

FUTURE FUNDING OF UK MEAT CONTROLS**EXECUTIVE SUMMARY**

- 1. The primary responsibility of the Food Standards Agency and a core principle since its inception is to provide the best possible protection for UK consumers from risks which may arise from food. This protection should not be based on changed economic circumstances or the ability of an industry to pay.**
- 2. It is clear that providing a subsidy to businesses is inconsistent with the role of a regulator. It is not a function of the FSA to subsidise industry and if a continuing subsidy is to be provided it should come from elsewhere. The FSA has no remit within its constitution to subsidise private businesses.**
3. Earlier this year the Board agreed that the FSA should seek a 4% increase in the charges the MHS and DARD make to the meat industry for the controls provided in 2009/10. This was in line with the Board's objective agreed in July 2007, to reduce the burden of meat industry inspection on taxpayers, while recognising that at this stage full cost recovery was not practical. In April 2009 the Board agreed to change the timescale to 2014/15 for reducing the MHS subsidy for the industry in GB to £10 million.
4. The FSA was unable to secure UK ministerial agreement to the proposed 4% increase in charges, although Ministers did agree to move from the Maclean charging mechanism (lower of throughput or time-based charging) to time-based charging.
5. As not even this modest increase was agreed by UK ministers the FSA must reassess its meat charging policy.
6. The effect of having no increase in charges in this financial year means that, if the FSA wishes to work to a target net subsidy to industry in GB of £10 million by 2014/15, increases in charges beyond 2009/10 would have to be higher than those originally recommended by the Board. Increases of 17% a year each year from 2010/11 would be needed to get to a position by 2014/15 of recovering the full cost excluding SRM (see Annex 1). Increases of 12% each year would be needed to reach a £10m GB subsidy (see Annexes 2-3).
7. The strategic outcomes sought by the FSA are threatened by the lack of income. With the current and likely future squeeze /pressures on public funds, additional funding to cover the shortfall not raised from the modest increase in charges is

very unlikely. Given that food safety cannot be put at risk the FSA would therefore have to cut back considerably on some aspects of its other work such as dietary health, campaigns, research and communication activities The Board would need to review which programmes would have to cease or be deferred.

8. Overall, Government finances are stretched beyond historical limits. The 2007 Spending Review implemented funding cuts on the FSA for the first time. The next Spending Review may impose similar, or deeper, future funding cuts. Applying for additional funding from the Treasury to cover additional subsidies for official controls is not an option in the current economic climate and is inconsistent with the Treasury's charging policy.
9. HM Treasury guidance, Managing Public Money, applies to all UK countries. It requires that, if full costs are not to be recovered, the reasons for this should be clearly explained by Health/Rural Affairs Ministers across the UK. A justification of any subsidy, and the level of it, will need to be made. Ministers will be consulted on their views of what constitutes a realistic subsidy, if any, and how long it should apply for. Examples of where full cost recovery is normal can be seen in Government departments which provide Driving Licence and Land Registry services.
10. Full cost recovery of official controls (excluding SRM) if passed in full to consumers would result in minimal impact (see Annex 7 for details):

Product	Pence per item		
	Current	Proposed	Increase
Whole chicken (£4.00)	0.6p	1.4p	0.8p
500g. Lean mince (£1.92)	0.45p	0.92p	0.47p
Pork loin chop per kg (£6.15)	1.3p	2.7p	1.4p

11. If the full cost recovery were imposed by animal slaughtered in full on the farmer/producer the estimate of the impact would be (see Annex 7 for details):

Animal	Per carcase			
	Value	Current	Proposed	Increase
Chicken	£1.51	0.6p	1.4p	0.8p
Beef	£895	£4.38	£8.92	£4.54
Sheep	£74	£0.44	£0.89	£0.45
Pig	£100	£0.63	£1.27	£0.65

12. An agreed net subsidy, if any, and trajectory must be reaffirmed so that a long-term industry charging strategy can be implemented. This must then be aligned with the FSA's overall financial plan and government finances. In the mean time MHS continues to pursue cost reduction opportunities (as explained in Annex 5).

13. A stakeholder body would be constituted to consult on how best to apply the new policy. This would include farmers, slaughterhouse owners, packing plant owners, retailers, economists, and consumer representatives.

14. The Board is asked to:

- **agree** that providing the best possible protection for consumers from food risk should not be based on economic circumstances or the ability of an industry to pay;
- **agree** that it is not a function of the FSA to subsidise industry and if a continuing subsidy is to be provided it should come from elsewhere; and
- **agree** that FSA should consult with industry and government stakeholders on proposals for implementing the above strategy.

FSA/MHS

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FUTURE FUNDING OF UK MEAT CONTROLS

Issue

1. Earlier this year the Board agreed that the FSA should seek a 4% increase in the charges the MHS and DARD make to the meat industry for the controls provided in 2009/10. This was in line with the Board's objective, agreed in July 2007 to reduce the burden of meat industry inspection on taxpayers, while recognising that at that stage full cost recovery was not practical. The Board agreed to an overall £10 million subsidy for the industry in GB by 2014/15.
2. The FSA was unable to secure UK ministerial agreement to the proposed 4% increase in charges, although they did agree to move from the discredited Maclean charging mechanism (lower of throughput or time-based charging) to time-based charging.
3. As not even a modest increase was agreed by UK ministers the FSA must reassess its meat charging policy, and to ensure that it is in line with UK Government policy. To date our thinking and actions around the future funding of meat official controls has been linear, with incremental charging increases and no real change in overall strategy. This approach has not been effective and did not take account of political conditions in the UK, or possible future changes on the horizon both politically and in relation to public finances.
4. That being the case, the FSA Executive believes that a different approach must be taken. This paper proposes that a meat charging policy should be developed in line with the following principles:
 - a) the cost to the tax payer must be kept to a minimum in line with the Government's policy of full cost recovery for publicly provided goods and services;
 - b) FSA have to recognise the structure of the sector, in terms of size of plants and distribution across the UK;
 - c) increasing cost recovery must not adversely impact consumer protection required;
 - d) must meet EU obligations; and
 - e) test whether it is sensible for the imposition of meat control charges to fund the FSA which 'sponsors' both food safety and dietary health.

Strategic Aims

5. One of the outcomes in the draft FSA Strategic Plan for 2010-2015 aims for “A proportionate, risk-based regulatory regime relating to food, which is clear about the responsibilities of food business operators and others, and which generates public confidence in food”. The net subsidy to industry for official meat controls is funded through the Food Standards Agency. If this subsidy is not in line with plans, there will be less funding available for delivery of other FSA strategic priorities. The FSA’s new strategic plan will ensure that future resourcing reflects the priorities within this.
6. Overall, Government finances are stretched beyond historical limits. The 2007 Spending Review implemented year on year funding cuts on the FSA for the period 2008/09 to 2010/11 for the first time. The next Spending Review is likely to impose similar, or more probably deeper, funding cuts. If the MHS net cost of operations does not reduce significantly, this will limit the FSA’s ability to fund its new Strategic Plan. Currently around £36m of FSA funding (27%) is directed at meat hygiene enforcement and controls in GB.
7. A further £3.3m is paid to subsidise these controls in Northern Ireland (£6.7m cost of which £3.4m is recovered from industry).
8. Applying for additional funding from the Treasury to meet subsidies for official meat controls is not an option in the current economic climate and is inconsistent with the Treasury’s charging policy.

Background/Discussion

9. In April 09 the Board endorsed paper 09/04/06 “MHS Long Term Financial Plan” which showed the cost recovery trajectory for the MHS over the following 5 years to 2014/15. The Board agreed industry charge increases of:
 - 2009/10 4%
 - 2010/11 3%
 - 2011/12 7-8% and so on each year until 2014/15
10. These increases together with potential cost reductions of £10.8m (from reduced demand for industry hours, a scaling down of government programmes, efficiency reductions and One Agency cost saving measures) would result in a net subsidy to industry in GB of £10 million by 2014/15.
11. Despite the Board’s recommendation of a 4% charges increase in 2009/10 it was not possible to secure agreement from UK Ministers in the current economic climate. This has obviously had an impact on the funding of meat controls in the UK. Rather than hold off any charging increases until the economy is stronger (but conversely, probably lower livestock prices), the FSA has used this opportunity to consider its future funding strategy for official controls.

Impact of not securing the 4% increase for 2009/10

12. The effect of having no increase in charges in this financial year means that, if the Board wishes the FSA to continue to work to a target net subsidy to industry in GB of £10 million by 2014/15, increases in charges beyond 2009/10 would have to be higher than those originally agreed by the Board.
13. If there were no increase in 2010/11 followed by inflation matching increases of 2% for the following years, the net subsidy to industry would be in the region of £25 million by 2014/15. Higher than inflation increases in charges each year would be required to bring the net subsidy down.
14. The strategic outcomes sought by FSA are threatened by the lack of income. With the current and likely future pressures on public funds, additional funding to cover the shortfall not raised from the modest increase in charges is very unlikely. Given that food safety cannot be put at risk, the FSA would therefore have to cut back considerably on some aspects of its other work such as dietary health, campaigns, research and communication activities. The Board would need to review which programmes would have to cease or be deferred.
15. An initial zero-based budgeting exercise has started for 2010/11 and this will be refined for 2011/12. An effective process will ensure that resource allocation is prioritised in line with the new 5 year strategic plan. It will therefore identify projects that are no longer a priority within the overall budget.

Option for full cost recovery

16. Increases of 17% a year each year from 2010/11 would be needed to get to a position by 2014/15 of recovering the full cost (Graph in Annexe 1).

Option for retaining reduced subsidy

17. The FSA estimates that if the £10 million target net subsidy to industry in GB is to be achieved by 2014/15 then it would be necessary to increase hourly rates by an average of 12% every year between 2010/11 and 2014/15 (Graph in Annex 2).

Impact of current charging policy on meat prices

18. The cost to consumers of meat hygiene official controls is very low in relation to the cost of the meat they purchase. For example, the MHS element of the retail price per chicken is around 0.75p of a retail price of between £3 and £5 per bird. For a 500g pack of standard minced beef the maximum MHS element in the abattoir is 0.5p out of a retail price of around £1.92. For a pork loin chop the maximum MHS element is 1.3p per kg out of a retail price of around £6.15. The FSA is currently considering commissioning a firm of consultants to provide independent economic analysis of how increased charges are likely to impact on industry sectors. This work will consider input process, livestock and meat prices, the returns from farming and cost to consumers of meat control charges.
19. If all additional costs from the removal of the subsidy were to be passed on to the consumer, assuming no improvement in efficiency, the prices would be estimated to rise as follows:
- Chicken (less than 2kg) 0.8p;
 - 500g pack of standard mince 0.5p;
 - Lamb leg steak 2.9p per kg;
 - Pork loin chop 1.4p per kg.
20. If all additional costs from the removal of the subsidy were to be passed on to the farmer, assuming no improvement in efficiency, the cost per animal would be estimated to rise as follows¹:
- Cow (adult bovine) £4.54;
 - Pig (25kg and larger) £0.65;
 - Chicken (less than 2kg) £0.008 (i.e. 0.8p);
 - Sheep (over 18kg) £0.45.

In reality, as described below, efficiency is improving and is likely to improve further with a greater transfer of the cost to industry leading to greater incentives

¹ Estimated by calculating the average cost and charge per animal unit, based on 2008/09 throughput volumes and hours and 2009/10 charge rates.

to invest for greater efficiency, so these figures are likely to overestimate the impact.

The economics of the meat industry

21. Trends in the meat production sector suggest that the sector overall is performing well in a difficult economic climate. The volume of meat production in the UK has been relatively stable in recent years. There has been substantial growth in livestock and producer (farm gate) prices and retail prices of meat products particularly during 2008, with recent prices more stable at a higher level. Input prices in the sector have eased, with wages remaining fairly stable through 2009, and some recent falls in prices for materials and fuels. The depreciation of sterling against the euro has also given a boost to prices. The export of meat from the production and preserving sector rose by 12.5% in the year to June 2009. Provisional estimates of farm income data published by Defra in January 2009 showed that the total income from farming in the UK is estimated to have risen in 2008 by 41.9% at current prices, or by 36.3% in real terms, to £3.46 billion. This suggests an overall healthy sector.

Other revenue streams

22. A proportion of the MHS's net cost, not recovered from the meat industry, is paid by Defra as a result of the re-introduction in 2005 of rules to permit over 30 month cattle for human consumption. This amounts to around £3m million per year. As budgetary pressures increase on all Government Departments, Defra is keen for the FSA to absorb this cost. Income from Government customers has declined by 44% from £34.6m in 2006/07 to a forecast £19.3m in 2009/10. There is pressure from Defra and its Agencies for further reductions to be implemented in the rest of this financial year. In future years this has the potential to reduce MHS income by a further £3-4m and has already been built into the financial modelling.

Impact of FSA and MHS cost reduction work

23. The FSA and MHS continue to review costs to deliver savings which will translate into a reduction in net operating costs. However internal savings by themselves will not reduce the net subsidy to industry in GB to £10 million. To date the MHS has reduced its operating costs from £91.3m in 2006/07 to £69m in 2009/10. These savings mean that industry charges would not have had to rise by as much to reach a £10 million subsidy in GB. The scope for future significant savings in operating costs is minimal whilst the current EU controls on meat hygiene are in place.
24. The One Agency initiative will yield savings for both the MHS and FSA Corporate Services. These are expected to be around £1.8m. The MHS share of these savings will also need to be confirmed, but is estimated to be £0.9m.

Impact of business agreements

25. Business Agreements (BAs) build on existing provisions for the agreement of MHS staffing levels necessary to deliver official controls in line with the requirements of individual Food Business Operators. However, the BA goes into much more detail than in the past and the process of agreeing a BA can facilitate a much better understanding between the MHS and an industry client.
26. The roll-out of Business Agreements has now been carried out for Slaughterhouses and is progressing well for Cutting Plants. Regular reviews of agreements at existing establishments will continue on an ongoing basis. Of the 351 Slaughterhouses², that has been visited 176 have a signed BA in place and 175 have an unsigned Business Agreement. Efficiency improvements and staffing reductions are being introduced through this process and as part of normal business-as-usual activities. Business Managers are positively engaging with Food Business Operators to identify opportunities for further streamlining of MHS teams with Food Business Operator commitment.
27. In order to provide an indication of the impact of Business Agreements and the benefits to the MHS and to Food Business Operators, an analysis has been carried out on the agreements at all slaughterhouses. This has calculated the average hours of chargeable time per week for up to six months prior to and following the implementation of the agreement.

Table 1 Hours reductions following introduction of Business Agreements

Number of agreements analysed		Average weekly chargeable hours 6 months prior to implementation	Average weekly chargeable hours 6 months after implementation	Difference
329*	Totals	29,978	28,507	1,471 (4.9%)
	Average per Establishment	91.1	86.6	4.5

* 22 agreements were not included due to seasonal / infrequent operating which could not be used for comparison either side of implementation of the agreement.

28. In the six months following the implementation in slaughterhouses an average of 1,471 fewer hours per week have been worked. This is reducing industry charges by an estimated £1.3m in a full year. N.B. Business Agreements will have been a major factor in this but cannot be considered the only factor.
29. The figures show that the implementation of Business Agreements has been a key to reducing MHS staff hours in approved establishments.

² Out of a total 358 operational Slaughterhouses 351 have been visited and 7 only operate on a seasonal basis

UK Government policy on cost recovery

30. The UK Government has a clear policy to charge for publicly provided goods and services. The norm is to charge at full cost and for the same charge to apply to all recipients and users of those goods and services. Differentiation is not permitted for different kinds of customers and cross-subsidisation is not encouraged i.e. larger companies paying more to enable lower costs for smaller companies. If a financial target short of full cost recovery is set, Government requires that there should be a plan to achieve full cost recovery within a reasonable period, which must be agreed by Ministers. If this is not intended, as is currently the case with the FSA's meat charging policy, it is important to decide why and for how long any deliberate public subsidy should last.
31. The FSA is responsible for other chargeable statutory services including radiological risk assessment and monitoring of radioactive waste discharges from nuclear licensed sites. As a statutory consultee, the FSA fully reclaims costs for assessing the potential food safety implications of changes to authorisations. The FSA operates a monitoring programme where the costs for the majority of samples can be reclaimed from the nuclear industry. Some samples are taken to comply with EC and international requirements, and a small number of background samples are taken, that cannot be charged for.
32. Ministers must be consulted on their views of what constitutes a realistic subsidy and how long it should apply for.
33. The Chief Executive met with Treasury officials in September to discuss cost recovery options. The Treasury explicitly reaffirmed the principle of full cost recovery and confirmed they would provide support to the FSA in reducing the industry subsidy. They recognised the importance of matching policy responsibility with financial consequences.

Devolved Government's policy on cost recovery

34. The FSA works in a devolved area and must seek the agreement of Ministers in all four countries of the UK in any policy it wishes to pursue in relation to cost recovery. However, while policy on delivery of meat controls and charging is devolved, the budget in Scotland and Wales currently is not. This creates a tension where there is a mis-match between devolved policy decision-making and the fiscal consequences of these decisions.
35. Rural Affairs Ministers have a strong interest in this area, and their views are highly influential, as MHS charges have a direct impact on the meat sector for which they are responsible. They also recognise drivers to support local and rural slaughterhouses. We are bound by the European charging legislation in this area, which requires all Member States, including the UK, to take certain factors into consideration when setting fees. These factors include 'the interests of business with a low throughput' and 'the needs of businesses located in regions subject to particular geographic constraints'.

FSA Board's policy on cost recovery

36. To date the FSA Board has agreed with the UK Government's policy on full cost recovery for publicly provided goods and services. It also recognised however that moving to full cost recovery in the medium term would be unachievable in the current economic climate and therefore agreed to what is effectively a £10 million subsidy for the meat industry in GB from 2014/15. It agreed this subsidy in the belief that meat sector would accept modest increases to charges each year to reduce the financial impact, combined with costs savings delivered through MHS costs reductions, the introduction of the more efficient time-based charging regime, and business agreements. Industry's acceptance was not forthcoming. **The FSA Board therefore needs to consider whether its current policy on the £10m subsidy in GB should remain or change.**

Other ways of recovering costs: levy

37. The UK Government will permit compulsory levies to be charged, such as for a licence to operate. It would be important first to determine whether this is , taxation . Such licences are justified in the wider public interest and not to provide a beneficial service to those who pay for them. The UK Government may allow a statutory regulator to retain the fees charged if this approach is efficient and in the public interest. As with other fees and charges, levies of this kind must be designed to recover the full costs of the service provided. It is important for any levy raised to relate directly to the cost of the work undertaken. It may be appropriate to charge different levies for different kinds of approvals, depending on the cost of providing the approval. Any such levies would not be for officials controls and so would not be covered by existing charges regulations but would need to be covered instead by a separate Statutory Instrument. **The Board may wish to discuss whether a different charging regime is viable.** However the introduction of time-based charging was the overall preferred method of the stakeholder charges working group who considered possible options in 2008.
38. Other hybrid options could be considered, e.g. retention of time-based charges alongside an operator's licence fee using a turnover-based scale to bridge the funding gap. However this may be perceived as a barrier to trade and contrary to EC competition rules.

Alternative ways of reducing the FSA's shortfall in funding

39. We should consider better aligning policy decisions for charging with the financial consequences. This could be implemented by either:
 - a) invoicing the under-recovery of MHS costs by country; or
 - b) transferring budgets and financial responsibility for meat hygiene inspections and enforcement work to the devolved administrations.
40. FSA could consider further the possibility of differential charging in England, Scotland, Wales and Northern Ireland. This may be an option as there are significant differences within and between EU countries already, but would need to be looked into further.
41. On a country basis, incentives (such as increased food hygiene education and training) could be provided from the extra income raised in return for the acceptance of increased charge-out rates generally.

European Commission minima charges

42. The rules on meat hygiene charges are set out in European legislation. These set down minimum throughput charges and in general the charges made must be no less than these figures. Member States (MS) may make charges per carcase / tonne of meat or on a time basis. However, the charges made must be no more than the actual costs incurred in carrying out the official controls.
43. The EC report on Member State (MS) compliance with EU charging rules has recently been disseminated to MSs and a discussion and negotiation on possible changes to EC rules has commenced. The report³ shows that charges made vary significantly between, and in some cases within, countries. For example, in Germany fees being charged can vary considerably between German Federal Landers leading the German meat industry to contact the European Commission directly on this subject.
44. The report does not indicate the likely future direction of EC charging policy, leaving all possibilities from complete MS subsidiarity to fixed EC charge rates open for discussion. Any changes are unlikely to come into force until 2012 at the very earliest. This may affect our net subsidy and charging trajectory proposals. FSA could, however, seek to negotiate a new EC approach to charging that is more consistent with the overall UK Government approach to full cost recovery.
45. The key conclusions and recommendations from this EC report were that:

³ European Commission Directorate General for Health and Consumers "Study on fees or charges collected by the Member States to cover the costs occasioned by official controls" Final Report Prepared by the Food Chain Evaluation Consortium (FCEC) Civic Consulting – Van Dijk MC Arcadia International – Agra CEAS Project Leader: Agra CEAS Consulting Food Chain Evaluation Consortium 28 January 2009

- there is widespread variation between MSs in the interpretation and implementation of EC charging requirements;
- some MSs do not collect mandatory fees and some charge rates below EU minimum fees;
- there is a lack of a rationale for the EC minimum charge rates;
- there is widespread variation in the level, frequency and standard of official controls and significant variation in the structure and organisation of control authorities across MSs with consequential implications for the costs and charges for official controls (for example, in France the Government funds 70% of the costs of rendering, whereas in the UK this is entirely funded by industry); and
- the EC fees system creates some minor distortions in competition particularly discriminating against the meat industry [and smaller businesses] as it imposes the cost of official controls on meat producers whereas other businesses in the supply chain also benefit.

46. Aside from the above review, the EC is required to review minimum charge rates every two years. This is now overdue. FSA could formally recommend the EC minimum rates be increased ahead of the wider review of charging requirements.

47. Evidence is emerging that the full cost of meeting the controls required by the EU are passed on, in full and sometimes with a profit margin added, to farmers in some EU countries.

48. Annex 4 to this paper provides further detail of European charging approaches by MSs.

Subsidise or not? How to allocate?

49. When the Board last discussed meat charging it effectively agreed to subsidise the meat industry in GB by £10 million a year from 2014/15. In seeking to secure the finances of the FSA for the future, the Board should decide whether it wishes this subsidy to continue to exist in any finance strategy the FSA devises. However, this should be done with firm reference to the UK Government position that any subsidy cannot continue indefinitely without documented justification and consideration of how long the subsidy should remain.

50. If the Board decides to continue with a subsidy it should also consider how it wishes the subsidy to be allocated taking into account the requirements in the EU charging legislation, and seek input from the rural affairs departments. Should it be allocated equally across the whole sector or, for example, by size and location of business so that those businesses with lower levels of throughput

or who are geographically isolated receive a greater share of the subsidy than large or easily accessible businesses? Care would have to be taken however not to subsidise inefficient or non-compliant businesses.

51. Distributing a subsidy could be based on any or all of the following:
- a) Geography – remote plants could be subsidised for reasons of animal welfare and sustainability;
 - b) Size of plant – based on throughput or turnover. This might be assessed daily, weekly, monthly or annually for seasonal plants (time-based charging has a greater impact on ‘inefficient’ operations with slow production processes);
 - c) Local Economy – in areas where potential closure of an establishment would have a significant impact on the local economy.
 - d) Competition – to facilitate competition within an area where any closures would leave remaining establishments in a more monopolistic position.
 - e) Compliance Levels of food business operators – those who take more responsibility could receive more subsidy than those who do not and require more controls.

Financial impact

52. The graph in Annex 1 illustrates costs, total income and the increases in industry income required to achieve full cost recovery by 2014/15. Increases of 17% for each year from 2010/11 to 2014/15 would be necessary to meet that objective.
53. The graph in Annex 2 illustrates the income from other possible scenarios for increases. The gap between total income and cost, the subsidy target, ranges from £10m with 12% increases in industry income to £25m with no increase in 2010/11 followed by 2% for inflation. Income from industry by 2014/15 ranges from around £40m to £25m. (All figures are in monetary terms). Lower increases in earlier years would mean proportionately greater increases in later years in order to meet any particular target.
54. Cost Reductions – MHS cost trajectories are analysed in Annex 5. The costs included in the scenarios presented in Annexes 1 and 2 include reductions realised or expected as a result of:
- the implementation of time-based charging, business agreements, optimisation recommendations and business efficiency measures,
 - an estimation of the savings from integrating MHS/FSA Corporate Services; and
 - scaling down of government programmes e.g. cattle passports checks

Further savings may be realised if changes to the EC regulatory regime are made. However, this will not happen in the short to medium term and has not been included in the projections.

55. Certain SRM, by-products, policy and approvals work is now managed by MHS. Whilst this has no effect on FSA overall finances it does have a direct effect on MHS net cost of operations, which increases by the same amount as the reduction in FSA Food Safety Group costs. This will have a purely presentational effect of increasing MHS net cost of operations by the value of the transfer (£8m). There is no impact on the net subsidy to industry from this change, e.g. in 2009/10 the MHS net cost will be £8m more than before the change and the FSA's programme costs for Meat Hygiene will be £8m lower. The 'One Agency' impact is neutral. The Board decided in April 2009 that, following the results of consultation, no charges would be made to industry for SRM related costs. However this paper assumes that SRM controls will continue to be funded by Government. The April 2009 Board paper did not rule out the possibility of charging industry for these controls in the future.

Conclusion

56. An agreement regarding any subsidy and trajectory for achievement is required so that a long-term industry charging strategy can be implemented. This must then be aligned with the FSA's overall financial plan and government finances, and agreed with Ministers across the UK.
57. A stakeholder body would be constituted to consult on how best to apply the new policy. This would include farmers, slaughterhouse owners, packing plant owners, retailers, economists, and consumer representatives.

Previous Board consideration

58. The 'MHS Long Term Financial Plan' (paper 09/04/06) was presented to the FSA Board on 21/4/09 illustrating the cost recovery trajectory for the Meat Hygiene Service. This highlighted industry charges increases and potential cost reductions which would result in a target net subsidy to industry in GB of £10m by 2014/15. The Board endorsed the paper, which reaffirmed the £10m net subsidy target. This provided an indication for all stakeholders of likely future charging increases in the medium term.

Board Action Required

59. The Board is asked to:

- **agree** that providing the best possible protection for consumers from food risk should not be based on economic circumstances or the ability of an industry to pay;
- **agree** that it is not a function of the FSA to subsidise industry and if a continuing subsidy is to be provided it should come from elsewhere; and
- **agree** that FSA should consult with industry and government stakeholders on proposals for implementing the above strategy.

List of Annexes

- Annex 1** Financial Strategy for Full Cost Recovery (excluding the cost of SRM controls)
- Annex 2** Financial Strategy Cost & Alternative Income Trajectories (SRM controls not charged).
- Annex 3** Alternative scenarios
- Annex 4** Inspection Rates for Other EU Countries
- Annex 5** Cost Trajectory
- Annex 6** Illustrative Distribution of Subsidy
- Annex 7** Impact of MHS Charges

Figure 1 Financial Strategy for Full Cost Recovery (excluding the cost of SRM controls)

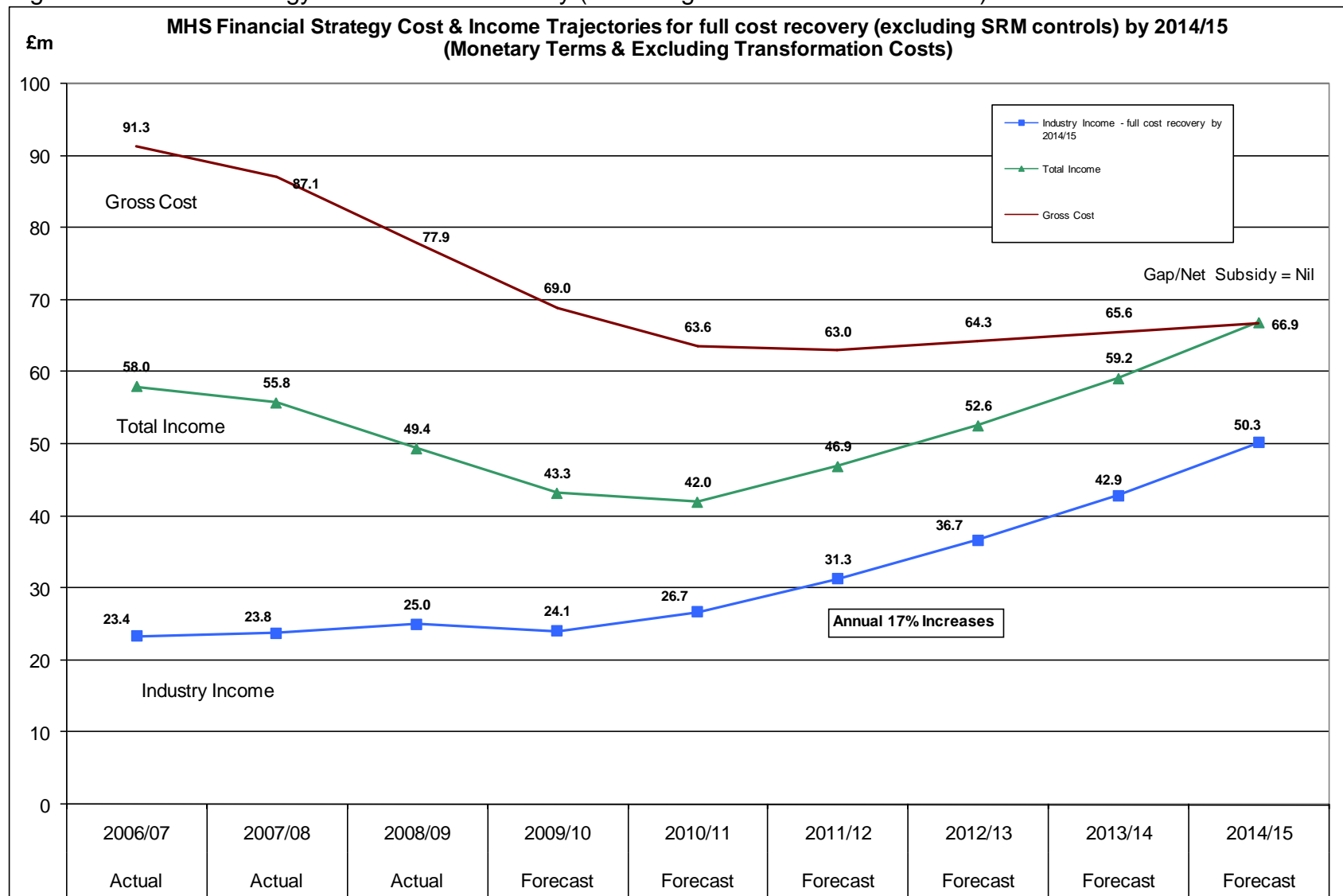
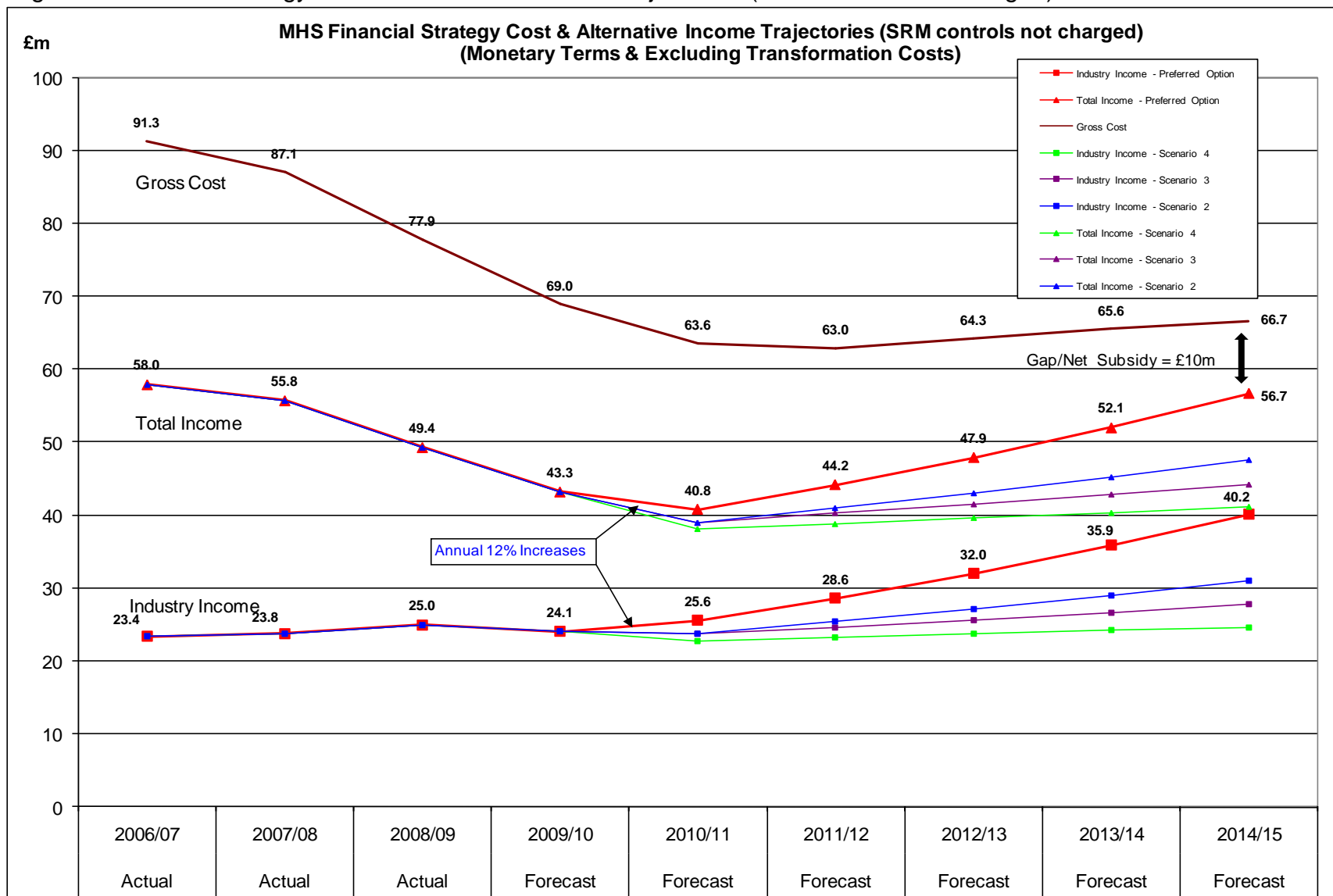


Figure 2 Financial Strategy Cost & Alternative Income Trajectories (SRM controls not charged). Details of scenarios in Annex 3



Alternative scenarios

- Four alternative trajectories to 2014/15 are set out below. These show that no charge increase in this financial year or next means the increases required in later years would need to be significantly higher to achieve a £10m net subsidy in GB.

Table 3 Alternative % Increases in hourly rates (The costs and income for these scenarios are presented graphically in Annex 2)

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	Net Subsidy (excluding SRM)
Current GB Subsidy 2009/10							£25m
Scenario 1 - To reach £10m Net Subsidy	0%	12%	12%	12%	12%	12%	£10m
Scenario 2 - £19m Net Subsidy	0%	4%	7%	7%	7%	7%	£19m
Scenario 3 - £22m Net Subsidy	0%	4%	4%	4%	4%	4%	£22m
Scenario 4 - £25m Net Subsidy	0%	0%	2%	2%	2%	2%	£25m

Inspection Rates for Other EU Countries

1. The table below demonstrates that costs in absolute terms are very low and that the UK is broadly in line with other EU Member States (MS).
2. It is taken from the European Commission Directorate General for Health and Consumers “Study on fees or charges collected by the Member States to cover the costs occasioned by official controls” Final Report Prepared by the Food Chain Evaluation Consortium (FCEC) Civic Consulting – Van Dijk MC Arcadia International – Agra CEAS Project Leader: Agra CEAS Consulting Food Chain Evaluation Consortium 28 January 2009.

**COMPARISON OF MS THROUGHPUT CHARGES FOR ADULT BOVINES,
POULTRY (<2KGS), AND PIGS (>25KG) AS A % OF PRICE**

CATTLE

Country	Charge (Adult Bovine) (€)	Charge per kg of usable meat (€)	Price per kg of live weight (€)	Charge as a % of price
France	5	0.025	1.85	1.30%
Italy	5	0.026	1.92	1.40%
Poland Auto	2.85	0.016	1.04	2.10%
Poland non auto	3.89	0.022	1.04	1.60%
Slovakia	5.6	0.031	1.27	2.40%
UK	5	0.022	1.63	1.40%
Ireland (90% FBOs)	4.75	0.021	1.45	1.50%
Ireland (other FBOs)	5.40	0.024	1.45	1.70%

Data Source: FAOSTAT (<http://faostat.fao.org/>)

Notes: Charge per kg of useable meat based on average carcass weights in 2006; prices per kg of cattle live weight calculated from average prices per tonne live weight in 2006 (most recent data available for all MS included); 70% of a cattle carcass is assumed to be useable meat; prices obtained in US\$ and converted at the average US\$:Euro exchange rate in 2006.

POULTRY

Country	Charge (Poultry < 2kg) (€)	Charge per kg of usable meat (€)	Price per kg of live weight (€)	Charge as a % of price
France	0.0068	0.0080	0.88	0.91%
Italy	0.005	0.0042	0.74	0.57%
Poland	0.01	0.0095	0.64	1.48%
Slovakia	0.006	0.0057	0.67	0.84%
UK	0.0095	0.0089	0.76	1.16%

Data Source: FAOSTAT (<http://faostat.fao.org/>)

Notes: Charge per kg of useable meat based on average carcass weights in 2006; prices per kg of chicken live weight calculated from average prices per tonne live weight in 2006 (most recent data available for all MS included). The method of slaughter for chickens in Poland is consistent with the other countries. The charge for poultry in France is assumed to be taxed at the same rate as for adult bovines. 70% of a chicken carcass is assumed to be useable meat; prices obtained in US\$ and converted at the average US\$:Euro exchange rate in 2006.

PIGS

Country	Charge (Pigs > 25kg) (€)	Charge per kg of usable meat (€)	Price per kg of pig live weight (€)	Charge as a % of price
France	1	0.016	0.97	1.63%
Italy	1	0.012	1.39	0.88%
Poland auto	1.06	0.018	0.91	1.92%
Poland non auto	1.42	0.023	0.91	2.57%
Slovakia	1.12	0.017	1.20	1.44%
UK	1.23	0.023	1.22	1.87%
Ireland	1.30	0.024	1.30	1.81%

Data Source: FAOSTAT (<http://faostat.fao.org/>)

Notes: Charge per kg of useable meat based on average carcass weights in 2006; prices per kg of pig live weight calculated from average prices per tonne live weight in 2006 (most recent data available for all MS included). 70% of a pig carcass is assumed to be useable meat; prices obtained in US\$ and converted at the average US\$:Euro exchange rate in 2006.

Cost Trajectory

Figure 3 Cost Forecasts

MHS Cost Trajectory 2008-09 - 2014/5					
2008-09 Baseline (excl TMHS)	2008-09	2009-10	2010-11	2011-12	2012-13
Plant-Based Employed Inspection and Veterinary Staff	34.9	31.4	27.6	28.3	28.9
Contracted Inspection and Veterinary Staff	25.3	20.1	18.9	18.3	18.6
HQ Staff & Operational Support Costs	7.2	7.2	7.2	6.4	6.6
LGPS Additional Pension Contribution	1.4	1.0	1.0	1.0	1.0
Laundry Sampling & Equipment	2.5	2.5	2.3	2.3	2.4
Capital Charges	0.4	0.6	0.7	0.7	0.7
IT, Accommodation and Administrative Overheads	6.3	6.3	5.9	6.0	6.1
	77.9	69.0	63.6	63.0	64.3
Assumptions	Inflation	2%	2%	2%	2%

Comparison of MHS Gross Cost Estimates between April and September Board papers							
Paper	Actual 2006/07	Actual 2007/08	Actual 2008/09	Forecast 2009/10	Forecast 2010/11	Forecast 2011/12	Forecast 2012/13
April	91.3	87.1	78.1	71.5	67.2	65.4	62.7
Sept	91.3	87.1	77.9	69.0	63.6	63.0	64.3
Variance			-0.2	-2.5	-3.6	-2.4	1.6

1. A fresh look at cost assumptions since the April Board Paper shows that MHS will continue to reduce costs until a plateau is reached after 2010/11. After this it may not be feasible for the cumulative effects of inflation to be offset by further efficiency measures on top of the significant progress that will have been made by that time.

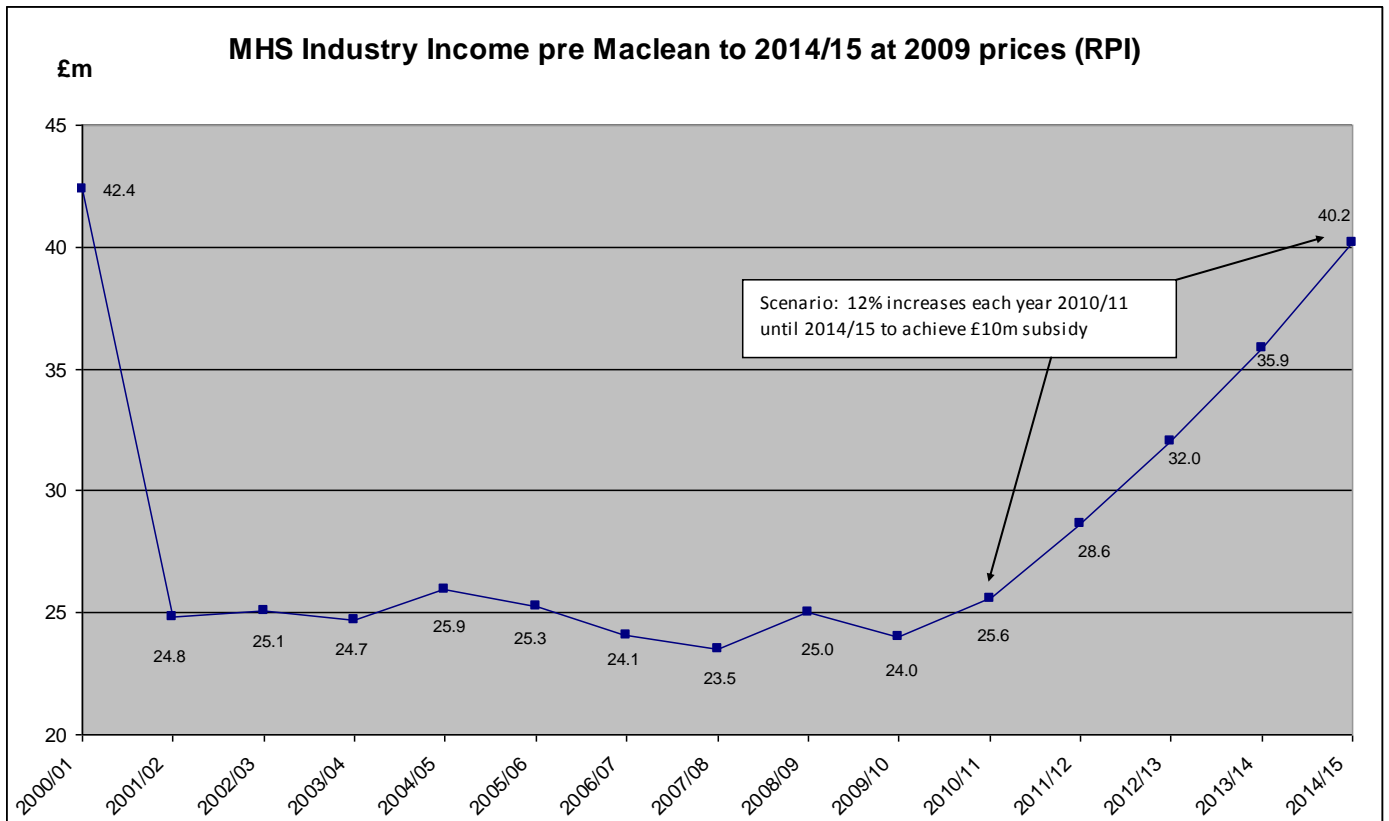
Operational Efficiency

2. Since the beginning of 2009 ongoing efficiencies are expected from an integrated programme of changes which are plant specific:
 - Optimisation, including the move to risk-based activities and FBO changes to their methods of working in plant (some of which may require significant investment by FBOs);
 - Working in partnership with FBOs on local business agreements, which identify effective planning and deployment to save industry costs and allow improved management of MHS resources. For every £1m gross cost saving from official controls work it is estimated that the net cost may be reduced by £500k. This assumes around 50% of the cost is recovered

from industry, and overheads can be reduced in line with operational cost reductions. Government work is charged on a full cost recovery basis, and therefore gross cost reductions here have nil effect on net cost;

- Introduction of time-based charging which will focus attention by the FBOs on activity and associated costs to drive more effective MHS resourcing;
- Continual improvement brought about from organising MHS resources on a cluster basis, including the deployment of Lead Veterinarians to manage plant activities; and
- Implementation of the new contracting arrangements for Official Veterinarians and Meat Inspectors are targeted to promote performance improvement leading to resource reductions as well as providing significant cost savings (c. £5m p.a. from 2009/10). This saving has been incorporated into MHS future forecasts.

Figure 4 MHS Industry charges comparison with pre Maclean situation. 2014/15 charges of £40.2m would still be below the £42.4m charged in 2000/01 (all figures at 2009 prices).



Illustrative Distribution of Subsidy

1. The table below illustrates a scenario where hourly rates are increased by an illustrative 12% in 2010/11 and indicates the resulting subsidy using the current distribution across differently sized meat plants. This distribution results from the effect of the Maclean charging method i.e. all sizes of plants benefit from a subsidy. A £10m GB subsidy would be enough to continue the current position for all micro plants (up to 1 livestock unit per week) and small plants (between 1 and 100 livestock units per week) with some remaining subsidy for distribution to a proportion of larger plants (over 100 livestock units per week). This could be done using some or all of the criteria in the examples given above

Table 2 Distribution of subsidy 2010/11 (with 12% hourly rate increase)

Size Livestock units per week	Micro less than 1	Small 1 to 100	Medium 100 to 1,000	Large 1,000 to 2,500	Very Large over 2,500	Total
No. of slaughterhouses	47	207	125	26	7	412
Subsidy	£m	£m	£m	£m	£m	£m
Red	0.1	3.4	11.1	1.9	0.4	16.9
Poultry	0.1	1.5	2.2	2.0	2.4	8.2
Cutting	0.1	0.1				0.2
Game	0.1	0.2				0.3
Total	0.4	5.2	13.3	3.9	2.8	25.6
Cumulative total	0.4	5.2	13.3	3.9	2.8	25.6

Impact of MHS Charges

Full cost recovery of official controls (excluding SRM) if passed in full to consumers would result in minimal impact:

Product	Pence per item		
	Current	Proposed	Increase
Whole chicken (£4.00)	0.6p	1.4p	0.8p
500g. Lean mince (£1.92)	0.45p	0.92p	0.47p
Pork loin chop per kg (£6.15)	1.3p	2.7p	1.4p

Estimated by calculating the average charge and cost per animal unit, based on 2008/09 throughput volumes and hours and 2009/10 charge rates. Note that this assumes no improvement in efficiency, whereas we know that efficiency is improving and is likely to improve further, so these figures are likely to overestimate the impact.

If the full cost recovery were imposed by animal slaughtered in full on the farmer/producer the estimate of the impact would be:

Animal	Per item ⁴			
	Value	Current	Proposed	Increase
Chicken	£1.51 ⁵	0.6p	1.4p	0.8p
Beef	£895 ⁶	£4.38	£8.92	£4.54
Sheep	£74 ⁷	£0.44	£0.89	£0.45
Pig	£100 ⁸	£0.63	£1.27	£0.65

⁴ Charges per item estimated by calculating the average cost and charge per animal unit, based on 2008/09 throughput volumes and hours and 2009/10 charge rates.

⁵ This price is for live chickens

⁶ This price is for beef carcasses. Deadweight value for beef estimated using AHDB meat services data on weekly deadweight producer (farmgate) prices per kg (average from January to August 2009) multiplied by average dressed carcass weight in 2008 (latest available) from the Defra publication Agriculture in the UK

⁷ This price is an average for standard quality quotation (SQQ) old and new season lambs sold at auction

⁸ This is the average price at auction