

Rural Industries Research and Development Corporation Amendment Regulations 2002 (No. 1) 2002 No. 309

EXPLANATORY STATEMENT

STATUTORY RULES 2002 No. 309

Issued by the Authority of the Parliamentary Secretary to the Minister for Agriculture, Fisheries and Forestry

Primary Industries (Excise) Levies Act 1999

Primary Industries Levies and Charges Collection Act 1991

Primary Industries and Energy Research and Development Act 1989

Primary Industries (Excise) Levies Amendment Regulations 2002 (No. 11)

Primary Industries Levies and Charges Collection Amendment Regulations 2002 (No. 8)

Rural Industries Research and Development Corporation Amendment Regulations 2002 (No. 1)

Section 8 of the *Primary Industries (Excise) Levies Act 1999* (the Excise Levies Act) provides that the Governor-General may make regulations prescribing matters required or permitted by those Acts to be prescribed or necessary or convenient to be prescribed for carrying out or giving effect to that Act.

Section 30 of the *Primary Industries Levies and Charges Collection Act 1991* (the Collection Act) provides that the Governor-General may make regulations prescribing matters required or permitted by that Act to be prescribed or necessary or convenient to be prescribed for carrying out or giving effect to that Act.

The purpose of the regulations is to implement a levy scheme to fund egg promotion activities by the new egg industry service company called the Australian Egg Corporation Limited (AECL).

AECL will be responsible for providing generic promotion and research and development services to the industry and is to be declared as the relevant industry service provider company under the provisions of the *Egg Industry Service Provision Act 2002* and the *Egg Industry Service Provision (Transitional and Consequential Provisions) Act 2002*.

The egg promotion levy will be imposed on eggs that are produced in Australia and sold or used by the producer in the production of other goods. The levy will be payable by the egg producer.

The levy reflects agreement between the Government and the peak industry body, the Australian Egg Industry Association (AEIA) and forms part of a broader industry led initiative to establish a Corporations Act company, as the egg industry service provider.

In meeting the Commonwealth Levy Principles, the AEIA has demonstrated significant majority industry support for the proposed new promotion levy.

The egg promotion levy is designed to provide support for the industry to ensure its long-term viability and sustainability. This support consists of promotional activities that aim to increase the

level of egg consumption and improve the communication links between consumers, government and within the industry itself. The current R&D levy will be redirected from the Rural Industries Research and Development Corporation (RIRDC) to AECL.

Sub clause 2 of Schedule 27 of the Excise Levies Act provides that regulations may impose a levy.

The Regulations:

- provide for a statutory levy on eggs that are produced in Australia and are sold or used by the producer in the production of other goods. The levy is payable by the egg producer;
- prescribe that the number of laying chickens bred or purchased for use in the commercial production of eggs is a measure of the presumed production of eggs in Australia.
- provide for the levy to be collected upon each laying chicken bred by a producer, or purchased by a producer for use in the commercial production of eggs.
- set an initial operative levy rate of 32.5 cents for each laying chicken bred by a producer, or purchased by a producer, for use in the commercial production of eggs;
- provide for the manner of payment of levy, the provision of returns by persons who must lodge returns and the keeping of records.

The Regulations commence on 1 February 2003. This date has been agreed to by the egg industry. AECL will be operational by this date and have the systems in place to manage the levy funds.

A Regulation Impact Statement is attached.

Attachment

REGULATION IMPACT STATEMENT

Background

The egg industry is currently serviced at a national levy by the peak industry body, the Australian Egg Industry Association (AEIA) and an egg sub-program under the Rural Industries Research and Development Corporation.

At present, a levy of 7.87 cents per laying chicken placement in the industry is imposed under the *Primary Industries Excise Levies Act 1999* where more than 1000 laying chickens are hatched in one year. The overall industry levy is split to accommodate research and development, residues testing and animal health issues, as follows:

- 7.2 cents per laying chicken is directed to RIRDC for research and development,
- 0.4 cents per laying chicken is directed to the NRS, and
- 0.27 cents per laying chicken is directed to the AAHC.

The 7.87 cent levy is imposed on, and collected by, the hatchery owner, with some or all of the costs passed on to the egg producer when they purchase laying chicks.

Nature and Extent of the Problem

The egg industry has experienced a difficult period since deregulation of marketing arrangements in the late 1980s. Further pressures in recent years have resulted from the Newcastle Disease outbreaks and changes to layer hen housing to meet animal welfare requirements. In particular, egg producers have suffered from an inability to adopt a whole-of-industry approach on crucial issues, to communicate the health benefits of egg consumption to consumers and to benefit substantially from industry R&D, market promotion and other service provision.

Over the last decade, eggs as a food source have suffered from negative consumer perceptions regarding dietary issues and animal welfare. Nutritional research is increasingly showing the benefits of eggs, but there has been no avenue through which to promote this information effectively to consumers. Whilst the industry has been fighting to retain the place of eggs as a preferred food category in the face of dramatically changing consumption and lifestyle preferences, declining consumption has forced some producers to leave the industry, and those remaining to question their viability.

Between 1989 and 1999, Australia's average annual egg consumption decreased from 146 to 137 eggs per person (source ABS), well below the industry's target of 200. The AEIA has argued strongly that this decline is a result of a market failure in egg promotion. Whilst there are some producers large enough to carry out marketing and create brand recognition, this has not proved enough to redress the declining per capita egg consumption. In addition, the structure of the industry and the nature of the product mean that the marketing efforts of individual firms benefits other egg marketers, without the latter's contribution to the cost. This "free-riding" problem results in a commercial disadvantage to the investing firm, and as a result, generic promotion is hindered.

Over the past fifteen years the Australian egg industry has made several attempts to address the need for generic promotion through voluntary levies. However, the levies have ultimately failed. The industry believes that demand for eggs can be generated through promotional activities, but that being generic in nature, the cost should be shared by all.

In early 2001, the Australian Egg Industry Association (AEIA) presented the Commonwealth Government with a proposal for a new Corporations Act company to undertake generic promotion, the research and development services currently provided by the Rural Industries Research and Development Corporation (RIRDC) and some strategic industry service provision. The proposal also involved a new statutory promotional levy of 32.5 cents on each laying chick purchased from a hatchery.

Objectives of the Regulation

To assist the egg industry to become more sustainable, competitive and profitable through generic promotion and to develop a structure to effectively and efficiently manage that promotion as well as industry R&D and service provision.

Options

There are three possible courses of action for the egg industry.

- i) Continue without generic promotion for eggs. This option would mean that the industry would continue with some individual brand promotion by larger producers, but no generic promotion in terms of public health, food safety, nutrition and dietary benefits
- ii) Develop a system for collecting voluntary contributions towards generic promotion. The contributions would be collected independently from Government, and the industry would be entirely responsible for developing and administering a system for collecting monies.
- iii) Establish a compulsory promotional levy through regulation. This is the option that the egg industry have chosen to pursue and involves a promotional levy of 32.5 cents, to be imposed on producers per laying chick purchased from a hatchery. The AEIA selected the rate of 32.5 cents per laying chick as a balance between affordability for producers and the estimated operational budget for an effective promotional campaign. The levy would be collected by the hatchery at the time of purchase, and remitted to Commonwealth on a monthly basis. Under the proposal, AFFA would disburse the monies generated to the new industry company, Australian Egg Corporation Limited.

The AEIA have proposed that the new 32.5 cent promotional levy would be additional to the existing industry 7.87 cent levy. As all egg producers purchase laying chicks from a hatchery, the AEIA believe that the proposed imposition mechanism is an effective way to collect a promotional levy from all producers.

Assessment of Impacts

- i) Continue to operate without generic promotion

Costs: The egg industry comprises a range of producers, from the small rural and regional operations with little market power, to the larger organisations which have greater market power and the potential to promote a distinctive brand. Whilst the larger producers have the opportunity to develop recognition for their brand, the atomistic nature of the industry means that it is not in their commercial interests to promote the egg generically. Between 1989 and

1999, Australia's average annual egg consumption decreased from 146 to 137 eggs per person (source ABS), well below consumption in other Western nations with similar diets and the industry's target of 200. The ASIA has argued strongly that this decline is a result of a market failure in egg promotion. According to the AEIA, the industry faces a continuing decline in per capita egg consumption if generic promotion is not undertaken. In addition, the nature of the marketing system, which is dominated by the supermarkets, means that generic promotion is the most appropriate method of communicating to consumers.

Without generic promotion, the industry has almost no way to communicate the result of research and development, particularly in relation to the dietary and health benefits of egg consumption. The result is likely to be a continued decline or stagnation in consumption, reducing profit margins for the industry, declining number of producers and inadequate investment in new infrastructure and technologies. In addition, product quality and food safety may also suffer. As egg production tends to be concentrated in regional clusters, this would have a flow on effect to the communities surrounding those clusters, as well as to Government, who would be required deal with adjustment issues, and to the general public, who wish to see welfare and disease issues addressed through investment in infrastructure and technology.

Benefits: Without generic promotion, individual producers will not be required to make individual contributions towards funding the program. This would be particularly attractive for some marginal producers who are already struggling to retain viability, and who may suffer negatively as a result of voluntary or statutory contributions towards promotion.

ii) Implement a voluntary promotional levy

Costs: The industry has in the past attempted to fulfil the need for generic promotion via a voluntary levy. For example, the now defunct Incredible Egg Company, established by the AEIA in 1987 to promote egg consumption and the egg industry nationally, initially enjoyed the support of the organisations that supplied around 70% of the Australian market. However, that support fell away and the company failed due, to a large extent, by resentment at the large number of "free riders" benefiting at the expense of those producers who paid their contributions. In addition, the administrative costs of managing the collection of the voluntary levy and chasing defaulters proved to be a disproportionate burden for the Incredible Egg Company. These problems are likely to apply to any new voluntary levy that the industry was to implement.

In addition, the uncertainties associated with voluntary levies would make it difficult to design a promotional strategy with long-term goals. This is particularly the case given the industry's history with voluntary levies. For any promotional program to be effective, there must be enough financial security to make the decisions that generate the greatest benefit for the industry in the longterm.

Benefits: With a voluntary scheme, producers would more easily be able to demonstrate their satisfaction or dissatisfaction with the promotional program. In addition, they would have more flexibility to make contributions in accordance with their financial state at the time.

iii) Establish a statutory promotional levy

Costs: The levy will be charged to egg producers at a rate of 32.5 cents per laying chicken purchased from a hatchery for the purposes of future egg production. In terms of impact, 32.5 cents is equivalent to 5% of the current average cost of a pullet, or 1.7 cents per dozen eggs sold. The levy will increase egg production costs as a proportion of GVP by about 1%. In the first year, the levy is expected to generate approximately \$3.1 million dollars, with the industry's current GVP at just over \$300 million.

Although the levy will be imposed on, and paid by, producers, the hatchery operators will be responsible for collecting the levy and remitting it to the Commonwealth. This is likely to involve a separate remittance from that used for the existing industry levy, and therefore some additional cost to the hatchery operators. However, the ASIA wrote to each of the sixteen hatcheries that pay the current levy, outlining the detail of the proposal and their role in collecting the new levy. A survey was included in the letter. The AEIA received 10 responses, 9 of which supported the proposal. Despite some extra cost in collecting the levy, benefits generated through generic promotion will flow through to the hatcheries in terms of additional chicks purchased.

The latest Australian Bureau of Statistics (ABS) figures (for the year ending 30 June 2000) indicate that there are just over 500 egg-producing establishments in Australia. The AEIA argue that only 340 are commercial producers (those with a minimum of 1000 laying hens). Although the remaining producers may not be commercial, they will be required to pay the new promotional levy when they purchase laying chicks from the hatchery.

Benefits: Disbursement of the existing R&D and new promotional levy to a single industry corporation will allow a unified; efficient, informed and sciencebased approach to R&D and promotion, benefiting industry and consumers.

The proposal put forward by the AEIA spreads the costs of generic promotion across the industry according to the size of each operation and in an equitable manner. As the promotional levy is paid on the laying chick at the time of purchase, operators with a larger number of laying chickens will pay a larger levy than the smaller operators. In terms of those involved in niche products, they too have supported the levy, as any increase in egg consumption will ultimately feed through into their products as well. In addition, all payers of the promotional levy will be eligible to register for membership of Australian Egg Corporation Limited, and will be able to vote on issues such as the rate of the levy.

The difference between the existing levy and the new levy is that the promotional levy will be imposed directly on the egg producer (at the point of purchase of laying chicks) where the laying chicken levy is imposed on the hatchery operator (on chicks hatched). However, in both cases the hatchery operator is responsible for collection of the levy and remittance to AFFA. Using this mechanism to collect what is essentially a producer levy limits the number of collection points (at present 21) and hence the costs to the industry. In addition, because all producers purchase laying chicks from the hatchery, use of this mechanism is an effective way to impose the costs of the levy directly on those who stand to receive the greatest benefit from generic promotion.

As a result of the policy of cost recovery, there should be no net cost to the Government in terms of collecting and processing the levy. The promotional levy will not be matched by Commonwealth funding, however the R&D levy will continue to be matched up to 0.5% of GDP.

In New Zealand, the egg industry has been turned around by generic promotion. They funded their promotional campaign through a statutory levy set at a similar rate to that proposed by the AEIA, and have used their limited funds for strategic promotional activities. Since the commencement of the promotional program five years ago, per capita consumption in New Zealand has increased by approximately 12 eggs per year, to an average of 208 eggs. Statutory levies have also been used in Canada and the United States to fund promotional programs with positive outcomes.

Competition Policy

The levy will be applied equitably to all egg producers, with generic promotion designed to benefit the entire industry rather than individual producers. As a result, the proposed levy will

have no impact on competition within the industry. However, it is anticipated that the levy will allow the industry to compete more effectively with other fresh food production industries.

Consultation

In order to satisfy the Commonwealth's Levy Principles, the ASIA embarked on an Australia-wide consultation during the period from April to June 2001. This was later extended to 30 September 2001 in order to ensure that all stakeholders were aware of the proposal and had the opportunity to provide comment. The consultation was primarily directed at producers, but also others involved in the wider egg industry, including hatcheries and egg marketing companies. The AEIA circulated a letter on the proposal to all known producers, included articles in their industry newsletter, "The Eggsaminer", and conducted media interviews on the proposal and the levy. In addition, regional meetings were held in each state for producers and other industry stakeholders.

During the regional meetings, and through the period until 30 September 2001, producers were asked to vote on the proposal. Each egg producing business was allocated one vote, and 238 votes were collected in total. The AEIA claim that these producers represented over 96% of the ownership of laying hens in Australia. From these producers, 93.7% supported the establishment of a privatised company and 87% supported the levy being set at 32.5 cent per laying chick purchased from the hatchery for egg production. In terms of flock ownership, 92.7% supported the levy at 32.5 cents.

In terms of the proportion of industry included in the vote, the latest data from the Australian Bureau of Statistics (for the year to 30 June 2000) indicate that there are 508 egg-producing establishments in Australia. Of these, the ASIA argue that only 340 are commercial producers (those with a minimum of 1000 laying hens), which would mean that 70% of commercial producers have voted on the proposal. As mentioned above, the AEIA estimate that they represent 96% of the Australian flock.

In addition, the AEIA have consulted with hatchery owners on the proposal, and they are in support. Whilst the hatchery owners will not pay the new levy, they will be responsible for collecting levies from the producers and remitting the monies to the Commonwealth.

Opposition to the proposed levy

Opposition to the levy has been limited, and there has been no campaign of letters to the Government or the AEIA opposing the levy. Of those who did vote against the proposal or the levy, the AEIA have listed the following reasons:

- philosophical dislike of generic ideas stemming from a post-regulation environment;
- some larger producers indicated that they were already conducting local marketing and do not see the need to contribute to generic promotion; and
- lack of understanding of the proposal and industry issues.

Conclusion and recommendations

Over the past year the AEIA has been working to ensure that the Commonwealth Levy Principles are fulfilled and the proposal is viable. Through the AEIA's consultation process, both producers and hatchery operators have demonstrated significant support for the new company and the proposed nature and size of the promotional levy.

On the basis of consultation and analysis, the proposal for a statutory levy for egg promotion conforms to the Government's levy guidelines and principles, does not restrict competition and has clear potential to benefit the industry and consumers. It is therefore recommended for implementation.

Implementation

Legislation enabling the establishment of the new company has passed through Parliament and the new company - Australian Egg Corporation Limited (AECL) has been registered with the Australian Securities and Investments Commission. The regulations have been drafted and provide for the new levy to commence on 1 February 2003. All producers who pay the statutory levy will be able to vote on changes to the levy through their membership of AECL.