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## STRATEGY ON CHARGING FOR MEAT OFFICIAL CONTROLS

Report by Andrew Rhodes, Director of Operations

For further information contact Andrew Rhodes on 020 7276 8615, email:

[andrew.rhodes@foodstandards.gsi.gov.uk](mailto:andrew.rhodes@foodstandards.gsi.gov.uk)

### 1 SUMMARY

- 1.1 The FSA's proposals for the introduction of full cost recovery for meat official controls have not received the necessary regulatory approvals.
- 1.2 The current system is not sustainable, due to the inequitable distribution of the subsidy and the distortions in the market this can cause.
- 1.3 Considerable effort has been invested in stakeholder engagement on meat charging issues over recent years. While there are many points of contention there are several aspects on which there is agreement. There is the potential to use this as a platform for closer partnership working with stakeholders in order to build greater consensus.
- 1.4 The Board is asked to:

**Note** that:

- Decisions on meat charging policy are affected by a range of other issues
- There is an appetite among stakeholders for greater collaboration

**Agree** that:

- The FSA's priority in relation to charging policy is to protect the interests of consumers
- That the FSA should pursue a more collaborative approach with stakeholders interested in these issues, working in partnership to deliver shared outcomes
- That priority should be given to building a more consensual approach to progressing three issues:
  - A review of the current discount system making recommendations on how to reform the system to address anomalies
  - Joint working to identify further ways to reduce costs while continuing to deliver effective consumer protection, building on the outcomes of an efficiency review.
  - Exploring with stakeholders the options for alternative delivery models, including through the use of a control body
- An external efficiency review of the delivery of UK meat official controls and support functions should be carried out
- Discussions should continue with other Government departments on their appetite for taking on responsibility for allocating any ongoing subsidy

## 2 INTRODUCTION

2.1 The discussion section of this paper is divided into the following sections:

1. An overview of the meat processing industry in the UK, the legislative requirements on controls and how they are currently delivered
2. The costs of delivering the controls and the current charging system
3. Current Europe-wide issues
4. Future challenges and recommendations

2.2 The paper provides a high level overview of the current situation and issues. It refers to several major Board discussions in recent years including:

- July 2007 – Review of the Delivery of Official Controls in Approved Meat Premises [FSA 07/07/06]
  - November 2009 – Future Funding of UK Meat Controls [FSA 09/11/06]
- Board members may wish to refer to these papers as they contain considerable additional information on the charging structure and the decisions made by the Board at those dates.

## 3 STRATEGIC AIMS

3.1 Charging policy is a contributory part of strategic outcome 5: “regulation is effective, risk-based and proportionate, is clear about the responsibilities of food business operators, and protects consumers and their interests from fraud and other risks”.

## 4 DISCUSSION

### Section 1 – Overview of meat industry and official controls

4.1 In 2011/12 there were 376 slaughterhouses, 51 game handling establishments and 906 cutting plants in the UK, at which close to a billion birds or animals are processed each year. Table 1 shows the breakdown of these plants by size and country.

Table 1

**Distribution of Approved Establishments Based on 2011/12 Throughput**

|                         | <b>Red Meat<br/>Slaughterhouses</b> | <b>Poultry<br/>Slaughterhouses</b> | <b>Game Handling<br/>Establishments</b> | <b>Cutting<br/>Plant</b> |
|-------------------------|-------------------------------------|------------------------------------|---|--------------------------|
| <b>England</b>          |                                     |                                    |   |                          |
| Small                   | 55                                  | 19                                 | 8                                       | 151                      |
| Medium                  | 54                                  | 19                                 | 9                                       | 191                      |
| Large                   | 55                                  | 20                                 | 8                                       | 183                      |
| Very Large              | 47                                  | 17                                 | 10                                      | 163                      |
| <b>Total</b>            | <b>211</b>                          | <b>75</b>                          | <b>35</b>                               | <b>688</b>               |
| <b>Northern Ireland</b> |                                     |                                    |   |                          |
| Small                   | 1                                   |                                    | 1                                       | 19                       |
| Medium                  | 1                                   | 2                                  |   | 5                        |
| Large                   | 3                                   | 2                                  |   | 9                        |
| Very Large              | 9                                   | 2                                  |   | 24                       |
| <b>Total</b>            | <b>14</b>                           | <b>6</b>                           | <b>1</b>                                | <b>57</b>                |
| <b>Scotland</b>         |                                     |                                    |   |                          |
| Small                   | 13                                  | 3                                  | 3                                       | 33                       |
| Medium                  | 4                                   | 1                                  | 3                                       | 14                       |
| Large                   | 9                                   | 1                                  | 4                                       | 23                       |
| Very Large              | 10                                  | 1                                  | 5                                       | 29                       |
| <b>Total</b>            | <b>36</b>                           | <b>6</b>                           | <b>15</b>                               | <b>99</b>                |
| <b>Wales</b>            |                                     |                                    |   |                          |
| Small                   | 3                                   | 1                                  |   | 23                       |
| Medium                  | 12                                  | 1                                  |   | 16                       |
| Large                   | 4                                   |                                    |   | 12                       |
| Very Large              | 5                                   | 2                                  |   | 11                       |
| <b>Total</b>            | <b>24</b>                           | <b>4</b>                           | <b>0</b>                                | <b>62</b>                |

4.2 EU legislation requires meat official controls to be delivered in all meat plants; their aim is to protect public health, animal health and animal welfare. The FSA is the central competent authority in the UK in relation to meat hygiene. In England, Scotland and Wales the official controls are delivered directly by the FSA; in Northern Ireland the controls are delivered by the Department of Agriculture and Rural Development through a Service Level Agreement with the FSA in Northern Ireland.

4.3 Official controls are not unique to the meat industry. Official controls are carried out in a wide range of premises and embrace a variety of functions including inspections, approvals and certification. For example the FSA is also directly responsible for the official controls on shellfish, wine and dairy. The local authority inspections of food and feed premises are official controls. However, in these other examples the cost of delivering controls is not directly charged for. Meat official controls are different because they require a permanent presence of veterinary and meat hygiene inspectors in the majority of premises that slaughter. During 2011/12 the FSA employed, either directly or through contractors, 270 veterinarians and 769 meat inspectors (Full Time Equivalents) to carry out the official controls in Great Britain. In

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Northern Ireland DARD Veterinary Services employs 30 official veterinarians and 100 meat hygiene inspectors.

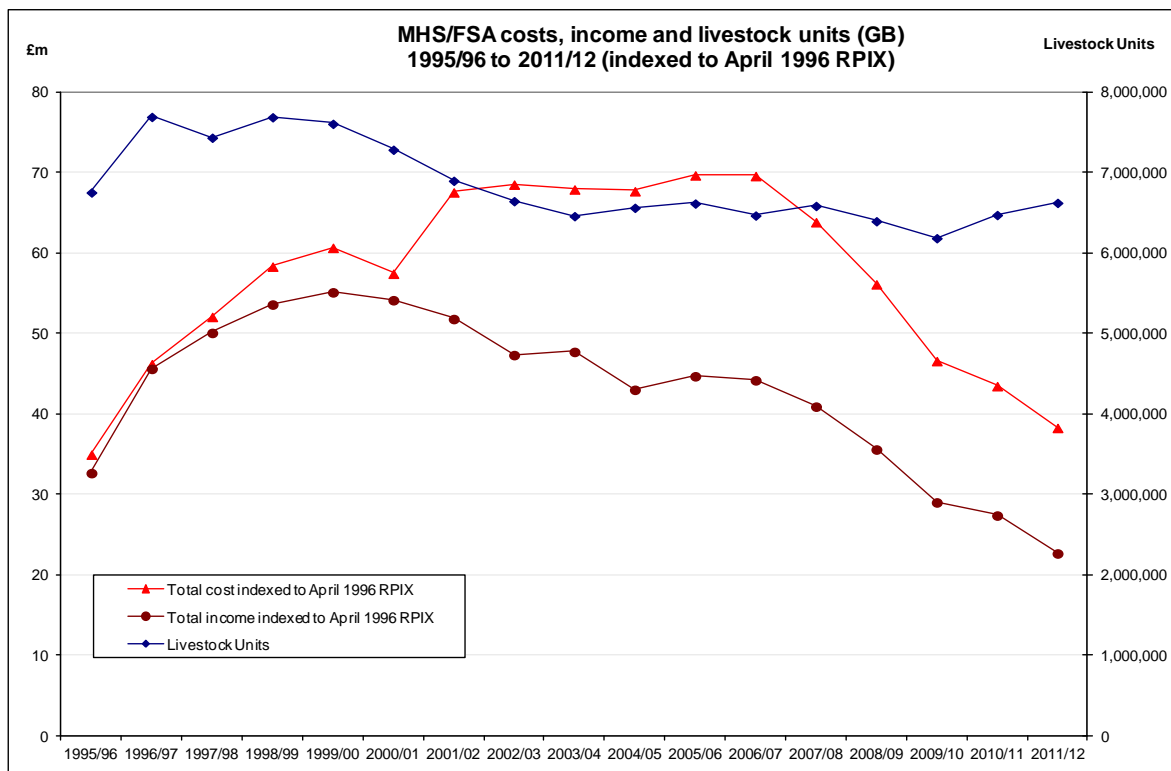
- 4.4 The current system of meat controls dates back from the late 19<sup>th</sup> century. There has been a long-standing concern that the system is based on sensorial inspection (visual, palpation and incision) and, while this was appropriate when introduced, it does not address the most significant current public health risks which arise in meat plants, which are microbiological. In July 2007 the Board agreed that the FSA should:  
*Develop and implement a strategy actively to engage with other member states, the European Commission and international partners to secure the regulatory changes necessary to adopt a more risk-based, proportionate, targeted and cost-effective approach to meat regulation.*
- 4.5 A further option within the current system is that a central competent authority may designate certain delivery responsibilities to a control body; enforcement responsibilities must remain with the competent authority. This could mean an independent organisation delivering some controls on behalf of the FSA under contract. It is anticipated by some organisations that this could be an effective way of driving down costs, through greater efficiency and the introduction of an element of contestability.
- 4.6 The control body option was considered in 2007 and 2008 but not taken forward; instead the Board opted to achieve cost reductions through a transformation of the Meat Hygiene Service. One of the principal reasons for not pursuing it was that potential providers of such a service showed no appetite for developing proposals for a pilot.
- 4.7 The control body option was revisited again in 2011 when Defra's Farming Regulation Task Force, chaired by Richard Macdonald, proposed that a group should be set up to consider the criteria for accepting the provision of meat inspection services by third parties for consistently competent businesses.
- 4.8 The Board considered this proposal in September 2011 and agreed that the FSA would invite industry to initiate and fund the development of options for alternative delivery models for consistently competent businesses. The FSA would provide support prior to options being presented to the FSA Board. A specific suggestion from the Task Force that a joint industry/Government group with an independent Chair should lead on this was rejected by the Board in July 2011.

## Section 2 – Costs and charges

- 4.9 Under EC legislation the FSA is required to charge for the cost of delivering certain meat official controls in meat plants. Under current domestic legislation across the UK businesses cannot be charged less than the EU minima, which is a charge per animal set in Euros, or more than the full cost of delivering the service.

4.10 The charging system in place in the UK from 2001 to 2009 was based on a comparison between the species rates based on the EU minima rates for each animal slaughtered and the cost of delivering official controls. Plants paid either the charge based on the species rates, or the time charges based on the costs of the vets and meat inspectors, whichever was less. The industry time charge rates were set below full costs from 1999/2000 until 28 September 2009. This system, known as the Maclean formula, was introduced in order to protect abattoirs from the sharp increase in costs which arose from 1997 onwards. These were caused by increases in veterinary supervision levels required to achieve full time veterinary supervision in most plants as required under EU legislation and increases in charge rates.

4.11 The graph below is indexed to 1996 RPIX for comparative purposes which diminishes the visual impact of increased costs. Over the period from 2001/02 to 2006/07 time costs increased in monetary terms (while remaining flat in real terms), but the EU minimum rate per animal did not increase, and so the charge based on headage became the cheaper option for the vast majority of plants. This graph for Great Britain also demonstrates that while costs were increasing the income from charges steadily reduced in real terms. The gap between costs and income peaked at £25m in 2006/07 but while in real terms cost and charges have reduced steadily since 2006/07 there remains a substantial gap.



- 4.12 In 2007 the Board decided to move towards a time-based charging system. This was intended as an important step towards incentivising businesses to be more efficient in their use of FSA staff.
- 4.13 At the time the Board also proposed increases in charges as part of a progressive move towards industry paying the full cost of the delivery of official controls. The aim was two-fold: that the incentive of time-based charging would be enhanced with each increase in charging and that the subsidy should be progressively reduced to £10m by 2014/15. The principal area of concern about the subsidy at this time was that it diverted FSA funds from other areas which could more effectively deliver consumer protection.
- 4.14 Time-based charging was introduced in 2009 although the decision was agreed by Ministers on the condition that if a business's throughput and all other factors remained unchanged it would not pay any more than under the previous system, subject to compliance with EU minimum charging requirements. The discount they received under the Maclean formula would effectively be continued. This requirement remains in place.
- 4.15 In 2009 the Board re-examined the charging position and agreed three principles:
- 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
  - Providing the best possible protection for consumers from food risk should not be based on economic circumstances or the ability of industry to pay; and
  - The FSA should consult with industry and government stakeholders on proposals for implementing the Board's decision to recover full costs for official meat controls.
- 4.16 One potential solution to delivering the first principle was for other government departments to take on the subsidy. The FSA position is that it is not opposed to a subsidy, but that it should not be paid by the FSA; one alternative being for rural affairs departments to provide the subsidy. Discussions took place in 2010. One concern was that departments would not want financial responsibility for the subsidy without also taking on responsibility for the charging policy. Recently these discussions with the rural affairs departments have been resumed.
- 4.17 An extensive programme of engagement with stakeholders took place during 2010 and 2011, including a formal 12- week consultation and public meetings led by Board members. This preceded the Board's decision in May 2011 that full cost recovery should be introduced over a three-year period beginning in April 2012; this policy was consistent with HM Treasury guidance on the recovery of costs. The Board also agreed that support of £3.2 million would continue to be provided to certain low throughput plants (defined as plants processing up to 5,000 livestock units per year).

4.18 In May 2012 we confirmed to the Board that this proposal had not received the regulatory approvals from the coalition Government's Reducing Regulation Committee (RRC).

### **Section 3 – Current Europe-wide issues**

4.19 There are two long-term issues being taken forward in Europe which have a bearing on strategy. First there has been good progress on the move towards a more risk-based programme for controls, as outlined in paragraph 4.4.

#### EC programme to reform controls

4.20 The EC is now reviewing the meat controls and proposing moves towards a more risk-based system.

4.21 The FSA has always been clear that this would be a long-term programme which would take several years to deliver results. Good progress is being made however. For example the European Food Safety Authority published an opinion in July on poultry meat. The opinion has highlighted that traditional poultry meat inspection does not enable the detection of the most important hazards to public health (campylobacter, salmonella and ESBL/AmpC gene-carrying bacteria), and recommends improvements to the current system.

4.22 The primary aim of this programme is to deliver improved public protection targeting official inspections to tasks that address current public health hazards, which may also result in a reduction in the costs of meat hygiene controls. For this reason parts of the industry have argued that a move towards full-cost recovery should await a more risk-based system. There is no precise timescale for introducing reforms and a complex process to go through. It cannot therefore be predicted with confidence when reforms could be implemented.

4.23 A further European dimension relates to EC Regulation 882/2004 which sets the framework for the official controls which are carried out on food, feed, animal health and plants. The regulation is currently under review and one area which is up for consideration is whether there should be reform of the charging mechanisms which apply to all controls. It is recognised that the current framework, which gives considerable flexibility to member states, leaves considerable room for interpretation. One option that the EC may propose is to introduce mandatory charging at full cost for all official controls.

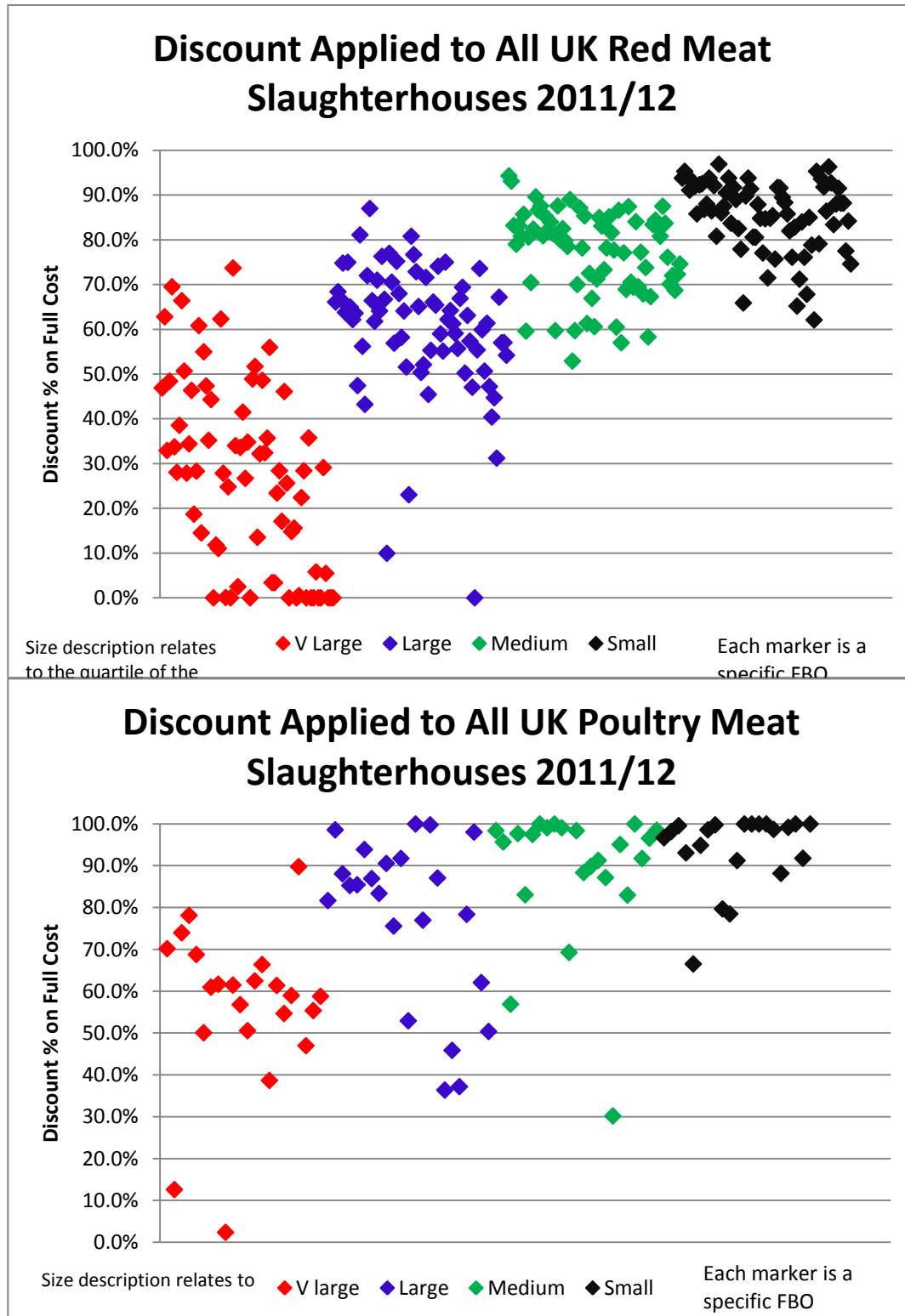
### **Section 4 – Future challenges and recommendations**

4.24 We will need to remain alive to how these Europe-wide issues develop. In both cases they may in time lead to fundamental changes. The timescales are however uncertain. The challenges which remain in the current system require more urgent attention. This section sets out proposals for three specific areas: reviewing the discount system, assessing control body options and examining the scope for further efficiencies.

### Discount System

- 4.25 The move to a time-based charging system established a system which was intended to create incentives for businesses to improve their efficiency. This has happened at the margins, where plants already paying close to full costs have a clear incentive to reduce those costs. But for the majority of plants, who receive high levels of discounts, there may be few incentives to reduce costs. This is mainly due to the businesses already paying only EU minima, due to their low throughput or their higher level of discount. This means that they are already paying the lowest amount allowed, so any reduction in demand for FSA resources would not lead to a reduced charge as that would mean the EU minima was not being paid.
- 4.26 The scatter graphs below show the distribution of discounts across the red and poultry meat slaughtering sectors banded by quartiles based on slaughtering volumes. While the distribution shows a general reduction in discount with an increase in the size of premises it also shows a high proportion of very large slaughterhouses receiving substantial discounts on charges. This reflects the distortions created by the Maclean charging system, where some premises which used FSA resources inefficiently were charged based on throughput rather than the costs of providing the official controls, even when Maclean was replaced in 2009/10 by time based charging. This is because the current discounts on charges perpetuate the Maclean system.
- 4.27 Plants of similar size may receive widely varying levels of discount. Irrespective of the level of subsidy, this system creates an un-level playing field and distorts the market. However, it would not be a simple task to reform this; without an increase in the subsidy any reform could lead to “winners” and “losers”.





Control bodies

4.28 Following the Board’s September 2011 discussion, the use of control bodies as an alternative model for delivery is being actively explored by parts of the industry. The British Meat Processors Association has engaged with the FSA over the past six months as part of its work on developing proposals for

delivery models for consistently competent businesses based on control bodies. It has recently submitted an outline proposal to the FSA. Further discussions are taking place with the executive to help the industry develop the proposal. The Association of Independent Meat Suppliers has also submitted a proposal to the Public Health Minister.

- 4.29 Previously the question of control bodies has focused on the potential for private organisations to take over responsibilities. However, control bodies do not have to be private sector organisations. The current Westminster government is supporting greater use of mutual organisations in the provision of public sector activity. The policy is particularly supportive of the development of employee-owned mutuals and a number have already been established in the healthcare sector. Meat inspection potentially provides an area for which mutualisation would be an option worth exploring. It is far too early to say definitively whether it is desirable or achievable.

### Efficiency

- 4.30 The FSA has made considerable progress in reducing the costs of delivery of meat controls over the past five years. A key part of delivering progress has been the introduction of business agreements. These specify the hours of work for which plants will require FSA staff and allow for agreement on notice periods to changes in those hours. Business agreements have been put in place for meat plants in GB and slaughter establishments in NI and have helped contribute to more efficient use of FSA and DARD staff time and hence reduced costs. The agreements are subject to regular review.
- 4.31 Nevertheless there still remains a considerable amount of unworked time, where plants have requested vets or meat inspectors to be on site, but not all of that time has been worked. Their costs are charged for even if they are not used. In total there was around £2.6m unused working time in 2011/12 in the UK. Of this 50% was charged to industry, but the discount system means that the other 50% was borne by the taxpayer.
- 4.32 A further area that delivers improved efficiency is the use of Plant Inspection Assistants (PIAs) in poultry plants. PIAs are employed by plants and are able to carry out certain controls. At present the high level of discounts means there is little financial incentive for plants to introduce PIAs.
- 4.33 A critical concern for industry historically had been the indirect costs such as operational management, IT and finance which formed part of the total charges. The merger of the former Meat Hygiene Service into the FSA has reduced overhead costs. We are also far more transparent about the basis for calculating those overhead costs. For the last two years a detailed report has been published setting out the activity-based costing model which determines the overheads.
- 4.34 When the Reducing Regulation Committee rejected the FSA's proposals for full cost recovery Committee members expressed concern that the FSA had not done enough to demonstrate that it had identified all the efficiencies that

were deliverable within the current European and domestic regulatory framework. This is against a background of similar claims from the meat industry. The FSA therefore proposes to commission an external efficiency review of UK delivery of meat official controls and support functions. This will allow a detailed examination of whether controls are being delivered as efficiently as possible within the scope of current legislation.

4.35 The Board's agreement is requested for the efficiency review to be carried out. Subject to this the executive will seek the necessary political sponsorship to have the review carried out by the National Audit Office. The FSA will ask the NAO to consult with industry stakeholders and trades unions on the efficiency review. It is expected that the review will take approximately 12 months to complete from the date of commissioning.

### Recommendations

4.36 There is a wide range of issues which need to be taken account of in setting charging policy. Given the impact of those issues on the industry it is important that we seek to build a greater degree of consensus where possible. The most effective way to address these issues would be to do so in partnership with industry bodies.

4.37 We are proposing to establish a new partnership group to pursue actions in a number of areas. The three areas of priority would be:

- A review of the current discount system making recommendations on how to reform the system to address anomalies
- Joint working to identify further ways to reduce costs while continuing to deliver effective controls (including building on the recommendations from the efficiency review)
- Exploring with stakeholders the options for giving greater responsibility to consistently competent businesses, and alternative delivery models including through the use of a control body, without negatively impacting on public health

4.38 Subject to the Board's agreement, discussions will begin with all interested stakeholders on the composition, governance and terms of reference for the group. An early task for the partnership group will be to identify a timetable for these projects. An update report will be given to the FSA Board early in 2013.

4.39 The Executive also proposes to continue discussions with other Government departments on their views on transferring the distribution of the subsidy from the FSA.

## **5 IMPACT**

5.1 This paper identifies a number of areas relating to charging where the FSA would seek to make progress. As there are no specific policy proposals in the

paper no impact assessment has been undertaken at this stage. This would need to form part of future policy development as specific proposals emerge.

## **6 CONSULTATION**

- 6.1 The issues have been discussed with a range of stakeholders, particularly from meat producers and processors, for some time. The proposed way forward will require ongoing detailed discussions with industry and other government departments. Any detailed proposals would need to be subject to formal consultation.

## **7 LEGAL IMPLICATIONS**

- 7.1 Regulation (EC) No. 882/2004 (known as the Official Food and Feed Controls Regulation or “OFFC Regulation”) requires the Competent Authority to charge food businesses for carrying out meat hygiene and welfare at slaughter official controls. The charge must not be more than the total cost of the controls and must not normally be less than the amount calculated from minimum EU charge rates. Any future proposals on charging will require the FSA to remain compliant with this Regulation.

## **8 RESOURCE IMPLICATIONS**

- 8.1 At this stage the resource implications for the FSA relate to the time of staff engaged in taking forward this work and the cost of the efficiency review.

## **9 RISK IMPLICATIONS**

- 9.1 There is a potential risk to the FSA from challenges to the current discount system on grounds of unfair competition.

## **10 DEVOLUTION IMPLICATIONS**

- 10.1 The Scottish Government recently announced its intention to establish a separate food standards body in Scotland, which would include meat inspection. If specific proposals emerge prior to the separation of meat inspection in Scotland, then particular attention will need to be given to their future application in Scotland.
- 10.2 These issues are of interest in all four countries and progress will require continued close engagement with governments and stakeholders across the UK.

## **11 CONSUMER ENGAGEMENT**

- 11.1 It has always been difficult to engage consumers in the questions around meat hygiene charging. The sums involved, while significant in the context of the businesses, are minor in their contribution to the price of meat. The FSA and the industry have always been clear that the charging issues must never impact on food safety which quite rightly has been the principal concern for

consumer organisations. We will endeavour to keep the consumer voice engaged on this issue, for example through our Consumer Advisory Panel.

## 12 SUSTAINABILITY ISSUES

12.1 As there are no specific policy proposals in the paper no sustainability assessment has been undertaken at this stage. This would need to form part of future policy development as specific proposals emerge.

## 13 CONCLUSION AND RECOMMENDATIONS

13.1 The Board is asked to:

**Note** that:

- Decisions on charging policy are affected by a range of other issues
- There is an appetite among stakeholders for greater collaboration

**Agree** that:

- The FSA's priority in relation to charging policy should remain to protect the interests of consumers
- That the FSA should pursue a more collaborative approach with stakeholders interested in these issues, working in partnership to deliver shared outcomes
- That priority should be given to building a more consensual approach to progressing three issues:
  - A review of the current discount system making recommendations on how to reform the system to address anomalies
  - Joint working to identify further ways to reduce costs while continuing to deliver effective consumer protection, building on the outcomes of an efficiency review
  - Exploring with stakeholders the options for alternative delivery models, including through the use of a control body
- An external efficiency review of the delivery of UK meat official controls and support functions should be carried out
- That discussions should continue with other Government departments on their appetite for taking on responsibility for allocating any ongoing subsidy.