why it does not recover the full cost of the service if no other government explicit statement exists along those lines. The benefits of the user charging in that regard is that arrangements are in place for net appropriation determination whereby departments can retain their own operating revenue from fees and charges. It is normal for statutory authorities to retain their revenues from their services under their governing legislation. The ability to retain those revenues is an important incentive for agencies to seek to become more efficient to free up resources, whether it be through appropriation resources from the central Government or from their own operating revenues to generate resources or free up resources to put into the higher priority areas of the agency and, in the wider picture, to free up resources to be released to perhaps other higher priority areas of government.

The CHAIRMAN: Other than costing and pricing government outputs, are there any other government policy statements or directions on cost recovery?

Mr Doyle: There are no other explicit statements.

The CHAIRMAN: Is this self contained and seen as "the bible"?

Mr Doyle: In terms of the methodologies for accurately costing services and in setting charges based on cost recovery, whether it is full cost recovery or a percentage thereof, they are the guidelines.

The CHAIRMAN: In 2001 the Productivity Commission released a report and made certain recommendations. Are they covered in this latest version of the guidelines?

Mr Duca: I do not think so. This is the October 2001 version. It is probably due for review in the next 12 months or so.

Mr Doyle: We referred to the Productivity Commission, but its report also refers to when full cost recovery should be applied. Our guidelines do not refer explicitly to when full cost recovery should be made. They make the assumption that if a Government decides on full cost recovery, that is how it is done.

The CHAIRMAN: In general terms, are there any serial offenders who breach these guidelines? Have you struck any difficulties with any agencies not complying with these guidelines?

Mr Duca: Certainly as part of the review of fees and charges, agencies are pretty good at identifying fee increases. It is a matter of the agency profile. If an agency's profile leads it to be a heavy fees and charges type of agency, there is a lot more emphasis at our end and at their end. When core public sector agencies might raise less than one per cent of their costs, it is a matter of care and maintenance. It is about putting effort into areas that deem it necessary. I could not identify any agencies that are not meeting their obligations.

Hon ALAN CADBY: You referred earlier to social responsibility. I suppose some agencies or departments are exempt from cost recovery. The Commissioner of Police referred to cost recovery for a child's action some time ago. He referred to the estimated cost to put out a fire and the cost of the police and fire services at $100 000. What is Treasury's position on the actions of the public, such as the cost of a search for a child? We all have the view that Treasury is after as much money as it can get hold of. It seems to be a wonderful way of raising money.

Mr Duca: Obviously, Treasury wants as much money as possible. However, in a case like that it is for governments to decide. It is a matter of policy. Our advice to government is to do whatever it likes to try to raise as much money as it likes. We would not comment on those issues.

Hon ALAN CADBY: There is a view that some agencies are exempt from the cost recovery model.

Mr Doyle: There are no explicit exemptions, but, in the review of fees and charges that is conducted annually, one part of the review is a sensitivity analysis. Agencies and the Department of Treasury and Finance are required to identify sensitive issues in any proposals that are submitted. In that case, it is brought to the Government's attention and the Government will make a decision on whether to apply a form of charge, whether it be cost recovery or some other fee. Treasury would need to assess the impact on the community and how sensitive the community might be towards that charge.

The CHAIRMAN: Government policy must address the extent to which taxes, for example, increase in a year. Obviously certain political commitments must be met by government on the quantum of any tax increases. For example, local government might decide to increase a fee by, say, 1 400 per cent. Those fees would not be subject to this process; yet they would be an input cost on small business. Would they not have some impact on the overall strategy to maintain only small tax rises, for example?

Mr Doyle: In terms of local government?

The CHAIRMAN: I am saying that external fees set without much oversight by Treasury have some impact on any contention that fees and charges are not rising, or they send signals that costs are rising. I am saying that only a portion of the taxes that are imposed are subject to Treasury scrutiny. Do those other fees still impact on the community?

Mr Doyle: Local government is outside our jurisdiction.

The CHAIRMAN: I am not suggesting there is any difficulty. I am asking whether high fee hikes in areas outside of Treasury's responsibility have the potential to erode its policy to maintain charges and fees at a reasonably low level of increase?

Mr Duca: I suppose that the answer is yes. We can only look at the fees and charges that are raised -

The CHAIRMAN: We are not sheeting home blame. One of the committee's concerns is that there should be an overall strategy. The fact that some fee setting is outside Treasury's control is not necessarily a good thing in overall strategy, policy and consistency of approach.

Mr Duca: That is right. It also impacts on our agencies. The price of fuel has increased, for example, so our agencies must bear that. It is a cost to government. It is the same sort of thing. If an agency sought a 1 400 per cent increase, that would be at the top of the sensitivity sheet that we would give to the expenditure review committee and the Government would have to think very strongly about that. A great deal of scrutiny is done of the levels and of particular fees and charges because of community sensitivity

Mr Doyle: A case like that probably would not get to government. If an agency were proposing a huge increase in any fee, before taking the matter any further, we would liaise with it to fully understand why it is seeking to do so.

The CHAIRMAN: That brings me to some technical terms that we would like you to define so that when we are reading literature and talking to various people we have a notion of what Treasury accepts. Firstly - cost padding?

Mr Doyle: Exaggerating the cost of producing a product, good or service.

The CHAIRMAN: Regulatory creep?

Mr Doyle: When regulators increase the range and scope of their regulation and begin to micro manage the bodies that they are meant to regulate; that is, to go into too much detail in setting regulations.

The CHAIRMAN: Cost shifting? I think we all know that.

Mr Doyle: In the context of joint responsibility services, such as state and commonwealth services, there is a reduction in service by one party in the expectation that the other party will be compelled to increase its level of activity in compensation.

The CHAIRMAN: We are pretty concerned about cross subsidising.

Mr Doyle: It means financing of an unprofitable part of a business or agency with a more profitable part.

The CHAIRMAN: In general terms, what is your attitude to cross subsidies, in the context of fees and charges?

Mr Duca: We do not support it. It is a grey area - when does a service or a good stop being a CSO and become a commercial product? Some agencies are more aligned to CSOs in their goods and services. Other agencies produce more, if you like, widgets, for the community to use as a commercial arrangement. We would not want one to subsidise the other.

Mr Doyle: That would generally mean that there was more than full cost recovery for a particular good or service, which is outside the Government's policy. Government does not set a policy to recover more than full cost on a good or service.

The CHAIRMAN: Can we say that cross subsidisation happens on occasions?

Mr Doyle: I imagine there are occasions.

The CHAIRMAN: Would it be true to say that in circumstances in which there are strong social and policy imperatives for there to be a level of service that would ordinarily be uneconomic, it is more likely to be acceptable from a Treasury perspective?

Mr Doyle: If it were within an agency or a portfolio and there was a relationship between the outputs that an agency might recover greater than its cost in order to benefit the other output, there would be some degree of acceptance. Generally it is a matter for government to set its policy.

The CHAIRMAN: Gold plating?

Mr Doyle: Gold plating means that an agency is providing an unnecessarily high standard of service. It is gold plated if it has features for which the additional cost is not proportionate to the benefits produced.

Mr T.K. WALDRON: What examples do you have?

Mr Doyle: I do not necessarily have a government example. It would be gold plating if someone bought a Rolls Royce rather than a Holden Commodore.

Hon ALAN CADBY: This committee examines cost recovery in local government. I understand you are here today to give us advice on this. It is very difficult for us to scrutinise cost recovery because we do not know the costs. We rely on information given to us. Can you give us any tips on questions we should ask when we are looking at cost recovery from local councils? We said earlier that some fees suddenly increased by 1 400 per cent, which seemed to be a helluva rise. What advice can you give us concerning cost recovery models and whether the fee rises are justifiable?

Mr Doyle: In describing the elements of a full cost of providing a good or service, we have spoken about direct and indirect costs. The direct costs of production include costs of employing staff directly involved in producing the service and direct material costs associated with a good or service and indirect costs such as corporate services overheads. Rental of an entire building, for example, may not be a direct cost of production but it is still a charge. Other costs include capital related costs such as depreciation of assets used in the production of goods or services.

[10.40 am]

Over the past two years the Government has introduced a capital user charge, which is effectively an opportunity cost of capital. If a person needs to make an investment in a particular service, then there is the opportunity to spend that money, or make that investment, in some other service, to repay a debt or to put it in the bank and earn interest. An opportunity cost of capital must also be taken into account. For State Government agencies that figure is set at eight per cent, which is equivalent to the capital user charge. If taxation is paid directly, it is generally not a goods and services tax because, as a rule, agencies get input credits for goods and services tax. However, if they have to pay taxation, such as local government rates or payroll tax, then that should be added. For some government agencies any service received free of charge, such as the audit performed by the Auditor General, would be an indirect cost if it were transacted. There are a number of components to working out the full cost.

Hon ALAN CADBY: Would you then agree that it is easy for us not to get the right information?

Mr Doyle: It could be. It is not as simple as it may seem in terms of the cost.

Mr P.B. WATSON: I will pick up on what Adrian said before about building in increasing fuel prices or wage rises. Do you have some fat in the system for that?

Mr Duca: Not really. We provide for a level of escalation in all agencies - I think it is about 2.25 per cent at the moment for the forthcoming budget year. Agencies would argue and I would agree that it is never enough. Government will never have enough to meet the demand. It is a question of priorities.

Mr P.B. WATSON: How do you organise that component of it?

Mr Duca: Our economic area annually works out the gross state product - GSP - implicit price deflator as part of the budget papers. We apply that to an agency's non-salaried expenditure generally. If an agency has a $100 budget for non-salaried expenditure and we apply the GSP implicit price deflator, it will get an extra $2.25 in next year's budget. It is supposed to use that money to meet all the increasing costs. Many agencies argue that it is not enough, and we would agree. However, it comes down to a question of how is that funded? The Commonwealth does not generally escalate its grants to us, and our revenue sources are not always going up at the same rates. The demands are always much greater than the revenue streams. It is a question of the Government providing some sort of escalation and it is also a question of priorities.

The CHAIRMAN: We are keen for any sort of cost recovery to be reasonably transparent. When people put in submissions to you about fees, is there any requirement to do some sort of fee impact statement or anything like that?

Mr Duca: As part of the justification the agency would argue over some details about the fee. If it is an ongoing fee we would already have that information on our files. If it is a straightforward request to keep up with the rate of inflation, it would be a fairly standard submission. However, when the agency commences to argue for a greater level of recovery than inflation, we would question the nature of the services being produced and the numbers. For example, if the agency is selling publications to the public, we would question the type of publication and how great its use is. Our analysis would cover that level of detail.

The CHAIRMAN: If agencies are astute enough to fly under the radar, they are probably not going to be subject to that much scrutiny. Would it be the case that the more outrageous they are, the more likely they are to attract your attention?

Mr Duca: Where the increase being sought in a particular year is greater than the normal consumer price index, then it is more likely that we will raise questions with the agency.

The CHAIRMAN: But is it true that even if it were at CPI or slightly below, that could certainly be more than cost recovery in that particular year?

Mr Duca: I would not say that -

Mr Doyle: There is a possibility that that could be the case.

The CHAIRMAN: Can you provide an example of a well-designed cost recovery arrangement?

Mr Duca: A well designed cost-recovery arrangement! Do you have any ideas Graeme?

Mr Doyle: One that follows our guidelines I suppose.

The CHAIRMAN: What about an independent person reviewing it or, in terms of transparency, the cost recovery details could be published in an annual report?

Mr Doyle: My understanding is that agencies are not required to publish -

The CHAIRMAN: No, we are not talking about what they have to do but whether it is a good thing to do for transparency reasons.

Mr Doyle: In their annual reports and their financial statements there are full details of the revenues they get from their fees and charges -

The CHAIRMAN: But that means people literally have to look up the inputs and outputs, fiddle around with them and work out how much income the agency gets, its expenditure and what is left over. It is not a very scientific or comprehensive picture that one gets in terms of cost recovery.

Mr Duca: Sure. In any additional information about the agency, if the expenditure can be linked to the revenue outlining the fees and charges that it will receive for the production of goods and services - that is, stating this is how much it will cost - that would be appropriate.

Hon LJILJANNA RAVLICH: What is provided in the financials? Is it just a percentage figure of the amount or the money value figure and the amount collected from cost recovery through fees and charges?

Mr Doyle: It is not classified as cost recovery. However, in the annual reports for all agencies they have on the face of their statements a line of user charges and fees. The notes will go into the detail as to exactly what components make up those user charges and fees. Someone should be able to see, for example, how much is recovered from school fees and all the individual components of those fees. There is also some detail in the budget papers for the agencies that are divisions of the consolidated fund estimates. They are also required to publish details of their revenues.

Hon LJILJANNA RAVLICH: So fees and charges equal cost recovery in terms of budgetary or financial statements?

Mr Doyle: Yes, some are cost recovery and some are just fees, such as school fees that are not based on a cost recovery basis -

Hon LJILJANNA RAVLICH: So it is not a true indication of what component is cost recovery as opposed to what would traditionally be called a fee. In a sense there is some scope for improving the transparency, which is what Madam Chair alluded to in relation to what component is actually full cost recovery or part cost recovery. It would seem to me that at the moment there is a problem with the definition.

Mr Doyle: There is no disclosure of cost recovery.

Hon LJILJANNA RAVLICH: Okay. It would certainly be helpful from the point of view of the public and the Government if that distinction could be made. In effect, that might lead government to shift policy - if you like - in a range of areas in relation to greater collection of revenues or whatever. Well, that may not be necessarily so, but at least government would have a clearer idea of what was before it prior to it making those sorts of decisions.

Mr Duca: Something like that would certainly assist.

Hon ALAN CADBY: I want to follow the point raised by Madam Chair. If the increases were below CPI and not tagged by you, does that not perpetuate inefficiency?

Mr Duca: If the increases were below CPI, we would have to -

Hon ALAN CADBY: If you accepted them in terms of CPI, then is that not likely to perpetuate inefficiencies within the agency?

Mr Duca: That would be the case if that review of fees and charges was done in isolation and we did not do anything else with the agency. However, as part of our expenditure examination we would examine their expenditure profiles. If there were inefficiencies, they would surface in the comparisons we may make. If in one year the agency's costs suddenly rose, we would question that. If its costs in a particular year were seen to be out of kilter with that type of industry or agency, we would also question that. If we just looked at the fees and charges and said, "Under CPI we will give it a tick", but if we actually looked at the expenditure profile of the agency or its output costs -

Hon ALAN CADBY: But you said earlier that you could not compare one agency with another. If an agency has always been inefficient and the fee increase is acceptable to you, then that is likely to perpetuate the inefficiency of that department.

Mr Duca: We are continuing to work with departments. It is hard to identify inefficiencies sometimes because of the very nature of the agency that may have always been like that. Again, there are elements of interjurisdictional comparisons that allow us to pick up trends. It might be a direct link to say, “You are inefficient by exactly 17.2 per cent.” However, trends can be picked up over time. We have worked with a number of agencies to improve the way in which they allocate their resources and spend their dollars. I suppose the answer to your question is yes, but a lot of work has gone into that area and will continue to do so to make sure that those inefficiencies surface.

Mr Doyle: Every agency goes through the rigours of budget review every year; that is, facing the expenditure review committee and having bilateral meetings to determine its budget allocation for the year. Examining the efficiency and effectiveness of an agency happens as a matter of course. The areas of inefficiency that you are suggesting will - at the least - usually be found out over time, although, perhaps not in one year. Perhaps the agency might get away with some inefficiencies for one or two years but over time the inefficiencies will generally be eliminated because of the ongoing scrutiny that happens as part of the entire budget process. The review of fees and charges is just one part of that process.

The CHAIRMAN: What is your definition of a “tax” as opposed to a “fee”?

Mr Doyle: Tax is not necessarily related to a discrete service. It is an amount set by government to generate revenue to fund the operations of government in a broad sense. A fee relates to a particular good or service. That is the primary difference. One does not directly benefit from paying a tax, but if a fee is paid for a birth certificate or a drivers licence, for example, then one gets a drivers licence or a birth certificate. That is the primary difference.

The CHAIRMAN: When you examine an impost, what pointers do you particularly look for to see whether it is a tax or a fee?

Mr Duca: When I am looking at fees and charges I look for what has been produced. If I were the consumer buying this good or service I would ask myself the basic question: “Am I getting value for money for this good or service?” If a fishing licence cost $1 754, one might think that that was a bit high. The basic analysis is to look at the fees and what they are for.

In the early 1990s when a greater emphasis was placed on this part of the budget process, we found that some fees from 1920 and 1925 had not changed, such as medical students’ fees and doctors’ licence fees. There had not been much emphasis on that side of the equation. The expenditure was the side of the equation that people always looked at. Over the years this has been refined to the point where one could say that a fee or a charge has been levied for the production of a particular good or service. I consider whether the charge is reasonable. If we are dealing with publications we might look up an annual report of Alcoa or a private company and say, “If they produce publications, how much does it cost them?” I might then look up the Department of Mineral and Petroleum Resources to see what its cost of production for a publication is. That is the sort of analysis that might be done in our reviews, certainly with those agencies that are very heavy on the fees and charges side.

The CHAIRMAN: We are a committee of scrutiny and it is not really our role to delve into these things in any great detail. However, part of our problem is the level at which the figures are presented to us that may determine our capacity to say whether it is a fee or a charge. For example, a local government recently said that a particular service was part of the whole building department’s budget. It was clear from what the particular service was getting that it required minimal work, minimal time and minimal capital outlay for the local government. Yet, it was producing figures to us for its whole building department. Obviously, we were not in a position to assess that. There were obviously external costs such as salaries, superannuation and all the rest that had gone into it. Even so, we were asked to compare apples with pears, if you like.

Mr Duca: There must be reasonableness in the apportionment of overheads in corporate services. What we found when agencies first started to do this earlier on was that they were not apportioning enough. They were just taking into consideration the direct costs. We would then say, "Well, do you not have to pay rent?" It must be reasonable. In the case you just described, it seems like they have gone over the top and tried to put everything in there to justify a rather larger claim. Again, it gets down to reasonableness. Is it reasonable to charge X dollars for that service, that publication, that workshop, that training seminar or whatever the agency is doing? A consumer should say, "Would I be willing to pay for that?" That is how we judge if it is reasonable or not.

The CHAIRMAN: Earlier you also talked about how you quite often compare like agencies. For example, if one local government charged X dollars and the other one charged four times that amount, would it be legitimate to ask, "How is it that this council can do it for a quarter of the price?"

Mr Duca: It may be found that one council is a lot larger and is billing in more overheads but producing the same service or good. It is reasonable to question that and say, "You should not be billing in a lot of the overheads that the larger council is or there should be a cheaper way of producing that good."

The CHAIRMAN: We referred to the report produced by the Commonwealth's Productivity Commission in August 2001. It noted that more than $3 billion had been raised in cost recovery in 1999-2000 and that cost recovery revenue grew by 24 per cent in real terms over the past five years. Are there any estimates on how much has been raised in Western Australia and is such information being routinely recorded?

Mr Doyle: As we mentioned earlier, in terms of classifying it as cost recovery, no. However, in terms of reporting revenues from user charges and fees or regulatory fees and licences, that information is routinely reported in the annual reports of agencies and in the budget papers at an agency level - if they are a division of the consolidated funds estimates - and at the whole of government level. In the case of the latter there are sectoral splits for the general government sector agencies - the public corporation-type agencies such as Western Power and the Water Corporation - and for the total public sector agencies. Details are reported in the budget papers for these types of revenues but they are not classified as cost recovery as such. I have a couple of figures here for the general government sector and the revenue from user charges fees and regulatory fees, such as licences. In the 2002-03 budget, the estimate was $919.3 million.

[11.00 am]

In 2000-01 for the same types of charges and fees it was $863.3 million and in 2001-02 it was $881.7 million. There is a trend upwards over those three years for the general government sector.

The CHAIRMAN: Has any independent or internal research been done for Western Australia similar to that done by the Productivity Commission?

Mr Doyle: No.

The CHAIRMAN: You have been very discreet and tactful and have said that there are no serial offenders in terms of complying with these guidelines. Do any departments stand out as being very good at complying with the guidelines or producing good information about cost recovery?

Mr Duca: The Department of Land Administration.

The CHAIRMAN: What does it do that makes you think it is so good?

Mr Doyle: It has a lot of tangible type goods that it produces and then makes available to the community, such as maps and title searches. You can actually get a grip on that stuff and work out a little easier than we can with policy advice, for instance, how much it actually costs to produce these things. When you have something more tangible to provide to the community, it is easier to cost the good or service that you are providing.

The CHAIRMAN: It has probably been in the business of cost recovery or charging for longer than a lot of other government agencies.

Mr Doyle: Yes, it has.

The CHAIRMAN: That brings me to another point. In some situations the users of a particular service are charged a fee but in fact it is cost recovery for the benefit of the community as a whole. What is the policy view on that? I suppose the obvious example is the Department of Fisheries. Fisheries charges are partly to protect the fish resource as a whole. The community in general benefits from that, in that the common property resources are not depleted, yet only some users are paying for that.

Mr Doyle: That links back to environmental responsibility. As I mentioned earlier, there is an environmental responsibility to protect our fish habitats. That is why there are regulations and restrictions on the fishing industry. The fees that are set by the Department of Fisheries for the commercial side of things are very much full cost recovery for the effort that the department puts into commercial fishing activities. However, the recreational fishing activities are not based on full cost recovery. Therefore, the fees that the department generates from recreational fishing licences only partly contribute towards the total cost of the services provided by the Department of Fisheries.

The CHAIRMAN: That is a broader political or policy constraint that has been put on the extent of full cost recovery. Are there any other legal or administrative restraints that you can think of for full cost recovery?

Mr Doyle: A fee or a charge cannot be applied unless there is legislative power to do so. Two examples are the governing legislation of statutory authorities, and the Fish Resources Management Act, which governs the operations of the Department of Fisheries. If there is not actual legislation that allows the setting and charging of fees, it cannot be done. Also, under the State Trading Concerns Act, an agency may apply to establish a charge for a particular good or service that it produces in accordance with section 4A if it is a department or section 4B if it is a statutory corporation. If there is no existing power to set a charge, then an agency may apply through that mechanism to do so.

The CHAIRMAN: Is the capacity of Treasury to oversee proposals for fees or charges somewhat limited by resources? How many people in Treasury are looking at this sort of stuff?

Mr Doyle: The Department of Treasury and Finance has about 40 people in the agency resources division who liaise with the agencies on these sorts of matters.

The CHAIRMAN: It is not just on fee recovery; it is presumably on their full financial management?

Mr Doyle: Yes.

The CHAIRMAN: Without getting to the cost recovery principles, how much of their time would that take?

Mr Duca: Perhaps five per cent of their time.

The CHAIRMAN: Is there a feeling in your department of “we will do it if we have enough time”, or do you think you have enough resources to have adequate oversight of all these examples?

Mr Duca: The fees, taxes, charges and tariffs process is a very dedicated part of the budget process. There is a process that has been in place for a number of years and there is a dedicated resource for that in the three months of the year leading up to the budget. Given that we have an \$11 billion or \$12 billion expenditure budget and this may be less than 10 per cent, we have to weigh up the priorities. However, the fees and charges part of the budget process is a dedicated process and it is given separate consideration by the expenditure review committee. It is an important and integral part of the budget process. Obviously the focus is on the other side of the equation - the expenditure demands of ministers and agencies. From our point of view at Treasury and Finance, we put the effort in with agencies when we get their submissions and we test them.

The CHAIRMAN: There was a case earlier this year related to the registration of business names, and the regulations were ultimately disallowed. The department was, if anything, a little too frank in talking about what its cost recovery was, and it was way short of what it was proposing to charge. I am a little concerned about how that got as far as this committee without those questions being asked.

Mr Duca: I have no idea, but the agency would have been tested on the cost recovery aspect of what it was trying to raise. I am not aware of that particular case. Certainly when the submissions come forward we ask the typical questions, such as: how much are you seeking to cost recover, is it in excess of the consumer price index, and what is it for? The usual analysis is done.

The CHAIRMAN: Is there some sort of standard form with things that they have to fill in - a check list or something - that could obviate these kinds of cases? It is expensive and unproductive. It meant in the case of that agency that it had about $4 million less to play with that year, all because the regulations were disallowed. What we are keen to do, frankly, is not have to look at this too often. We would like to be assured that somehow the process is fairly airtight.

Mr Duca: The agencies usually get a standard form to fill out as part of the review of fees and charges, identifying the type of fee, the existing rate, whether the increase is at CPI or above CPI, whether it is a new fee or charge, etc.

The CHAIRMAN: Would you undertake to supply to the committee a copy of that form?

Duca: Yes , certainly.

Hon RAY HALLIGAN: I would like to go back to the benchmarks, because that concerns me as well as other members. Are any checks made of those benchmarks? I know it will take some considerable time, but if you start off with the wrong figure, as Alan has said, and perpetuate it, you may accept it as being the right cost when in fact it is not. This is where the gold plating can come in as well. We had that situation with a local government agency that set up a number of committees and caused an application to go through those committees, hence an increase in costs, but it could not justify to us why an application had to go through all those committees in the manner it had set up. You mentioned that you compare current costs with previous costs - that is understandable - and that you also compare the costs with the costs of private enterprise in some instances if you can. The introduction to your document “Costing and Pricing Government Outputs” states -

> These Guidelines are intended to be of assistance to a wide range of users. They should be regarded as an **illustrative** guide to the factors which may be taken into account when carrying out a costing exercise as there is no costing methodology which can be applied universally.

What about the accounting standards? Secondly, if this is what is being handed out to people, how can you place yourself in a position to believe that they have gone down a particular route and have not formed their own methodology?

Mr Duca: These guidelines are guidelines. It is very difficult, given the wide range of government agencies, to apply a one-size-fits-all model.

Hon RAY HALLIGAN: The accounting standards do exactly that, do they not?

Mr Duca: They certainly do, but agencies do not always find them detailed enough or helpful enough. That is why these guidelines are produced. The accounting standards are very important from a financial management point of view. However, when we are talking about actual costing of their expenses, it is very difficult to refer to some of the accounting standards in that level of detail. Therefore, the guidelines have been produced and revised over the years to try to keep them contemporary with the current needs of the agencies.

Mr Doyle: That comment generally relates to the unique nature of the different goods and services. The accounting standards are certainly applied uniformly in terms of reporting revenues, expenses, assets and liabilities. That is universally applied.

In terms of calculating what it costs to produce a particular good or service, because each good or service has its own unique features or nature, you cannot have an exact one size fits all. That is why the guidelines go into the broad concepts of identifying all the direct costs about a particular service, and then the indirect costs, the capital-related costs and so forth. One particular good or service may not need any physical infrastructure assets to enable its production but another may need significant infrastructure assets to enable its production.

Hon RAY HALLIGAN: I am sorry, but you have not convinced me. I understand the uniqueness of different goods or services. However, the application of the accounting standards should be the same. The direct costs are easily identifiable. If you want to apply an overhead to that, that is something you can do, but you know what those costs are. It should be relatively simple. You have gone down a particular path. Do you have any examples of how this uniqueness may provide for completely different accounting standards to determine the cost of a good or service, as you are suggesting?

Mr Doyle: No examples come to mind readily. In terms of the accounting standards, expenses or costs are generally recorded by the nature of the expense, such as salaries, supplies, maintenance, grants and subsidies. The nature of the expense is recorded routinely and uniformly and is reported as such. However, different goods and services may require different amounts of each type of expense. They may need a different number of people to enable their production and so forth. That is where the inconsistency lies.

Hon RAY HALLIGAN: That is true, but I suggest the accounting standard remains exactly the same.

Mr Doyle: Yes, it does.

Hon RAY HALLIGAN: Do you provide any training to the staff of agencies during the financial year to enable them to determine the costs in accordance with these guidelines?

Mr Doyle: We do not take direct responsibility for the training of staff in agencies. However, we provide forums at least a couple of times a year on various financial management issues that are topical at different times. We also make it known to agencies that we are available to assist on issues like this if they require our assistance. Therefore, although we do not take direct responsibility for their skills, if you like - that is a matter for each particular agency - we play an advisory role on request. There are a number of agencies out there, and we cannot keep knocking on their doors and asking whether they need help. If we come across agencies that appear regularly to not be doing the right thing on these sorts of issues we will proactively go and see them, but in the absence of that we are there to give them advice if they need us.

Hon RAY HALLIGAN: Do you expect the Auditor General to check any of this on your behalf?

Mr Doyle: We also work closely with the Office of the Auditor General on these issues, and any management letters that agencies get and certainly any audit qualifications that he issues we will make ourselves aware of, and if we see a need we will liaise or consult with the agency on ways to deal with those concerns.

Hon RAY HALLIGAN: With regard to making sure that full cost recovery, or any cost recovery, does not go beyond full cost recovery, do you expect the Auditor General to assist the office in the work that it does on an annual basis?

Mr Doyle: Not routinely, but it is within his power should he choose to do so.

Mr Duca: If one of the reviews showed the potential for greater cost recovery or over cost recovery, we would certainly take notice and review those reports from the Office of the Auditor General.

Hon RAY HALLIGAN: So you are suggesting it would be of assistance to you?

Mr Doyle: Yes.

Hon RAY HALLIGAN: It certainly would be of assistance to us in a number of areas. Has Treasury ever put to the Office of the Auditor General that that might be part of his function?

Mr Duca: Not that I am aware of.

Mr Doyle: Not to my knowledge.

Hon RAY HALLIGAN: You are not contemplating that at the moment?

Mr Duca: No.

Hon RAY HALLIGAN: You have said - and rightly so - that the legislation has to allow for fees and charges to be applied. If there is not a great deal of detail in the legislation, does the agency itself determine what fees and charges are applied or does Treasury encourage the agency to look for certain aspects of its goods or services for which it can charge a fee?

Mr Doyle: If agencies are increasing a fee or charge or want to set a new fee or charge, we are generally reliant on getting information from the agencies that that is consistent with their governing legislation. If they do not have governing legislation - if it is a standard department - then they have to make application in accordance with the State Trading Concerns Act.

[11.20 am]

Generally we rely on information from the agencies, but if they put something to us about which we have questions or concerns, we would ask them to seek advice from the Crown Solicitor to confirm that it is lawful for them to initiate such a fee or a charge:

Mr Duca: That is it. In recent times we have become aware of occasions on which there is a capacity to do some cost recovery. Some agencies, for example, have been producing very costly reports for free for the public or other institutions. We have suggested that it is appropriate to charge something for such a service. It may not be full cost recovery in the early stages, but it will be over time. If it is not free, the agencies must think about whether they need to do it. That has happened over time. We make suggestions to the agencies, the agencies think it is appropriate and then they go down that track. We rely on the agencies, but we do oversee what we consider are appropriate charging regimes.

Hon RAY HALLIGAN: When you referred to agencies deciding on new fees, were you suggesting that the legislation allows for these fees? Do the agencies have to go through a process to send it through Treasury?

Mr Duca: Yes. As part of the annual review of fees and charges in deciding whether to raise a fee, there is a separate part of the program which we rely on for existing fees and charges, and which indicates that the increases relating to new fees are this much and the new fees and charges will be this much. It is a formal process through the expenditure review committee process, and ultimately it goes to Cabinet.

The CHAIRMAN: In the context of that review, have you ever recommended that a particular fee decrease?

Mr Duca: I cannot recall one in recent times.

Hon RAY HALLIGAN: In that regard, if a figure looks reasonable to you, it then becomes the benchmark, does it not? Do you do any checks on it other than just a cursory look at it?

Mr Duca: We do some testing to see whether it looks reasonable for the good or service that is being produced. However, we do not do an exhaustive amount of work.

Mr Doyle: It depends on the materiality of the total amount of revenue that it might raise as well. The higher the total amount of revenue, the more scrutiny the fee will receive.

Hon RAY HALLIGAN: Are some agencies required to meet full cost recovery targets?

Mr Doyle: No explicit target is set for agencies in general. Obviously, some of the statutory corporations - such as the Water Corporation and Western Power - which are all self-funding have to generate revenue from their operations to meet the total cost of their service. However, other than that generality for those types of organisations, to my knowledge there is no explicit statement that an agency will recover its full cost.

Mr Duca: I agree with that.

The CHAIRMAN: Thank you very much gentlemen. You have been of great assistance. Is there anything else that you would like to say before we conclude today?

Mr Duca: No. Thank you very much for listening to us.

The CHAIRMAN: Thank you for your help.

Committee adjourned at 11.23 am.