Statutory Intervention in Agricultural Marketing

A New Zealand Perspective

Veronica Jacobsen, Grant M. Scobie, and Alex Duncan
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FOREWORD

The lessons of experience from early reformers can assist policy advisers committed to economy-wide reforms in the Latin American and Caribbean countries. In most of these countries, the agricultural export sector is a relatively large one as is the case in New Zealand, an early reformer in the developed world.

In this study, three economists from New Zealand examine the appropriate balance between voluntary and statutory arrangements in agricultural marketing based on the New Zealand experience. The authors examine a range of options that must be considered along with their strengths and weaknesses.

This study offers a framework which is relevant to the current debate in Latin America and the Caribbean and, within which, the special features for the justification of intervention for agricultural export markets are discussed and the most appropriate steps considered.

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ABSTRACT

This study examines the options which are available to countries already committed to economy-wide reforms, regarding post-reform institutional set-up for agricultural exports.

This study examines the appropriate balance regarding exports between voluntary and statutory arrangements in agricultural marketing. The authors examine a range of options that must be considered along with their strengths and weaknesses.
PREFACE

As a pioneer of structural reforms (initiated in 1985) and a country heavily dependent on agricultural exports, New Zealand's reform program attracts increasing attention among Latin America's policy makers. A critical issue during the early phase of reform is the type of institutional set-up to be adopted by agricultural exports. In some countries such as Chile, agricultural exports have been privatized without quality control beyond mandatory sanitary and phytosanitary requirements.

Statutory marketing arrangements have a long history in New Zealand. State regulation in marketing ended as part of the reforms but producer controlled marketing boards for major exports were unaffected. Agricultural exports account for more than 70 percent of New Zealand's total merchandise exports. Of these, more than one half are influenced by statutory powers, backed by legislation. Though largely independent of government, these boards have statutory powers covering the acquisition, sale, processing and pricing of major agricultural export commodities.

To many observers in New Zealand, these statutory powers are an anachronism in a deregulated climate; to others, they represent an important institution in a distorted world food market. In this study on statutory intervention in agricultural marketing for New Zealand, Jacobsen, Scobie, and Duncan examine the principal approaches and options for statutory intervention.

The experience of New Zealand and the options analyzed by the authors offers a framework for the current debate on the regulation of agricultural marketing for exports in Latin America.

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### EXECUTIVE SUMMARY

The statutory powers of the boards were conferred long in the past. The New Zealand Meat Producers Board was established in 1922 in response to the collapse of marketing arrangements established during World War I. The New Zealand Wool Board was established in 1944. Many of the powers of the boards have not been used over recent years.

Since then, the boards’ roles have changed... The boards’ roles have changed in response to market and domestic pressure. At various times in its history until the 1980s the Meat Board directly controlled all or a part of meat exports. The Wool Board withdrew from supporting wool prices in the early 1990s.

but many of their wide statutory powers remain. Powers of the boards include the power to acquire meat and wool, to control the form, destination and prices of exported product, and to regulate the shipping and distribution of exports. Some of these powers can only be exercised after certain conditions are met and after regulations are implemented. The passage of time has seen an increasing gulf between the statutory powers of the boards and their current roles. The boards themselves see their future roles involving little use of the "big stick" statutory powers with which they were conferred at their inception.

The boards are funded directly by levies on growers The boards are funded through levies on all owners of stock at the time of slaughter and all owners of wool at the time of sale. The Wool Board levy is 6% of the sales value of wool. The Meat Board levy is $0.47 per lamb, sheep or goat, $0.24 per calf and $4.20 per cow, vealer or other adult cattle.
....which are very substantial.

Each year meat and wool producers spend directly and indirectly $69 million on the purchase of a wide variety of services provided by the Meat and Wool boards. In 1991/92, this money raised from compulsory levies represented an estimated 11% of total farm profits from sheep and beef farms.

In effect, producers are purchasers.

While it may not be immediately apparent, producers in effect acquire services or undertake investments through the levies they pay. These include marketing services provided by the boards, such as domestic and international promotion, transport coordination, grading and quality control, market development and provision of economic information.

Producers make these purchasing decisions every day

Producers are constantly assessing the quality and appropriateness of the services that they buy, such as banking and accountancy services. The choices they have open to them provide them with the power to make providers accountable. If they receive inadequate services they can go elsewhere.

....but in this case they have little discretion.

Producers cannot directly register their approval or disapproval of board activities through their purchasing decisions of services they buy from the boards since levies are compulsory. They cannot opt out. Nor can they choose among alternative suppliers.

Is this the best arrangement?

What is special about the services currently provided by the boards which justifies producers being compelled to fund them? This is the key focus of this review.
Generally, what justifies having statutory power?

There are generally accepted guidelines which indicate when the use of statutory power is appropriate. Government intervention may be helpful to safeguard basic rights, reduce the costs of commercial transactions by setting "rules of the game", reduce impediments to competition and foster the provision of goods and services which would be otherwise insufficiently provided. The aim should be to have the minimum amount of regulation that is necessary to achieve maximum producer profitability and benefits to New Zealand. The increasing complexity of markets and the greater information known to individual producers and traders means that reliance on voluntary transactions, without interference, is generally better than trying to regulate trade.

There are two broad types of statutory power.

The two types of statutory power are "prescriptive" industry-specific rules and "enabling" generic statutory powers. "Prescriptive" powers can be exercised without the mandate of producers (they do not require, for example, producer referendums). The Meat Export Control Act and the Wool Industry Act are examples of this. The initiative for setting or amending powers rests in the political process, in particular the Minister of Agriculture. The "enabling" approach provides statutory powers which are available to producers but which are not confined solely to the meat and wool sectors. Such powers might be contained in the Companies Act or the Commodity Levies Act. These powers help people with common interests to come together to provide services without the need for specific legislation.

What are the activities of the boards?

The boards provide a range of services. These vary among Boards and include market coordination, administering rules which place restrictions on exports, assisting in trade
Which of these activities justify statutory power?

Attempts to regulate exports, for example by setting minimum prices or restricting access to export markets, are likely to be counter-productive and are difficult to administer. They blunt incentives for enterprise and innovation. At worst, they may simply deliver export markets into the hands of our foreign competitors. Areas where it may be beneficial for producers to collectively fund activities are in trade representation, some aspects of promotion, and research and development.

These activities do not require industry-specific prescriptive legislation such as that under which the Meat and the Wool boards are constituted. The only exception would be for legislation to govern the allocation of export rights to markets restricted by quota. This could be administered by a special purpose agency or by a government ministry.

Statutory powers to raise levies to fund commercial investments by the boards are not warranted. There can be no justification for compelling producers to make investments where they would otherwise not choose to invest.

If it is justified, should we have it?

In many cases, the benefits of government action will not exceed the costs of not intervening and no action is justified. Sometimes, interventions can make matters worse. For example, funding generic promotion or research through levies may "crowd out" activities which would otherwise have been undertaken by the private sector. It may also block the development of "brands" and "quality marks" which may be of longer-term benefit to producers.

What are the options?

There are four broad options which span the range from the status quo through to the use of negotiation, administering classification/grading standards, undertaking investments, funding research and undertaking promotion.
generic legislation (i.e., no legislation specific to the meat and wool sectors with the exception of that dealing with export rights to restricted markets).

**Option A: Prescriptive**
**Legislation: Statutory Marketing Boards**

The existing system could be retained. The governing statutes of the boards represent a "prescriptive" approach to statutory intervention.

**Option B: Prescriptive**
**Legislation: Statutory Marketing Boards with Limited Powers**

The boards could be retained in their present form but the range of their (mainly unexercised) powers would be reduced. This is the approach that the Wool Board itself has recommended. The "prescriptive" approach to statutory powers would be retained under this option. The commercial investments of the boards would be sold outright or "spun off" by allocating shares directly to producers.

**Option C: Enabling Legislation:**
**Producer-Initiated Boards.**

Under this option, legislation would provide for the boards, or broadly equivalent organisations, to be preserved but with much reduced powers. However, referendums of producers would be held periodically to decide whether, and in what form, the boards would be retained and the amount of the levies. The referendums would be similar to those conducted under the Commodity Levies Act. Since the existence of the boards would depend on majority producer support, this represents an "enabling" approach to statutory intervention.

**Option D: Enabling Legislation:**
**Producer-Controlled Industry Organisations.**

Under this option, specific legislation relating to the boards would be repealed. If producers wished the organisations (or their functions) to continue, they could either be funded voluntarily, or the provisions of the Commodity Levies Act could apply. A structure similar to that envisaged under Option C would be possible, for example an entity which undertakes a range of functions related to the meat or wool sectors. Alternatively, separate entities could undertake discrete functions.
Conclusions relating to the need for statutory powers are summarised in the following table.
Table 10.2: Statutory Implications for Agricultural Marketing

<table>
<thead>
<tr>
<th>Activity</th>
<th>Need for Statutory Power</th>
<th>Comment</th>
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<tbody>
<tr>
<td></td>
<td>Prescriptive Legislation</td>
<td>Enabling Legislation</td>
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<td>Perhaps</td>
</tr>
<tr>
<td>Commercial Activities</td>
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<td>Yes</td>
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Source: Jacobsen, Scobie, and Duncan (1995)
1. INTRODUCTION

Background

Statutory marketing arrangements have a long history. The marketing of a major share of New Zealand's exports is conducted within a regulatory structure that has been in place for much of this century. Agricultural exports account for more than 70 percent of New Zealand's total merchandise exports. Of these more than one half are influenced by statutory powers. The Dairy Industry Act 1892 signalled the first of what was to become a series of statutes which eventually covered most of New Zealand's agricultural exports. The Meat Export Control Act 1921-22, the Fruit Control Act 1926, and the creation of the Wool Board in 1944 followed. Each had varying powers but all were backed by legislation. The creation of the Kiwifruit Authority in 1977 continued the established pattern, extending it to non-traditional exports.

Almost without exception the creation of marketing agencies was spawned by depressed prices. Little if any analysis was undertaken of the underlying causes, nor was any consideration given to a range of policy responses, which might have led arguably to an assessment of the alternatives. Producers, dissatisfied with the returns they were receiving, felt typically that either international prices were inequitable, or that their share of the world price was unjustly low. In either event, a producer controlled statutory marketing authority was seen as the appropriate response.

If prices on world markets were too low, then it was argued that collective action by producers would provide countervailing market power which would allow them to extract greater returns. If on the other hand, the depressed returns to growers were a consequence of inefficiency or exploitation by those marketing or processing the products, then grower control of these functions was seen as a way to avoid the excessive costs imposed by "middle-men".

Current Economic Climate

The passage of time has seen an increasing gulf between the statutory powers of the boards and their current roles. The circumstances prevailing at the time the Meat and Wool boards were created have radically changed. The Meat Board was established in 1922 when lamb prices in the United Kingdom collapsed following the termination of bulk purchase arrangements instituted for the years of World War I. The Wool Board was established in 1944 when the British Government had an agreement with New Zealand to buy the export clip for the duration of the war, and one season afterwards.

During the last decade, the domestic policy environment has changed dramatically with reforms which are likely to remain in place. In particular, changes over the last ten years in domestic policy have reflected a changing view of the role for government and improvements in the way the government carries out its functions. This shift in focus is important in a review of agricultural marketing organisations because it determines what they can expect from government. Recent reforms to the structure of government also provide models of alternative institutional forms.
The principal goals of the reforms were improving the efficiency of the economy and raising the sustainable growth rate. During the 1970s, New Zealand underwent increasingly ad hoc and restrictive interventions with devaluation, inflation, stabilisation attempts and unfortunate public investments. Growing overseas debt and poor economic performance led to greater awareness of the structural problems facing the government. At the same time the liberalisation experience of other western economies such as Britain and Chile signalled the direction of possible changes.

Economic liberalisation was aimed at reducing and simplifying the range of government interventions in the economy through the deregulation of financial, goods and labour markets, the attainment of low inflation and the reform of government trading activities.

Macroeconomic reform included floating the exchange rate, tight monetary policy to control inflation together with a broadening of the tax base and flattening of tax rates. Trade policy reform involved the abolition of import licensing and tariff reduction to shift the economy from import-substitution. Factor markets were freed through deregulation of the financial sector and labour markets, and reforms in energy, transport and research and development. Reforms of product markets included the removal of price supports for agricultural products and exports. Government activities were split into policy advice, provision of services and regulation. Government trading organisations were reorganised into market-driven corporations some of which were sold.

The benefits of the turbulent decade are now beginning to be felt. Inflation is low and growth rates positive. The government has abandoned a wide range of policies that favoured the few at the expense of the many. It no longer directs public monies to subsidise inefficient organisations. There is a reluctance to attempt to pick winners, or to plan and control the use of resources. Rather, the emphasis of government policy has been to provide an environment which encourages competitive markets to flourish and government enterprises to become more efficient. Given the undoubted efficiency gains, government is likely to be reluctant to reverse these policies.

Agricultural marketing organisations, established under statute, have enjoyed a long period in which they have had sole rights to serve the interests of producers. The activities of these organisations included the compulsory acquisition of product, negotiation with shipping companies, price stabilisation and export marketing. Changes in the domestic environment, such as the liberalisation of ports and shipping, suggest that it is timely to review the structures and statutory roles of producer boards which emerged from an earlier time.

Attempts to reform the boards which are currently under way in New Zealand have met with limited success. Some decisive political moves by the Labour Administration in the late 1980s, did result in the deregulation of the town milk, eggs, wheat and flour sectors (Sandrey, 1990). It is of interest that all of these were non-traded or importable goods. Progress is proving much harder for the major export industries. Reforms face "the inherent conflict between the pursuit of economic efficiency and the domination of the boards by producer representatives, who will inevitably be preoccupied by short-term political agendas as they seek to placate their constituents in farm organisations and keep peace with politicians on whose favours their powers depend" (Watson, 1990, p.9).
The persistence of inefficient statutory power can only be explained as a reflection of gains to special interests. However, the new domestic and international operating environment will increase the costs of intervention over time, and make them ever more obvious. There are several sources of pressure that signal change. Potential entrants, such as Applefields, seek to compete with statutory authorities. Producers appear to be increasingly disillusioned with the performance of the boards. A lobby group, Farmers for Change, have sought changes to the electoral procedures for grower representatives, in an attempt to enhance accountability. Meanwhile, growers of fine wool have been attempting to have the Wool Board reflect more of their interests. Consumers who have benefited from the freeing up of the domestic apple market and the town milk supply are increasingly aware of the benefits of deregulation.

New Zealand is not alone in this quest. Australia and other countries have undertaken reviews of traditional marketing arrangements for primary products. The Industry Commission in Australia has recently completed a review of the Australian meat industry. There have been increasing calls in Australia for a wholesale deregulation of the sector.

The Key Issue

The key issue to be addressed is the appropriate balance between voluntary and statutory arrangements in agricultural marketing. In considering the appropriate institutional arrangements, a range of options must be considered, and the strengths and weaknesses of each identified.

The regulatory structures that derive from the statutory powers affect the way in which resources are used, not solely within the agricultural sector, but throughout the economy more broadly. The effect of these powers is to create a regulatory environment which restricts choice, limits competition, creates barriers to entry, encourages wasteful rent seeking and generates signals that distort the way scarce resources are allocated (ACIL, 1992; Finlayson, 1993). Likewise, the incidence of the costs and benefits generated by the application of statutory power extends well beyond the farm gate. As a consequence there is a broad spectrum of stakeholders in the performance of agricultural marketing.

Three essential issues emerge in the debate about the regulation of statutory marketing:

- What are the special features of the export markets for New Zealand’s agricultural products that justify the need for intervention?
- Given that a case is established for some type of intervention, what form might it best take?
- Are the existing functions of the producer boards consistent with the optimal form of intervention?

The following considerations arise in addressing this issue:

- Producers purchase a wide range of services in conducting their businesses. These include marketing services provided by the boards which producers are compelled to
acquire by virtue of the levies they pay. Some or all of the services provided by the boards are, or could be, provided by the private sector.

- The complexity of most markets means that arrangements which allow market participants to pursue their respective interests in the light of the information they have are, in general, likely to be superior to intervention.
- The onus is on the proponents of statutory powers to establish the case for intervention. The case for intervention must be constantly reviewed in the light of changing circumstances.
- The overriding goal is to find the minimum amount of regulation necessary to achieve maximum efficiency in the meat and wool sectors and to ensure maximum profitability to producers.

The focus of the report is forward looking and general. It seeks lessons from the past and current agricultural marketing arrangements in New Zealand to draw a generalised framework for addressing the design and implementation of appropriate institutional arrangements in agricultural marketing in the future.

Outline of the Report

This report develops a framework for public policy on defining an appropriate structure for institutional arrangement for agricultural marketing. It draws on the New Zealand experience, in particular on the meat and wool sectors, which are currently undergoing institutional changes and where the debate is most intense.

Chapter 2 discusses the grounds for intervention in agricultural marketing and the range of statutory powers which can be called upon. Alternative institutional arrangements for core areas of statutory power are considered in subsequent chapters: market development (Chapter 3), market access (Chapter 4), promotion (Chapter 5), quality assurance and standards (Chapter 6), research and development (Chapter 7), education and training (Chapter 8) and commercial activities (Chapter 9). Chapter 10 concludes the report with a consideration of possible options for regimes of statutory intervention in agricultural marketing.
2. GROUNDS FOR INTERVENTION

Areas of Statutory Intervention in Agricultural Marketing

At the heart this report is an assessment of whether there are special circumstances which warrant continuing government intervention through legislation and regulation. The boards have a wide range of statutory powers. Many of them are no longer utilised, such as the power of the Meat Board to acquire meat, the power of the Wool Board to stabilise prices and the power to regulate shipping arrangements for exports. The main areas where statutory powers are still exercised in the meat and wool industries are:

- **Market development.** Powers of the boards to licence exporters and to set conditions on those licences represent interventions promoted to encourage market development, for example, by preventing so-called "weak selling".
- **Market access.** The most important issue here is the allocation of entitlements to ship exports to markets which are limited by import quota restrictions. While these restrictions arise due to multilateral trading arrangements, they are enforced through powers conferred on the boards to both grant licences and to impose restrictions on their exercise.
- **Promotion.** Funds raised through compulsory levies are devoted to promoting agricultural exports. Some would argue that adequate promotion might not occur in the absence of the powers of the boards to raise levies.
- **Standards, grades and quality assurance.** The boards exercise various powers to set standards and grades for agricultural products.
- **Research and development.** Funds raised through levies are used to fund research and development.
- **Education and training.** As with promotion and research, education and training is either funded or provided by the boards from the levies they raise.
- **Commercial activities of the boards.** The commercial investments of the boards are backed either directly or indirectly by resources procured because of their statutory powers. These resources might include levies, income generated from activities which, in turn, were funded from levies or government subsidies paid in the past.

The central role of the government in relation to the production, sale and distribution of agricultural products is to establish a regulatory framework which encourages individuals and firms to take decisions that will maximise their overall profitability. This role for government is no different than for any other economic activity. The key issue is to define the rules that are the most likely to facilitate the achievement of this objective. One aspect of this is to examine whether statutory intervention is likely to promote the objective of ensuring the maximum return from agricultural production. The criteria for assessing alternative institutional arrangements are whether they:

- facilitate or hinder agricultural exports;
- allow the exploitation of market opportunities;
• facilitate or stifle the growth, development and efficiency of the industry; and
• facilitate or hamper commercial decision making.

General Grounds for Intervention through Statutory Powers

The generally accepted economic grounds why interventions by government are necessary to ensure that community welfare is maximised are listed below.

Reducing Transaction Costs

In order to transact with each other, individuals and firms must bargain, define in a contract what is being transacted and monitor and enforce the contract. This involves costs which are known as "transaction costs".

An important role of government is to provide an environment in which the costs of transacting are kept as low as possible. Ways in which this is achieved include the definition and enforcement of property rights, procedures which enable the enforcement of contracts, and rules against theft and violence. These protections encourage individuals to invest knowing that they will be able to benefit later on and that promises to exchange will be kept.

Without an adequate system for the definition and protection of property rights, individuals can use resources without paying for them and the resource will be over-exploited, reducing the amount available for others. Property rights, in this context, are broader than bricks and mortar or the rights to land. The features of property rights include:

• the extent to which the owner alone may decide on the use of the resource;
• the rights of the owner to extract income from using the resource; and
• the authority, if any, of the owner to transfer or sell the rights to the property or resource.

An example of a property right in the meat sector is the right to export meat to markets with import quotas. The quota entitlement of any one exporter/processor represents a property right. Another example of property rights relating to the export of agricultural products, is the right of an exporter to sell where he or she chooses. To the extent that regulations limit these choices in terms of how, where and in what form to sell the product, property rights are constrained.

The more precisely property rights are defined, the less the uncertainty faced by the owner, and the lower the transaction costs of determining how the resource may be used. Statutes and regulations are important for defining property rights and setting procedures for modifying or transferring property rights through voluntary transactions.

There are weaknesses in the existing property-rights system for agricultural exports. The rights of exporters to decide how, where and when to market their product are constrained and may be uncertain, particularly if new regulations may alter those rights (for example, by opening up or closing a market
The way in which property rights for exporting meat to quota markets are defined and allocated may also mean that potential benefits to New Zealand are reduced. Market development and market access are discussed later in this report.

**Funding the Provision of Public Goods**

Incentives for individual firms to supply goods will be reduced where:

- it is difficult to exclude non-payers from the enjoyment of the benefits of the goods or services; and
- the extra cost (and therefore the price) of providing such goods or services is very low or zero. In a narrow sense, the cost of providing street lighting for the extra passer-by could be zero. The extra cost of providing wool promotion for one more grower could likewise be zero.

Goods which exhibit both these features are referred to as "public goods". Such goods are rare, if not non-existent, although many goods exhibit some of their features, such as street lighting and some aspects of research and development. If left to the private market, not enough of these goods would be supplied. In many cases, the benefits of government action will not exceed the costs involved and no action is justified. In other cases, government intervention might be justified.

Research and development, and promotion expenditure are the most commonly cited examples in the agricultural sector of services which have some of the elements of a "public good". In particular, there is the difficulty of excluding non-payers from the enjoyment of services funded by payers. Against this, however:

- there are effective mechanisms to exclude non-payers from the benefits of promotional expenditure. Examples include the development of brands and trade or quality marks. These represent property rights which are given statutory protection through trade-marks and patents. Rules protecting brands or trade-marks enable the person who invests in promotion or quality improvement linked to a brand or quality standard to capture most (if not all) of the benefits of that expenditure. Non-payers do not derive any benefit since they are denied to use of the brand or quality mark; and
- interventions could prevent the development of alternative mechanisms which may be more effective in the longer-term. The imposition of levies to fund generic promotion or research, for example, may reduce opportunities for brand development.

**Internalising Externalities**

Another reason why goods or services may be under-provided is that the acquisition of a good by one consumer may give rise to wider benefits to other consumers or to the wider community. An example is basic education, such as literacy. These benefits are known as "externalities" or "spillovers". Since the benefits are not confined to the consumer, he or she may "under-invest" and the wider community may forgo benefits. Accordingly, in the case of positive spillovers, subsidies might be called for (or taxes in the case of negative spillovers, such as pollution).
Generally for goods and services such as meat, wool and marketing services, the level of externalities, if any, does not warrant government intervention. Even in markets where externalities might exist (such as in the provision of computer communication networks) competing firms often cooperate by standardising technologies or protocols without any government intervention (an example was the sharing of the technology of “compact disks” by its developers).

**Promoting Competition**

Consumers lose from a lack of competition because:

- firms can charge consumers high prices without fear of losing their custom; and
- at the same time, firms are not under competitive pressure to provide goods and services of high quality, to produce new and innovative products or to develop lower cost production technology.

Natural monopolies occur when it is too costly for new entrants to enter the market, given the state of technology. One example of a natural monopoly is the network of telephone lines. However, profits in the telecommunication industry promote the search for new technologies such as cellular networks which can allow competition. A monopolist will behave as if there were actual competition whenever there exists the possibility that another firm will enter the market. As a result, it is vital that there should be no artificial barriers facing new firms, or limiting their access to particular markets.

A justification for past interventions in the agricultural sector has been that restricting competition among New Zealand exporters would increase returns to New Zealand because a monopolist is able to extract higher returns from overseas consumers. In a sense, this turns the traditional argument for government intervention on its head: instead of intervention being required to prevent a natural monopoly from developing, intervention is advocated to create such a monopoly. The rationale is that individual companies would be reluctant to invest in market development if they thought other firms could later capture their markets without incurring costs of market development. Monopoly status for certain exporters is therefore argued as being necessary.

Whether it is possible to duplicate the conditions required for a monopolist to exercise market power in an export market depends critically on:

- how costly it is for new entrants, such as foreign competitors, to enter the market, given the state of technology. Other countries are not bound by restrictions imposed by New Zealand, when they trade the same type of meat or its substitutes. By controlling activities of New Zealand exporters in foreign markets, interventions may in fact deliver markets to third countries and inhibit the development of marketing expertise among New Zealand exporters; and
- how readily consumers can choose cheaper substitutes. As noted above, in the telecommunications sector, even though it is costly for new entrants to set up a competing local network, there are potential substitutes such as mobile phone networks. These substitutes limit the ability of the monopoly supplier of the telephone network to exploit its position.
The situation in export markets for New Zealand's agricultural products means that it is unlikely that both of the above conditions can be met for anything other than a short period of time. This severely limits the ability of single sellers to influence underlying prices, as Australian wool growers found to their cost with the collapse of their reserve price scheme.

Restrictions on access to export markets limit the ability of New Zealand growers or exporters to choose from whom they will purchase marketing services. This is likely to reduce commercial incentives for the supplier to be enterprising and innovative.

A special case might exist where a single purchaser exists in an export market. The single purchaser may be in a position to “play off” many sellers, arguably to the detriment of New Zealand. Even here, intervention may do little to increase underlying prices if the single foreign purchaser can source product from a competing supplier or there is a ready substitute for agricultural products supplied by New Zealand exporters.

Incomplete or Unstable Markets

Intervention might be appropriate if certain markets are unable to operate well because of high information costs. This problem is referred to as “incomplete markets”. For example, the high cost of establishing whether a person is truthfully revealing information about his or her health status may impede the market for health insurance.

Another ground for intervention which has been applied to the meat industry in particular is the need to address the shortcoming of an "empty core" market (Telser, 1994). The conditions for an "empty core" market to exist are high fixed costs, economies of scale, and variable supply. Variable supply requires standby capacity to be available before actual demand is known.

In these conditions, it may be best for a "grand coalition" to exist among competing suppliers so that capacity can be optimally matched with demand and overall efficiency maximised. This might require, for example, agreement among processors to a configuration of meat processing plants of different sizes to take advantage of scale economies and to handle seasonal demands for processing capacity. However, with competition, the coalition is not possible and the result is an unstable market in which all processing firms suffer losses. The stock "procurement war" among meat processors is seen as evidence of this phenomenon.

The severity of the empty core problem depends on the number of firms in the “optimal” industry configuration under the “grand coalition”. The greater the number of firms, the smaller the problem. A general method of resolving an empty core market could be to impose upper bounds on the quantities that may be sold by certain sellers. An example would be to set a maximum killing quota for sheep and beef. Given the complexity of the meat processing industry and meat markets, such controls would be difficult to set. The regulator is as likely (if not more likely) to get it as wrong as the unregulated market. Regulatory intervention is therefore likely to impose related costs that are worse than the original problem. Some of the wider impacts of regulation are discussed later in this chapter.
There are ways of resolving the empty core market without regulation, such as:

- "loyalty rebates" which were once typical of the meat industry, and are also typical of conference shipping lines where the conditions for empty core markets can also exist;
- the negotiation of long-term forward contracts. Forward contracts work better when each party (the producer and the processor) have diverging interests other than the product involved in the particular exchange;
- vertical integration, where the producers own the processor. To work effectively, vertical integration entails closer relations between the two parties and usually needs agreement about many aspects of their operations. Vertical integration works best when the producers and processors have a number of common interests; and
- the establishment of joint ventures and other cooperative arrangements among suppliers. Such arrangements often arise in other industries where conditions for empty core markets might exist, such as airlines, shipping companies and railroads.

These alternative arrangements have been allowed to develop in other activities where some or all of the conditions for the development of "empty core" markets exist. It is important that statutory interventions do not impede the development of these alternative arrangements in the meat processing sector. Seeking to impose another layer of regulation to mitigate the effects of perceived empty core markets will intensify problems. The incentives for all participants of an industry to seek durable market-based solutions are greatly reduced if there is always the prospect that investors will be compensated with taxpayers' money or protected through regulation.

International Obligations

Another reason why the government may need to intervene is because of obligations imposed by other importing countries. Obvious examples include hygiene certification requirements and the administration of trade access rules.

Wider Impacts of Intervention

Where intervention is warranted, it may be best achieved through the modification of property rights, regulation or the provision of taxes (including levies) or subsidies. In other cases it may be best for the government to do nothing about the problem. This applies where the benefits of any government action would be smaller than any costs involved if no action were taken.

In deciding whether there could be a case made for intervention on any of the grounds cited above, the impact of regulations on the broader competitive environment in the industry sector should be taken into account.

The adverse effects of commercial activities previously undertaken directly by the boards, such as direct intervention to support minimum prices, are generally recognised. Commercial investments in subsidiary companies and the exercise of powers by the boards can affect the competitive environment.
The role and activities of boards cannot be divorced from their statutory powers. Boards are funded by way of compulsory levies and have other powers, such as the compulsory acquisition of product, the power to set conditions on export licences (such as minimum export prices), and to impose grading or certification requirements. These powers mean that involvement by the boards in certain activities, such as commercial enterprises, may have wider impacts, for example on the willingness of other investors to commit resources to the sector.

Crowding Out New Entrants

The boards' activities may "crowd out" potential investors. The activities of the boards in funding promotion, investing in commercial enterprises, undertaking research or in setting quality standards may displace activities that would otherwise have been funded by private companies. If the boards undertake these activities less efficiently than those other parties, or their activities impede competition or reduce incentives for enterprise and innovation, producers are the losers. On the other hand, involvement by boards may, in certain circumstances, enhance the quality or amount of provision of certain key services, such as promotion or research.

Stifling Development

The boards' activities and powers may impede development. The complexity of the marketing systems for agricultural products combined with the continual changes in world markets, means that each agricultural sector must remain responsive to market developments. Regulatory powers may impede the flow of information that normally passes from markets to producers. If regulatory powers reduce the rewards from seeking out market opportunities or lessen the sanctions for poor marketing performance, they reduce incentives for market players to seek out that information or invest in market opportunities. If central decision-makers have access to less information than the diverse range of importers, exporters and producers in the market, producers are again the losers.

Deferring Restructuring

Board activities may defer necessary restructuring. Several boards have invested in private companies that were experiencing commercial difficulties. These investments are likely to have deferred necessary restructuring in those sectors by retaining capacity which otherwise might have been retired. An example was the involvement of the Meat Board in supporting Waitaki International Ltd when it was facing financial difficulties in the late 1980s. In late 1987, the Board through its subsidiary Freesia Investments invested $41 million in Waitaki International. In 1989, Freesia was forced to write down the value of this investment by $34 million due to losses Waikato incurred. Freesia then invested another $25 million in a separate investment company to finance Waitaki's trading stock.

Arguably, the major beneficiaries of Freesia's investments were Waikato's two principal shareholders at the time, Goodman Fielder Wattie and Fletcher Challenge Ltd. The investments by Freesia resulted in levy payers incurring significant losses and deferred necessary rationalisation of the processing industry. Such examples make it difficult to argue that the Meat Board was acting at the time in the interests of producers.
Impeding the Flow of Information

Powers granted to the boards may reduce the willingness of other players to share information. Boards typically play a facilitative role in encouraging the development of their industries. In particular, the boards play a role in reducing the costs of information to various players in the industry, including producers and exporters. However, powers granted to the boards which enable them to impose controls or pursue commercial activities, for example, may make others less willing to share information and cooperate with the boards.

Some would argue that the powers and activities of the boards, such as their promotional activities and grading standards, have helped give New Zealand agricultural exports a positive image in foreign markets. It is difficult to assess, however, what would have happened if the boards had not undertaken those activities, or not had those powers. This is a difficulty faced both by those whose inclination is to defend existing arrangements as well as those who seek new arrangements.

The perceptions of other players in the market are crucial in determining how those players will respond. The boards, for example, may choose not to exercise certain powers they have. Nonetheless, the potential for those powers to be used at some time in the future may affect the attitude of investors or traders. Likewise, the boards may be scrupulous in ensuring that their dealings with companies in which they have commercial interests are kept at "arms' length". But it is the risk that the boards may favour their subsidiaries, that may affect investor attitudes.

The Range of Statutory Powers

There are two principal types of statutory powers that can be conferred on the industry through legislation:

- "prescriptive" industry-specific statutory powers. These are powers which can be exercised by the boards without the mandate of producers, as embodied in the existing Meat Export Control Act and the Wool Industry Act. The initiative for setting and amending statutory powers rests in the political process, in particular the Minister of Agriculture; and
- "enabling" generic statutory powers. These are statutory powers which are available for use by firms and individuals, but which are not contained in legislation that is specific to any particular sector. These powers are enabling in that firms and individuals may voluntarily elect to form together to provide services (by forming a company under the Companies Act 1993, for example). Likewise, producers can elect to levy themselves for particular purposes for a limited, renewable period using the existing provisions of the Commodity Levies Act 1990.

The role of governing legislation differs under the heavy-handed "prescriptive" and the light-handed "enabling" approaches to statutory intervention.
"Prescriptive" Approach

The prescriptive approach to statutory powers has been reflected in industry-specific legislation. The general features of such legislation are that:

- the statute provides considerable detail as to how activities will be governed and conflicts resolved. Under this drafting approach, detailed and complex rules covering a wide range of areas are enacted either in statutes or by regulation;
- there is little room for individuals to come to agreements privately to promote coordination or resolve conflicts. This traditional approach results in relatively complex legislation and simple private arrangements;
- in order to change rules, it is necessary to seek either a statutory change or a change to regulations through the political process. This can involve delays, add further complexity to legislation and overly politicise the process of change. This makes it difficult to tailor statutory powers to continually changing circumstances;
- the legislation is normally non-reviewable. Monopoly powers are often granted to an agency (as in the case for certain powers of the Meat and Wool boards); and
- provisions are generally industry specific. This reduces flexibility and perpetuates artificial "inter-industry" demarcations.

To date, prescriptive industry-specific statutory powers have been relied upon in the dairy, kiwifruit, apple and pear and meat and wool sectors. Such specific powers may no longer be warranted. However, this does not imply that no statutory interventions are appropriate. In the absence of specific legislation, producers would have available other, more general, legislation.

"Enabling" Approach

This legislation is provided as part of the government's wider responsibilities to provide a stable framework within which voluntary transactions can take place. Under the "enabling" approach, legislation provides an overall framework within which individuals and groups have greater flexibility to develop mutually acceptable arrangements to resolve conflict or to develop and use resources. Under this approach:

- the role of the legislation is to spell out the rights and obligations of the Crown and of other people affected by legislation and, where appropriate, the processes to resolve conflict. It is not to set out detailed rules covering a wide range of activities;
- legislation tends to be simpler than the "prescriptive" approach. However, the legislation paves the way for more complex private arrangements between individuals and groups to deal with the intricacies of business activities;
- the legislation itself will rarely contain specific examples of the detailed rules or agreements which parties may enter into. These rules would be an outcome of negotiations among affected parties, such as between a producer organisation and other industry stakeholders; and
- the role and functions of organisations can alter, within limits specified by the legislation, without the governing statute itself being required to be amended. This will be increasingly
important given the difficulties that might be faced in seeking legislative changes through Parliament.

The latter approach to drafting is reflected in the Employment Contracts Act, the Companies Act 1993 and the Commodity Levies Act 1990, among others.

**The Commodity Levies Act 1990**

The Commodity Levies Act 1990 is an important and relatively new statute which represents a possible alternative to the use of prescriptive statutory power for agricultural marketing. The Commodity Levies Act involves the voluntary establishment of a compulsory levy through a referendum of producers, with a periodic review. An important provision of the Act is its presumption that voluntary funding systems can benefit an industry. The onus is thus on those who propose the imposition of compulsory levies on the whole industry to show either that voluntary funding would be impossible or impracticable or that those who did not pay under a voluntary system would derive unearned benefits.

It requires that a majority of voters and of producers who account for a majority of output support its imposition, and that "overall, the benefits to the persons who will be paying the levy...will outweigh the disadvantages to them". The compulsory levy expires after six years, but can be extended in certain circumstances. Otherwise, a new referendum to renew the levy must be held at least every six years. It also requires the organisation to have a specific system for accounting to levy payers.

The Act may be used for various purposes, including "[r]esearch relating to the commodity or commodities concerned, or in relation to any matter connected with it". The Commodity Levies Act also restricts the uses to which the levy can be put. This links the levy to the objective of maximising producer profitability. The level of the levy is determined by the producers.

**Conclusions**

Heavy reliance on statutory marketing boards in the past arose in part from an incorrect diagnosis of the economic problems confronting the certain industries. Instead of being considered in the light of valid reasons for government intervention, previous policies were based on the assumption that the actions of private marketing agents were inherently detrimental to producers. The wider impacts of intervention were also often ignored to the substantial cost of producers and taxpayers over the last 20 years.

This throws into question the longstanding reliance on statutory intervention to support or stabilise the prices of agricultural products through the producer boards in the name of orderly marketing. In reality, the boards have never had the capacity to have much influence on the stability of farm incomes and they no longer have a role in delivering assistance through price support to producers.

Accordingly, intervention by producer marketing boards must be justified primarily by the profitability to producers of the marketing activities undertaken by the boards. Are the current arrangements operating
to maximise the profitability of producers? If not, are there other institutional arrangements which might better serve producer interests? These issues are considered in the remainder of this report.

To what extent are the existing regulatory mechanisms, designed to address very different circumstances in both the domestic and international operating environments still appropriate? To answer that question one must look at the functions that the existing agencies perform. These include significant holdings in commercial ventures, R&D, promotion, quality control and the setting of standards, allocation of access rights and, to varying degrees the exercise of control over exporters. This ranges from almost complete in the case of apples and pears and dairy, to partial in the case of meat, to minimal in the wool industry.
3. MARKET DEVELOPMENT

"Weak Selling"

The case for statutory power in agricultural marketing hinges crucially on the argument of "weak selling", as a *prima facie* example of market failure. Regrettably, proponents of this argument offer little in the way of a definition, an economic analysis or evidence that it is widespread in the absence of statutory authorities.

The chairman of the NZ Apple and Pear Marketing Board did offer the following definition: "Weak selling is... when... an exporter... accepts a lower price than that which could, and should have been achieved. This action could also result in a generally lower price level being established for that product across the market" (Pope, 1988, p.39).

The concern that underlies the case for weak selling is that there exists a market premium, which will be eroded away by competing New Zealand suppliers in the absence of state imposed collusion. The fact that the observed price is low (however that might be measured) cannot of itself be taken as evidence of weak selling. It is helpful in this context to regard the market price actually paid as made up of three distinct components. The first is the underlying element of price that reflects the supply and demand conditions in the market at the time. The second is a premium for value-added through quality, packaging, delivery, credit or goodwill. Finally there may be a premium for market power; in the parlance of economics, a monopoly rent.

Unfavourable market conditions leading to a low price typically lie beyond the control of a particular seller or selling country. A lower price may well reflect the extent to which marketing services or value-adding activities are present. There is nothing intrinsically superior about attaining a higher price in this way... "price premiums clearly can be obtained from market differentiation backed up by services targeted on those markets" (Industry Commission, 1991, p.46). Whether the pursuit of such premia is justified is a commercial decision best left in the hands of individual exporters.

This leaves the third component of price as the only legitimate element of concern in the weak selling debate. It is true that if there exists some market power which might be exploited to enhance returns, then failure to restrict access can result in the dissipation of the rent by competing suppliers. Were New Zealand to be the only supplier of a particular product for which consumers had few if any substitutes, then the standard argument for an optimal tariff would apply. That tariff, or more correctly export tax, should be set so as to capture the benefits of the monopoly power. The size of the tax, whose purpose would be to restrict supplies to the export market, would be inversely proportional to the (absolute) elasticity of demand faced by New Zealand exporters.

Such evidence as there is (Scobie, 1973) regrettably indicates that New Zealand is not so blessed. But suppose for a moment that it was. In order to capture the premium for market power, that power must be exercised. Its only form of expression is through the ability of New Zealand suppliers to act as a cartel to
reduce supplies. On the presumption that New Zealand’s share is significant enough, then the world price would rise.

However such a rise can only be sustained if there are restrictions on domestic supply. No board actually operates any explicit form of supply control. They accept whatever quantity producers offer. If they are successful in extracting a premium that is passed to producers in the form of higher prices, this will elicit greater, not lesser, supplies. Attempts by the Kiwifruit Marketing Authority to restrict the export supplies through severe quality standards have arguably led to a higher per unit price for New Zealand suppliers. But that is a reflection of a quality premium (albeit one that is artificially induced), rather than the genuine exercise of market power.

Were the boards to control domestic supplies (which they do not), extraction of market premia would still require two other conditions: namely that consumers lacked substitutes and other suppliers would not respond to the higher prices induced by the New Zealand cartel. The nature of New Zealand’s agricultural exports are such that it is improbable that such conditions apply. Zwart and Moore (1990) compared prices received for a range of New Zealand exports with those received by other countries. They concluded..."the evidence...while limited, does little to support the notion that they (the Boards) have provided increased returns to New Zealand producers" (p.272). Kraft, Piggott and Wright (1991) conclude that ..."any premia which are achieved (in rice exporting) are most likely payments for the services embodied in the Australian product rather than 'pure profit' associated with monopoly power"(p.ix).

It is extremely unlikely that weak selling could persist. An exporting company which consistently engaged in weak selling would be extracting less from the market than their competitors. As a consequence, they would not be able to pay their suppliers a competitive price and would soon be forced out of business. Producers would not want to supply to exporters who consistently returned them less than competing firms could offer.

The key issues are whether "weak selling" exists, and whether statutory powers to address the problem are the most effective mechanisms available.

Options for Market Development

Option 1: Statutory Power to Restrict Market Access and Set Minimum Prices

Attempts to address "weak selling" include the use of statutory power to set minimum price guidelines and to restrict access by exporters to certain markets. However, even were it to be the case that statutory intervention was justified, there are always considerable dangers that the statutory cure will be worse than the market disease. The structure of statutory monopolies ensures that they function very differently from competitive organisations.

Controls to prevent weak selling may be in response to a mis-diagnosis of the causes of lower prices. There is limited ability for a New Zealand exporter to differentiate products such as lamb and mutton sold in carcase form from those of competitors because:
• various attributes of the product are set by regulation which apply to all such product (for example, standard grades);
• restrictions may apply to the time at which product may be shipped (and, though less so than in the past, the shipper who must be used); and
• "generic" promotion of the product to foreign buyers makes it more difficult to establish a particular brand or product identity. This reduces incentives for exporters and overseas buyers to form longer-term relationships where an exporter can secure repeat business by providing superior service.

If many of the dimensions through which sellers normally compete, such as product quality, type and delivery, are regulated, competition will be more heavily focused on pricing considerations. In contrast, consider the market for home mortgages. Home mortgages are homogeneous products. Product differentiation among competing suppliers therefore must focus on dimensions other than simply price, such as service to customers and branding. Financial de-regulation was a major stimulus to the development of these strategies. If the only basis for competition among sellers is the price, because competition on other attributes is controlled (eg. quality, delivery, and customer services), then weak selling is encouraged.

Pressure on offshore markets may also reflect the way in which quota access to restricted export markets is allocated. A consequence of existing policies is that product which cannot be sold on higher-priced quota markets is diverted to alternative markets, thereby depressing prices.

Attributing market weakness to "weak selling" and seeking to impose minimum price guidelines or restrict access merely makes problems worse. It diverts attention and energy from addressing the root causes of market weakness, such as the need to reduce impediments faced by marketers who seek to differentiate their product, or the need to reorganise the way in which quota access to restricted markets is allocated.

Controls to prevent weak selling reduce incentives for enterprise and innovation in the provision of marketing services. Advocates of the need for "market discipline" sometimes argue that an exporter will not invest in product and market development unless they are protected from another exporter entering the market and "creaming" any premium which results from the hard work and expenditure of the initial exporter. However:

• foreign competitors are not restricted from undertaking the same strategy. Restrictions on access may simply deliver foreign markets to our competitors;
• it is the threat of losing market share that provides the most effective incentive to invest in marketing effort, such as product development and providing superior service as a reputable supplier in order to attract repeat business. This is particularly important since uncertainty is an important consideration for purchasers. Accordingly, a key to successful international trade is the reputation of private companies. The wool trade, for example, relies on the reputation of the firms involved. Reliability in both specification of wool and financial dealings are key ingredients of success; and
• the threat of intervention may reduce the willingness of exporters to a particular market to coordinate their efforts where there is a commercial incentive to do so. Such voluntary
marketing efforts are not uncommon in other important New Zealand export sectors, such as fisheries products and wine. The threat of an imposed solution that may favour a competitor, however, reduces the likelihood of exporters engaging in cooperative action, which relies on some sharing of information. Of course, the lack of willingness to cooperate may then be used to justify an “imposed” solution.

Controls to prevent weak selling are difficult and costly to administer. As the Industry Commission notes, "...export licensing or single-desk selling themselves can impose costs, since they limit market entry and can prevent competitive pressures from ensuring that sales into premium markets are undertaken at least cost... Thus the objective of capturing a market power premium on export markets through controls on competitive access would only be sound if any extra costs imposed by those controls were less than the extra income obtained" (1991, p.49).

The ability to extract a premium for marketing services by imposing restrictions on prices or access to export markets is likely to be limited. Indeed, by eroding cooperative action that may otherwise occur among sellers, imposing regulatory solutions may be counter-productive.

The processes through which prices are established in markets are complex. Imposed solutions may subvert these processes and may hamper markets reaching full maturity. Innovation and enterprise in marketing may be stunted. Difficulties arise when the power of the boards to license exporters is used to control the way that trade is conducted by New Zealand firms in overseas markets, such as restricting access to markets to one or a few participants. It is unlikely that central decision-makers have access to enough information to decide appropriate marketing strategies and restricting access may reduce incentives for exporters to undertake market development.

Rules which limit the dimensions of competition among suppliers (such as standards for product quality, type, delivery and service to customers) will contribute to the problem of “weak selling”.

In short, it is likely to be difficult to promote the durable and sustainable development of markets through regulations imposed on parties because:

- the ability to extract a premium for marketing services from such measures is likely to be limited. Indeed, by eroding cooperative action that may otherwise occur among sellers, imposing regulatory solutions may be counter-productive;
- the processes through which prices are established in markets are complex. Imposed solutions may subvert these processes and may hamper markets reaching full maturity. Innovation and enterprise in marketing may be stunted; and
- rules which limit the dimensions of competition among suppliers themselves contribute to the problem of “weak selling”.

**Option 2: Marketing Firms**

Under this option, the powers of the boards to intervene in marketing through placing restrictions on market access, setting minimum prices or acquiring product would be abandoned. Otherwise, the boards
would concentrate on fulfilling a facilitative role and undertaking other functions such as promotion and trade access.

There would be complete freedom for new marketing organisations to enter the market. Giving producers a choice of marketing firms will ensure that none can afford the luxury of weak selling. The fear of losing market share will keep exporters from engaging in practices which are not in their own commercial interest. Only when competition is eliminated by restrictions on who can sell in a certain market, need producers fear a case of weak selling.

Producers, not their agents, are the best judge of whether weak selling is occurring. In the same way as they choose accounting firms, banks or contractors, they will choose providers of marketing services who best serve their interests.

New marketing approaches have to establish their merit in competition with existing systems. Some firms will prosper and others will fail. This is an important part of the market process since, in contrast to the operation of the boards, it ensures that marketing firms which do not meet the needs of their clients are replaced by those which do.

Conclusions

Producers must be viewed as purchasers of marketing services. A system of competitive marketing would give them choices and the power to sanction the performance of those who supply the services to them. Producers are well equipped to make those judgements. They make such decisions about who should supply them with banking services, accountancy or legal services, farm contracting services, vehicle repair services. They will have no more difficulty making the same business judgement about the preferred supplier of export marketing services. Industry-specific statutory powers in respect of market development are unnecessary.
4. MARKET ACCESS

Access to Export Markets

Access to overseas markets is essential for agricultural export industries. However, as virtually all the questions relating to access arise in the context of the meat market, this chapter focuses solely on meat.

There are two broad areas of concern relating to issues of market access for meats. These are to:

- ensure that NZ has the widest possible access for its exports. This is a long term issue; and
- define and allocate the rights of access to NZ exporters for those markets for which there are defined limits. This is a more immediate issue.

Currently, the powers of the Meat Board are relied upon to administer quota access. The nature of access rights and their allocation are considered in this chapter since this affects:

- the nature of the statutory powers necessary; and
- whether those powers should reside with the Meat Board.

Negotiating Market Access

The long term issue is one of continuous negotiation. New Zealand’s interests must be represented in the widest possible bilateral, regional or multi-lateral forums. The question arises as to how this might best be carried out.

At present, the Ministry of Foreign Affairs and Trade (MFAT) handles all negotiations. It is assisted by the Ministry of Agriculture and Fisheries (MAF) in some areas. The boards have an input, but it is MFAT which is responsible and does the negotiating. The rationale for this approach rests on the specialist role of international negotiating that resides with the Ministry. In addition, it could be argued that MFAT is the agency best placed to represent the totality of New Zealand interests. It can and must make difficult trade-offs between sectional interests in a way that ensures New Zealand’s overall interests are best served.

Given that MFAT does not have sufficient staff with the skills and background in the particular industries, the government could delegate the negotiating role to another agency, such as the Meat Board to act on behalf of New Zealand interests. This would ensure that those with the greatest incentive to invest in information pertinent to the negotiations would do so. However, it would have to be recognised that such delegation of authority could run the risk that the sectional interests of the meat industry might take precedence over the national interest in some circumstances. While in many situations there would not necessarily be any inherent divergence of interests, the issue is indicative of the more ubiquitous problem...
of principal and agent. It can be difficult to ensure that the agent (the boards) has the same incentives and interests as the principal (the nation).

In fact, a combination of the two would seem ideal. MFAT would act as the official representative of New Zealand. This would be consistent with the structure of GATT or the World Trade Organisation. The boards would act as the producers' agent, providing information to inform the negotiations. The critical point is that there would not seem to be any crucial implications involving statutory powers. Where appropriate, the government could presumably delegate any organisation to act as an agent in negotiations. The acceptance of this agency to other parties to the negotiations would hinge on the delegation of powers to represent New Zealand, rather than the constitutional standing of the body within New Zealand.

Allocating Access Rights

Some importing countries choose to protect their domestic producers by limiting competition from foreign suppliers. There are a whole range of trade barriers which they can erect. These include: artificial hygiene standards, tariffs, variable levies, quotas, voluntary restraints or even outright bans. As a small, open, trading nation New Zealand has no choice but to accept the world's trading environment and do the best it can given the barriers (while all the time chiselling away at the walls of protectionism through negotiation).

As an aside, the existence of the Meat Board backed by statutory powers might potentially make it easier for importing countries to impose restrictions, and therefore increase their willingness to do so. Likewise, the existence of a technically competent and efficient government-provided meat inspection service might encourage importing countries to impose increasingly stringent certification requirements as a form of non-tariff barrier. Be that as it may, however, New Zealand is confronted with import restrictions and must manage their allocation.

Two major markets (USA and EU) use various forms of barriers to limit the imports of New Zealand meat. In the USA, trade has been regulated since 1965. Since 1980 it has been controlled by the US Meat Import Law. This covers the import of beef (fresh, chilled and frozen), veal, mutton and goat meat, and some processed beef and veal. A formula allows imports to grow in line with increases in domestic production. Access is reduced whenever there is a cyclical upturn in cow beef production in the USA. The so-called Voluntary Restraint Agreements (VRAs) are negotiated with each supplying country.

For 1994, New Zealand has an access of 184,000 tons. Under the Uruguay Round outcome of the GATT, New Zealand is expected to have an access of 213,000 tons sometime in 1995. This will remain fixed for the duration of the current GATT outcome, providing greater certainty for New Zealand exporters. They would be able to ship quantities in excess of this amount, but these will attract a tariff of initially 31.6 percent. Similar arrangements apply to the EU sheepmeat market, although the out of quota tariff rate is extremely high.
What are the consequences of these VRAs? Since imports are restricted, domestic prices in the importing countries are held artificially above the world market price. World market prices are depressed as a result, because some of the supplies which can no longer obtain entry are diverted to third markets.

The high internal prices encourage domestic producers to expand their output, and some of that finishes up on world markets further depressing the already low prices. The only clear beneficiaries of such a system are the domestic producers who are protected. Domestic consumers lose, while consumers in third markets may gain from lower prices.

Exporters will have a strong incentive to supply these quota markets in order to capture the "economic rents" - that is, the extra returns which these markets offer over the next best alternative market.

These extra returns can be sizeable. In recent times, lamb carcasses have fetched as much as $6 more in the EU quota markets than elsewhere; beef in the USA market has sold for up to $1 per kg above the price in other markets. Were these premiums to apply to the estimated tonnages in 1994, the total economic rent from the combined quota markets would approach $300 million. These figures are merely indicative of the size of the premiums. They will, of course, vary from time to time according to market conditions, both inside the quota markets and in third markets.

Clearly, with sums of this magnitude at stake, there will be intense competition. Those who hope to gain will have the incentive to invest considerable resources in pursuit of access. In fact, depending on the system used to allocate the rights to quota markets, a good deal of the economic rent can be frittered away by lobbying and unproductive activities, or dissipated rather than being captured by New Zealand.

New Zealand has rightly welcomed the increase in the quotas that are expected to follow from the completion of the Uruguay Round of GATT. It might well be that over the next few years, the quota will not be filled. While it is true that this will make the question of allocating quota rights less critical, it does not remove the need for an appropriate system to define and allocate quota rights. After all, these levels are set politically, not by market forces, and can be changed on a political whim.

It is important to recognise that access rights are a scarce and valuable resource. Whenever a valuable resource exists, there has to be a clear understanding of who "owns" the rights. In the first instance they belong to the country which has decided to control access to its markets. In fact, they could easily sell them. In the case of the USA, in 1979, Congress granted the President the right to auction the import quotas. Rather than exercise that right, the USA has essentially given away a valuable resource to selected suppliers.

Given that they have been granted by the importing country, the question arises as to their "ownership" in New Zealand. There is no simple answer. Some will argue that these are rights negotiated government-to-government and they must therefore be regarded as belonging to society as a whole.

Others would claim that the fact that governments negotiate quotas, is beside the point. They do it because international convention dictates it. They would argue that quotas must belong to the industries which developed the markets. To the extent that producers have made past investments in quota
markets, it is argued that they would be unjustly denied the benefits of that investment if the quota rents were now assigned to consolidated revenue.

It is worth reiterating that quota rights are created by political decisions. There is no inherent underlying economic rationale for them. As such, they can be altered at any time. In other words, they are subject to political rather than market risks. At the time of the debate over quota allocation in 1993, there were reports that the bankers who hold loans to large processing companies were keen to see the rights allocated to the companies in a "permanent way" that would improve their balance sheets. This assumes that the USA will continue to concede the economic rents to the supplying countries. But this is subject to a political change at any time. Access rights would therefore be a rather risky asset against which a banker might lend.

**Options for Allocating Access Rights**

Like any scarce resource, access rights are valuable and must be allocated among competing users. There are a number of options for allocating the entitlement to a quota market. Entitlements can be based on one or a combination of:

- the volume of past exports to the quota market;
- the volume of past exports to quota and other markets;
- the volume of past sales to both domestic and export markets;
- the level of production in some past period;
- the value, rather than volume, of sales to any combination of the domestic, quota and non-quota markets; or
- an auction or tendering system, where the rights are annual, renewable periodically or permanent.

The criteria to assess the options are that any quota allocation system should:

- capture the full benefit of the quota premiums and returns it to New Zealand;
- avoid over production through sending the wrong signals to producers;
- give processors the incentives to maintain the right amount of killing capacity;
- stimulate competition in the provision of marketing services; and
- encourage producers and processors to continually seek to improve the efficiency of their operations.

There are three essential types of allocation system: production based, export based or a tradeable rights system.

**Option 1: Statutory Power to Allocate Access Rights**

The present system is production based; a variant would be an export based system. It fails against all the criteria.
A key role of the Meat Planning Council (MPC) is to decide if there should be a quota allocation system and how entitlement is to be earned. How is a quota allocation system selected? Currently, the MPC recommends a system for New Zealand exporters, and the Meat Board then makes the final decision as to whether to endorse that recommendation. For all markets and types of meat, rights are allocated to existing firms on the basis of their share of the total national export-graded kill.

Predictably, firms would like to have a larger share. They have a strong incentive to increase their current kill in order to claim a greater share of the more profitable quota market next year. They have been willing to pay farmers an additional premium in order to procure greater supplies of live animals.

In effect, meat companies have been buying their entitlement to part of the quota, by increasing their throughput. The resultant bidding up of farm gate prices, while welcomed by most producers, has other harmful consequences. With higher prices, producers will be encouraged to increase their production. Livestock production will appear, at the margin, more profitable to them than using their resources in some other enterprise.

What happens to the extra production? By definition it cannot be sold in the quota markets. If it could, that would mean there is unfilled quota available. But in that case the quota access rights would have no scarcity value, so the issue of higher procurement prices due to quota hunting would not arise.

When the additional output can only be sold in other markets a lower price inevitably results. If that were not the case the companies would have preferred to have sold in these markets rather than to the quota market in the first place. As a result, consumers in those markets will benefit. In short, some of the value of the quota access rights is lost to New Zealand precisely as a consequence of the manner in which companies buy their entitlement to the quota markets.

To the extent that farmers perceive the system results in a higher price to them, they will be unlikely to campaign for a change. By allocating quota rights in this way, producers receive a price signal that acts as an incentive for them to expand output. In fact they are being told that world markets are demanding extra output which can be sold profitably. What is not obvious to them is that extra output will have to be sold at prices which may not cover the total costs of producing and processing. In other words, extra resources are attracted into livestock raising which are not going to be rewarded fully by the prices received on overseas markets. This is not a good use of our resources.

In the case of producer cooperatives who are obliged to accept the extra output from their supplier-members, this system will encourage them to maintain additional killing capacity over and above that which would be required if they were only processing the amount of stock that could be sold profitably.

The issue is further complicated by the over-capacity that exists in the processing sector. As a result of a long history of intervention by governments, both directly and indirectly, the meat industry today is financially unsound and has excess capacity, reportedly as high as 30 percent. Poor commercial judgement, itself a consequence of past government intervention, has compounded the problem. The need to be accountable to one's shareholders is greatly reduced if there is always the prospect that they will be compensated with taxpayers' money for commercial ineptitude.
That over capacity in the processing sector has led companies to pay more than the market value for stock in order to cover some of their high fixed costs. This has occurred despite the fact that as an industry, they have been consistently making losses. In the last four years alone, these losses total more than $300m.

The present allocation system based on production helps to perpetuate both the over capacity and the losses in the meat industry. Added to this, milk prices paid to dairy farmers induce an over supply of meat from that industry and compound the problem for the meat processing sector.

Because the present system uses production for export as its basis, an additional distortion is created. Under this system, domestic prices are higher than they would have been. How does this arise?

The answer is simply that animals are diverted to the export market until the price paid by domestic consumers is at least the same as returns to processors from exporting. The export value is made up of the return on world markets, plus the value of the additional quota allocated on the basis of extra export production. The domestic price is increased by this amount. Only if the quota were to be allocated on the basis of all production, both export and domestic, would this distortion of the domestic price be avoided.

With the way the export quota system operates, New Zealand producers give up some of their benefits, and pass them on to foreign consumers. Why producers would want to do this is not immediately apparent. The answer may well lie in the fact that the losses of the premium to foreign consumers are not transparent and producers feel the present system gives them higher farm gate prices. If producers received a cheque for the total quota benefits of let us say $2,000, but then had to write a cheque made out to foreigners for $500, they would see the costs that the present system is imposing on them.

When producers receive a payment for their livestock, it is typically made up of three parts:

- a payment for the animal based on the amount that the market will pay for the product;
- a return to their share holdings in the cooperatively-owned processing facilities; and
- a share of the premium associated with New Zealand's privileged access to higher priced quota markets.

Until these payments are separated, New Zealand cannot expect to produce the right amount of meat, sell to the right markets and develop and maintain the right amount of capacity in processing. Farmers lose, shareholders lose and the nation loses. However, any arrangements for processing and marketing New Zealand meat which do not result in maximising profitability for producers and exporters alike, are simply not sustainable. In its 1991 Annual Report, AFFCO - the largest meat company in New Zealand - noted that it:

"...has consistently failed to separate the interests of its shareholders and suppliers. While the company has had to pay competitive prices for livestock, the need to produce commercial rates of return on shareholders' funds has not been given priority. As a consequence the company's overall performance has been unsatisfactory".
In 1993, the Chairman of AFFCO stated that the company was looking at several options "to boost its low ratio of shareholders' funds to assets". Among the key issues to be addressed were: "separation of shareholder returns from supplier returns;" and "establishment of a true market value for shares which would unlock shareholder wealth".

In short, the present system:

- creates uncertainty;
- is administratively clumsy;
- leads to over-production (eg. in manufacturing beef);
- causes misallocation of resources;
- discriminates against domestic consumers in favour of foreign consumers;
- dissipates some of the economic premiums that New Zealand should capture as a supplier to the quota markets;
- reduces national income; and
- contributes to the continuing overcapacity and losses in the meat industry.

**Option 2: Tradable Access Rights Administered by Government Agency**

Serious consideration must be given to a system of tradeable rights (TRs). The rights of access to quota markets would be purchased either by tendering or auction. New Zealand has experience of this type of trading arrangement when tendering was used to allocate the rights to import. The tendering was done by the former Department of Trade and Industry. A tendering scheme for tradeable rights could therefore be administered by a government department under enabling legislation.

The allocation of quotas in the fishing industry provides an insightful analogy with the problem of quota allocation in the meat industry, although the limited quantities that are set as the allowable catch in the fishing industry are set for different reasons than meat export quotas which are set by importing countries. Until the early 1980s, fishing quotas, to the extent they applied at all, were competitive. That is, fishers collectively fished as hard as they could until the quota was reached. This situation was not dissimilar to how meat export quotas are currently allocated by reference to export kills. By the mid-1980s, the fishing industry was in crisis. The industry was vastly overcapitalised, particularly in the inshore fisheries. Profitability was low. There was a lot of criticism of bulk harvesting methods which rewarded those who caught the most fish in the fastest time, regardless of where and how the fish would be marketed. In 1986 the quota management system was introduced. Under that system, each fisher was allocated an individual quota. Most commercially harvested fish stocks were allocated under this scheme. Quotas were transferable. While not without its problems, the quota management system profoundly affected the way the fishing industry conducted its business. With secure access, companies were able to better plan their harvesting of fish to fit in with processing and marketing plans. A lot of excess capacity was retired. The same, or often reduced, amounts of fish were caught with fewer vessels and less factories. Profitability improved. Markets for products which required careful harvesting and handling of fish blossomed, such as the export of fresh snapper to Japan. Greater security of supply meant that overseas
buyers were more interested in entering into longer-term relationships with New Zealand exporters, including the joint promotion of New Zealand fisheries products. Brian Rhoades, then Chief Executive of Sealord Products Ltd and Chair of the New Zealand Food and Beverage Exporters Council noted that:

"trading in catching rights has led to a rapid restructuring of the seafood industry and created a stable economic platform for companies to invest in value adding which would never have been possible in the uncertain economic environment which existed when the catching of fish took place on a competitive basis."

Few fishers or fish exporters would want to return to the old systems of fisheries management.

Through a system of TRs processors in the meat export industry would pay for their rights directly rather than by bidding up the prices paid for livestock. This would mean that the price signals received by producers would reflect the true underlying market conditions and would not distort their decisions.

Quota rights would be an asset treated in the same way as any other asset. Once purchased they would be fully transferable. New entrants would have to buy quota rights in the same way as they have to invest in plant and equipment. Those who are the most efficient would be able to offer the highest bids for the rights. This would encourage efficiency and assure that the returns to the scarce rights are maximised.

Who should receive the payments? There is no simple answer. If it is believed they belong to New Zealand as a whole, they should be paid into the consolidated revenue. That is where the revenue from the import licences went.

If, on the other hand, they are to be returned to producers, this must be done in a way that clearly separates the quota cheque from the returns to selling livestock. If the value of quota were capitalised through a one-off sale, the returns could go to producers on the basis of recent sales. This would ensure that the future price signals reflect the true, underlying market conditions.

There would be a need to make suitable transition arrangements in order to protect the interests of existing holders. The scheme could be phased in over a 5 year period, with the rights sold permanently. The possible reaction of importing countries to tendering of rights would need to be considered, however.

An alternative could be periodic tendering of the quota rights. Under this approach, the quotas would be tendered on, say, a rolling 5 year basis. Such a rolling basis would reduce concerns about the ability for new entrants to acquire access, but a term that is too short will reduce the ability of firms to maximise benefits from quota.

Whether or not a system involving periodic tendering would be appropriate depends largely on the distribution of the payments. If producers receive a stream of payments related to their volume of output, either as a direct "cheque in the mail" or through a reduction in levies, the problem of distorted signals will persist. They will simply factor in those payments when deciding on how many resources to devote to meat production. Of course, were the payments to go to consolidated revenue, then clearly this problem would not arise.
In summary, the debate over the fine tuning of the present production/export based quota system is largely sterile. It misses the key point. Any such system is inherently flawed. Quota rights are assets. They must be traded and recorded like any other form of asset. Current problems will persist and New Zealand will continue to forego benefits unless they are treated that way.

Conclusions

Access to international markets must be constantly monitored and negotiated. The Ministry of Foreign Affairs and Trade must have the ultimate responsibility for this. As well as having the delegated authority, it can take a broad, rather than sectoral view of that which is in New Zealand’s best interests.

No justification for granting statutory power to producer boards arises from the need for international negotiations. Other countries create barriers to entry to protect their producers. This raises their domestic prices, and makes exporting to those markets more attractive. The right to sell in these markets becomes a valuable asset. The existing system fails to maximise the value of that asset to New Zealand. In effect, the scheme is a political creature, largely determined and administered by the MPC. The system creates uncertainty, is administratively clumsy and misallocates resources.

An appropriate scheme would capture the full benefits and return them to New Zealand, avoid over-production and the maintenance of over capacity, and stimulate competition and improved efficiency among processors. Any scheme based on awarding quota rights according to the volume of production or exports will fail to meet these criteria.

Proper valuation and accounting for these assets will only come about when they are traded like any other asset. Serious consideration of this option is overdue. The current "muddle-through" approach from year to year creates uncertainty, leads to over production and dissipates the quota rents.

The need to allocate quotas in itself is no justification for granting statutory powers to the boards. New Zealand has experience in tendering tradeable quota rights for imports. That system was operated without difficulty by the Ministry of Commerce. No one suggested the need to pass special legislation in order that the footwear or textile producers run their own quota tendering scheme. An independent government agency, such as the Ministry of Commerce could manage the allocation system for market access for agricultural exports.
5. PROMOTION

Promotion as a Marketing Strategy

Promotion is part of a marketing strategy that facilitates market development. Promotion not only provides information to consumers about the product and its value, but also persuades the customer to act on that information and purchase the product at the best price that can be extracted from the market. Promotion includes, but is not limited to, advertising and other marketing initiatives.

Promotion is costly and its benefits are hard to determine. Nonetheless, the benefits of promotion, however measured, must be constantly weighed against costs. Poor promotion results in the relative contraction in market share while successful promotion expands it. It is always difficult to determine exactly how much of the gain or loss in market share relates to promotion efforts and how much to other factors. It is not wise to expand market share (or increase the price received) if the costs of such actions mean that producer profits actually decline.

The marketing of agricultural products has long been characterised by generic promotion, since with essentially homogeneous products there is little or no potential to establish a premium for a product which is available from a diverse set of suppliers. Generic promotion strategies are constrained by the incentive for individual firms (or nations) to free ride and let others pay the generic promotion bill. "Country of origin" labelling, which aims to benefit the producers of that nation, has displaced traditional emphasis on generic promotion, most recently in relation to wool. However, this is not necessarily an effective promotional strategy, particularly for products blended in the manufacturing process. In addition, naming the country of origin has the potential both to encourage and discourage consumer purchases. Furthermore, it is extremely difficult to define adequate rules concerning country of origin labels. Does the origin just refer to the source of the raw materials, or does it refer to where the processing activities took place? The increasing globalisation of manufacturing and definitional problems can result in country of origin labels becoming increasingly difficult to interpret.

Branding can allow even homogeneous products to be differentiated by the quality of a company's service or presentation. The greater the profits to be made by differentiation, the greater is the incentive of firms to create brands. Branding can thus undermine the benefits of generic promotion by skewing the benefits of promotion from firms which rely solely on generic promotion to those which brand their products in addition.

The challenge for producers is to ensure that adequate and appropriate investment is made in promotional activities. The primary vehicle for encouraging such investment is institutional rules which allow players the opportunity to reap the rewards of their initiatives. The critical issue is whether statutory intervention is necessary to ensure that adequate promotion of New Zealand agricultural products.
Options for Promoting Agricultural Products

Option 1: Statutory Power to Levy and Promote

Under this option, agricultural marketing boards have the power to levy producers and spend funds on promotion. The funding of promotion through a compulsory levy on producers has traditionally been justified on the basis that otherwise insufficient resources would be devoted to promotion since those who do not contribute nonetheless derive a benefit.

Both producers and processors benefit from the promotion of agricultural products, but the costs are borne by producers. Promotion funded by producers provides a subsidy to processors and retailers saving them the costs of investing as much in promotion. Nonetheless, some agricultural processing and exporting firms themselves invest in promotional activities where they can capture the benefits through brands and trademarks. Although some firms, such as those in the wool industry are early-stage processors with little scope for promotion of final products, it is likely that producer-funded promotion crowds out investment in promotion by processors.

The statutory power to levy producers is a valuable asset for the boards. The assured income means that boards have little incentive to assess the effectiveness of their promotional activities or to ensure that they meet the needs of the funders. There is insufficient information for producers to assess promotional performance; indeed, boards tend to use levy monies constantly to promote promotion, rather than provide information about its effectiveness. Nor do producers have any direct mechanism to influence promotional activity. The recent change in the direction of wool marketing from generic "Woolmark" promotion to country specific "Wools of New Zealand" promotion, with little if any information on the efficiency or effectiveness of the two strategies, illustrates the problem.

Promotion is typically carried out directly by the marketing boards. Even if there are valid reasons for funding promotional activities from compulsory levies, there can be no presumption that they extend to the provision of such services. In-house provision does not necessarily ensure that promotion is carried out cost-effectively or in a manner which maximises net benefits for producers.

In short, the use of statutory powers to collect levies on a compulsory basis from producers to fund promotion has several disadvantages:

- it can crowd out investment in promotion by firms;
- the costs of promotional activity are not shared commensurately with the benefits;
- there is little incentive for the boards to monitor the effectiveness of promotion;
- there is little incentive for the boards to carry out promotional activity efficiently; and
- producers are unable to choose between promotion and other on farm and off farm investment.

If promotion, including country of origin promotion, continues to be funded from compulsory levies, producers could realise some of the value of their previous investments in this area by progressively
seeking to recover a greater proportion of the costs of establishing brands from firms using them. Such an arrangement would have several advantages:

- it would share the costs of promotion between producers and processors more closely in line with the benefits;
- a more explicit linkage between costs recovered and rights to use the brand would help to assess the brand’s value to manufacturers and retailers;
- it would enable promotional costs to be targeted more effectively on products which are most responsive to promotional effort. Levies could be reduced for producers of products which are relatively insensitive to promotion;
- the provider of the logo (the boards) would have a greater incentive to ensure that the logo meets the needs of marketers; and
- incentives faced by producers and processors would more fully correspond with those dictated by the market place. Because marketers would directly bear a greater proportion of promotional costs, they would be more motivated to ensure that the programme was cost effective.

Promotional expenditures could be allocated on a fully contestable basis across promotional and advertising firms. The central task of the boards would be to manage the funds and to monitor the performance of different firms and their promotional efforts in different markets.

**Option 2: Voluntary Funding of Promotion**

If promotion were to be funded entirely on a voluntary basis, it does not follow that promotion of New Zealand meat product would cease. Companies would continue to have incentives to promote their own product to improve their sales and profits. To the extent there is value in joint promotion, firms are likely to club together for joint promotional activities. Companies work together at times on domestic issues (for example, recent proposals for a joint tender for the assets of Weddel New Zealand Ltd) and sometimes in the market place in regulating the flow of produce onto a market.

The value of brands and classification standards already established could also continue to be realised if promotion were funded voluntarily. As noted above, exporting firms could be licensed to use brands currently owned by a board.

A cautious attitude to promotion is consistent with the risks associated with venture capital type investments. Promotion initiatives are very risky and it is unlikely that all farmers would want to share in these risky investment strategies. Those producers who wish to invest in promotional programmes could do so by directly investing in farmer-owned companies that invest heavily in promoting their products.

If expenditure on the promotion of wool became entirely voluntary, the wool processing, distribution and retailing industries would still remain. An environment would be fostered which encouraged these industries to take more initiative in promotion. Net gains could come from better management of advertising funds and producers would bear a lower proportion of promotion costs.
Against this, however, there is a concern that because certain New Zealand products such as wool are exported in early stages of processing, there would be insufficient incentive for processors, distributors and retailers to promote the unique attributes of New Zealand wools. New Zealand wools would have a much weakened brand image to end-users. This debate turns on the question of the effectiveness of “country of origin” promotion for intermediate inputs like New Zealand wool. In increasingly globalised production processes, New Zealand wool is combined with other products to satisfy the requirements of end-users and may lose its identity. This is not harmful to the long-term interests of producers, however. To the extent New Zealand wool has the attributes demanded by consumers, the interests of processors, distributors and retailers in promoting their products will coincide with the interests of New Zealand producers. Such promotion may not necessarily be on the basis of the country of origin of raw materials.

**Option 3: Funding Promotion under The Commodity Levies Act**

If producers believe that they will obtain net benefits from funding promotional activity, avenues are available under the Commodity Levies Act for a compulsory levy to fund promotion.

**Conclusions**

The central question in respect of promotion is whether specific statutory intervention is necessary to ensure there is adequate promotion of New Zealand wool and meat. This intervention would be in the form of a compulsory levy on producers to fund promotion, but risks “crowding out” other means by which promotion can be funded, such as funding by exporters, distributors, manufacturers and retailers. Promotion funded through levies must necessarily be more generic than promotion undertaken by individual firms and thus risks impeding the development of brands and other means by which non-payers can be excluded from the benefits of promotional expenditure. These risks need to be acknowledged and taken into account in deciding the extent to which promotion funded by compulsory levies is appropriate.

Where producers believe that they should fund promotion of meat and wool, avenues are available under the Commodity Levies Act for a compulsory levy to be introduced to fund promotion. Specific statutory powers to strike levies to fund meat or wool promotion are therefore superfluous.

If promotion is funded by compulsory levies, it is important that accountability and responsiveness be encouraged through funding promotional activities on a more commercial basis and consistently with “user pay” principles. This would be achieved, for example, by seeking to progressively recover a greater proportion of the costs of establishing brands from the users of those brands. This would build on approaches already being pursued by the boards, such as jointly-funded promotion with private firms.
6. QUALITY ASSURANCE AND STANDARDS

The Need for Quality Assurance and Standards

Standards facilitate markets by defining products. Precise, clearly defined and widely used definitions facilitate trade by providing information to customers and producers about the precise nature of the product.

Standards and grades are widely used in commerce to facilitate communication between buyers and sellers. The information they convey helps producers to discern what the market wants and enables them to compare prices paid by competing companies for similar stock or wool and consumers to have confidence in the product on delivery even when supplied from overseas. Defining standards, measuring product and auditing involves significant costs. The challenge is to provide the optimal level of involvement in relation to the investment made.

Quality assurance programmes are critical at all stages in the farm-to-customer chain. They allow the product to reach the consumer in such a form that the consumer is satisfied and is likely to engage in repeat business. Quality assurance may form part of a business strategy to enhance employee performance. This can be of great help to senior managers and directors wishing to monitor performance. Quality assurance programmes can also reduce waste resulting from sub-standard product and reduce the role of regulators in an industry.

In addition, importing governments may require inspection of agricultural products, largely as a result of health concerns, although sanitary and phyto-sanitary requirements can be used as trade barriers. However, inspection requirements set by importing governments are not met through the use of statutory power.

The critical issues are whether statutory powers should be used to define a system of standards and quality assurance, and whether compliance with the system should be compulsory.

Options for Quality Assurance and Standards

Option 1: Statutory Power to Set Standards

Some marketing boards use their statutory power to set classification standards. For example, the Meat Board sets classification standards and audits company classification practices. The Wool Board sets standards on packaging. In addition, the Wool Board uses its statutory power to register wool testing laboratories.

The setting of standards by boards provides buyers in overseas markets with an implicit guarantee of quality. The implied rationale for the use of statutory power is the potential negative effects of poor quality.
exports by one firm on other domestic exporters, and thus producers, and the potential benefit to all processors of presenting New Zealand products as being independently tested and guaranteed to meet description.

The principal disadvantages of this system are that:

- the standards set by the boards may not necessarily be commercially appropriate;
- boards can become involved in policing the activities of processors and exporters; and
- standards are set for processors and exporters at the expense of producers.

**Option 2: Standards Set by Independent Body**

With no statutory power granted to boards, it is likely that those existing board-set classification standards which were commercially valuable would remain, others would slowly disappear and new standards would emerge.

Under this option, grading standards would be set and audited by separate independent bodies. There is no reason for this body to be established by statutory power: commercial competition would allow the emergence of one or more credible, reputable standard-setting and auditing organisations. The process of competition would also ensure that the standards set would meet the informational needs of export markets. Because exporters would directly bear a greater proportion of classification costs, they would be more motivated to ensure that the programme was cost effective.

Processors and exporters would pay to use a quality mark which would assure buyers of adherence to quality standards. Such a market would be protected by enabling legislation protecting intellectual property rights. In a similar fashion, the characteristics of products such as wool could be tested to provide buyers with information and to allow sellers to meet their specifications. Since the costs of operating the grading system would be met by those producing graded products, grading would be targeted more effectively on products which were most responsive to the setting of standard grades or quality marks.

The reputation of the standard-setting and auditing bodies would implicitly guarantee the stated quality of export products. The standard-setting body would have incentives both to ensure that the grades met the needs of importers and consumers and to retain the integrity of the standards to safeguard its reputation. The potential costs to these firms of non-adherence to the set standards would induce close policing of processors and exporters. Fraudulent use of quality marks could be remedied through the courts.

There is no reason for exporter and processors to be required to meet such standards or to undergo product testing. There is no reason why trade could not be based on the reputation of private firms. Testing and certification to assure product quality is costly, but will be undertaken voluntarily as long as it produces a net benefit: if it does not produce a net benefit, compulsion will induce losses. In addition, buyers have strong incentives to demand quality assurance and product testing, since it reduces their costs of transacting. In a competitive environment, sellers will provide this information.
Little or no industry-specific statutory powers would be necessary for this option. Such powers, if any, would only be needed to define who can specify standards. Existing enabling legislation related to property rights would be used to protect quality marks.

Conclusions

Standards and product testing facilitate market development by differentiating products as having the attributes demanded by consumers and by improving communication between buyers and sellers. No industry-specific statutory powers are necessary for classifications and standards.

With no statutory power granted to the boards, commercial firms would emerge to set and audit standards. Existing standards could be progressively commercialised and privatised by changing existing classifications into brands. The use of standards would be optional. Intellectual property legislation would be used to protect quality marks and brands.
7. RESEARCH AND DEVELOPMENT

Investing in R&D

Investment in research is vital to maintain dynamic, efficient and innovative industries. The overriding objective of investment in R&D by producers must be to maximise their net return. R&D directed at products and processes on the farm contributes directly to profitability by allowing producers to increase productivity and/or reduce costs. R&D at the processing stages can also benefit producers by increasing the demand for their products.

Any institutional arrangement has to manage the investment in R&D so as to maximise profitability. The efficient management of an R&D investment portfolio involves the following steps:

- establishing an optimal level of investment relative to other on-farm and off-farm opportunities;
- establishing appropriate funding mechanisms for investing in R&D so that investors can capture the returns;
- allocating R&D investment efficiently between different areas;
- utilising good science to maximise the likelihood of successful research;
- obtaining an adequate rate of return on the investment; and
- ensuring accountability to investors.

The advantages and disadvantages of alternative institutional arrangements need to be assessed in terms of ensuring:

- that the right amount of investment is made in R&D; and
- that investment is managed efficiently to maximise the net returns to the producers.

Options for Funding and Provision of R&D

The structure of alternative institutional forms for investment in R&D has important consequences for the extent to which each can maximise profitability. Each produces incentives which shape the behaviour of individuals: if the structure is unsound, it is unlikely that producers’ interests will be well served, despite the best efforts of those involved.

Intellectual property rights legislation is available under all the options for the funding and provision of R&D. It provides the protection of the results of research necessary to induce scientific inquiry.
Option 1: Statutory Power to Fund and Provide R&D

Industry-specific statutory power involves the compulsory acquisition of levies by the statutory boards and the control and allocation of research funds by the boards. Typically, a significant proportion of the levy income of boards is spent on R&D.

There is no explicit justification for the use of these statutory powers, nor is there an explicit mandate from producers. It could be argued, however, that the statutory powers are used to overcome perceived problems of the voluntary funding of research by the industry.

The fundamental problem with the structure of the boards is that they do not contain inherent incentives for the efficient management of an R&D portfolio, nor do they automatically achieve the objectives of maximising the profitability of producers. The boards themselves do not benefit from research, and there is no mechanism to ensure that they act automatically in the interests of producers. Importantly, the system means that insufficient information is produced to assess the efficiency of the investment.

The research activities of the boards do not appear to be explicitly linked to the objective of maximising producer profitability. As a result, there is little current incentive for the board to assess R&D performance in terms of determining the rate of return to producers and establishing whether the rate received is better than that which could be obtained by using the funds elsewhere.

The levy percentage is fixed. Accordingly, the value of levy income varies with the base, whether volume or value. Fluctuations in income from levies determine the level of R&D funding, so there is little incentive to determine whether the current level of funding is too low, too high or just right. Since producers are required to pay the levy, there is little need to inform them about the returns they receive from their investment in R&D.

The board is politically accountable to producers, but political accountability alone is unlikely to be effective in ensuring that the board funds and manages R&D in a way that maximises returns from such activities. This is because elections of any kind are seldom determined on a single issue, such as the returns to R&D; there tends to be a lack of accessible information to voters; voters are often discouraged from voting because they find it a chore; or voters feel that their vote will not affect the outcome.

The very nature of the compulsory collective funding of R&D by a large number of small contributors with political accountability by the boards to investors accounts for these structural weaknesses. It is possible that accountability to the producers could be somewhat improved by:

- clarifying the objectives of the research levy;
- setting research priorities;
- funding research on a contestable basis between competing research organisations;
- assessing the research effort; and
- informing producers about the returns received.
This accountability, however, is likely to be blunted, since producers dissatisfied with the performance of the R&D portfolio have no means of venting their dissatisfaction other than through the electoral system.

In short, the present system:

- does not necessarily result in the optimal level of investment in R&D;
- does not create incentives for efficient management of the R&D investment portfolio to maximise the returns to producers;
- coerces the funding of R&D by all producers without an explicit or renewable mandate; and
- is not directly accountable to producers.

**Option 2: Voluntary Funding of R&D**

The principal characteristic of agricultural export industries is that there are many small producers. It is unlikely that any single individual would be able to fund large and costly R&D projects. However, voluntary funding on a collective basis would allow producers to invest in R&D which benefits them all.

It is often argued that the collective funding on a voluntary basis could involve high organisation costs. Nevertheless, producers have a strong incentive to invest in activities which generate a satisfactory net return. That is, they will invest where all the costs, including the costs of organisation, are less than the expected benefits.

Voluntary funding would be likely to involve setting up a research funding organisation to receive contributions and manage the R&D portfolio. This organisation would have strong incentives to manage the funding of R&D efficiently and accountably, since failure to do so would result in a falling away of contributors.

The costs of organisation are often used to justify compulsory funding. Yet there is no reason to suppose that the costs of organisation in this case would be any less: in fact the additional costs of enforcement, for example, could make them greater.

Another justification for compulsory funding is that those who benefit from R&D would not fund it, but rely on the contributions of others. Yet there is always an incentive to invest where the return is worthwhile, regardless of the fact that others may also benefit. This is the reason why some "free riding" is tolerated throughout the marketplace.

The apparent underinvestment in R&D which results from voluntary funding is also used as a justification for coercion. Yet the level of funding is a rational choice by investors. If they consider that their funds would be more profitably invested elsewhere, then there is no underinvestment. Requiring compulsory funding in these circumstances over and above that which would be made voluntarily, would simply drive down the overall return to each producers' investment activities.

The voluntary funding of research is fundamentally different from the use of statutory power to impose levies.
• it results in the "right amount" of investment in R&D, since individual producers determine the level of their contribution;
• it creates incentives to manage R&D efficiently and maximise the returns to producers who invest;
• it is voluntary, rather than coercive, and does not require statutory powers; and
• it is directly accountable, since producers dissatisfied with the returns to their investment could simply decline to contribute further.

Option 3: Funding R&D under The Commodity Levies Act

This option utilises enabling legislation to allow producers to levy themselves to fund R&D. Producers determine the levy through an implicit assessment of the relative rates of return from R&D and alternative on-farm and off-farm investment opportunities. In addition, the levy rate can be altered if necessary at the time of renewal. As a result, the optimal level of investment in R&D is likely to be determined.

An organisation to collect and allocate R&D funding from many small producers would face many of the same issues currently faced by the boards. However, it would be fundamentally different from the boards in its accountability to producers. Unlike a board, but like a voluntary research organisation, it would face disbandment if it failed to meet the expectations of producers. This threat produces strong incentives for the organisation to keep producers informed about the returns to their investment and this effect is likely to be transmitted into efficient research management.

The use of the enabling legislation in the form of the Commodity Levies Act is different from the use of statutory power:
• it creates the incentive to invest the "right amount" in R&D, since producers determine the levy;
• it creates incentives to manage R&D efficiently and maximise returns to producers;
• it is coercive of a minority of producers with the voluntary and renewable mandate of the majority; and
• it is directly accountable, since producers dissatisfied with the returns to their investment could decline to renew the mandate after the required period.

Conclusions

Investment in research is essential to maximise profitability. In industries with a large number of small producers, different arrangements can be made for the funding of R&D.

Agricultural marketing boards use statutory powers to collect levies, part of which is spent on R&D. There is no explicit justification for the use of these statutory powers, nor is there an explicit mandate from producers. It could be argued, however, that they are intended to overcome perceived problems with voluntary funding of R&D.
Voluntary arrangements can be used to fund R&D where such research is worthwhile. Intervention to coerce all the producers in a particular industry to pay for research from which they all benefit, is only justified where voluntary arrangements are unsatisfactory. However, these conditions cannot simply be presumed to exist in an industry with large numbers of small producers, since the costs for voluntary organisations may be less than they are for compulsory ones; and producers have an incentive to fund profitable R&D regardless of the benefits that others may also obtain. For example, investors in research gain benefits from first use of leading-edge technology before others.

The Commodity Levies Act is increasingly being used to fund R&D and other activities within the agricultural sector. The principal disadvantage is that it is coercive of a minority of producers with the voluntary and renewable mandate of the majority. If there is a demonstrable failure of voluntary arrangements to adequately fund R&D, the use of the Commodity Levies Act is likely to be superior to specific statutory powers confined to a particular sector.
8. EDUCATION AND TRAINING

Investment in Education and Training

Education and training is an essential part of maintaining the skills of individuals and enhancing their productivity. Increasingly, industries are concerned with ensuring that there are mechanisms for identifying the training needs of participants and having systems to deliver that training in a cost effective way.

The principal objective for producers is the maximisation of profitability. Education and training contributes directly to farm profitability by increasing productivity and decreasing the costs of labour. On the other hand, individuals invest in their own education and training if they consider that the benefit from increased earnings resulting from that training makes the cost worthwhile.

Individual firms make business decisions to invest in the education and training of their employees if it contributes to their overall profitability. There is an expectation by firms that the enhanced skills are in the interests of both parties. These arrangements however, often involve some sort of bond in return for this funding: a contract in which the employee undertakes to work for the employer for a certain period. Apprenticeships are an example of this sort of arrangement. These arrangements give the employer sufficient time to recoup his or her investment in the employee, while simultaneously providing the employee with marketable skills which he or she can transfer to another employer. Firms which fund employee training may not require such arrangements where the skills obtained are highly specialised and cannot easily be transferred elsewhere.

Education and training affects the profitability of firms both directly and indirectly. A more educated workforce increases the productivity of a firm and thus reduces cost. Indirectly, education and training increases the supply of labour in a particular field. In the absence of wage setting, this will decrease relative wages and increase the firm’s profitability. Individual firms are unlikely to be willing to fund research on this basis alone, since the benefits are spread too widely for them to capture. Collectively, however, all the firms will benefit from education and training which reduces their labour costs by increasing the pool of skilled labour. Firms are likely to be willing to fund the acquisition of those skills specific to the industry. Funding skills which could be used in other industries would merely transfer the benefit elsewhere.

Options for Funding and Provision of Education and Training

Option 1: Statutory Power to Levy for Education and Training

Under this option boards use their statutory power to collect levies to fund education and training within the industry.
The most significant effort in this area is the Wool Board’s training of shearers and wool classers who are involved in wool harvesting. This is perhaps unsurprising, given the industry-specific nature of the skills involved in shearing, clip preparation and wool grading. An increase in the productivity and quantity of labour will result in a reduction in the costs of wool harvesting for farmers and an increase in profitability.

The Wool Board not only collects the levies, but it also carries out the training. While the programme is successful, this arrangement stifles the development of training programmes in wool harvesting which could be run by other organisations. It also hampers the emergence of new areas of training which could also be funded by producers. There are no means of assessing which funds are being used in the most effective way. Separating the funding of education and training from its conduct would permit the funds to be used in the most efficient way.

Option 2: Voluntary Funding of Education and Training

Individual producers will provide education and training to their workers where they consider it to be worthwhile. However, individual producers face several difficulties:

- they may be too small to employ and train another person economically; or
- the skills learned are likely to be highly transferable to other farms and other agricultural industries, making the returns difficult to capture and the investment unattractive.

A voluntary system is thus likely to result in too little funding of education and training. As is the case in R&D, a compulsory levy is often called for as a solution.

Option 3: Education and Training under The Commodity Levies Act

Under this option producers would voluntarily agree to levy themselves to fund education and training within their industry. The principal advantage of using the Commodity Levies Act to fund education and training would be transparency and accountability to producers. It would enable the industry to more easily determine the levy rate for education and funding, and to assess its effects. However, the level of funding currently devoted to education and training is relatively modest, and the benefits of using the Act for this purpose alone would have to be seriously considered against the costs.

Conclusions

Education is an investment like any other. Individuals have incentives to invest in their education and training if they think it is likely to be worthwhile. Firms also invest in the skills of employees when they can reap the benefits. Any industry has strong incentives to invest in enhancing the skills used in the industry.

The principal shortcoming of the use of statutory power to levy the funding and provision of training by a board is its effects on the emergence of new providers and new areas of training. The separation of the funding from the conduct of training would allow it to be carried out by the most effective providers and would allow new programmes and areas to develop.
While the use of the Commodity Levies Act offers some advantages of transparency and accountability, its use for education and training alone is unlikely to be worthwhile.
9. COMMERCIAL ACTIVITIES

Investment in Commercial Activities

Investments by the boards are funded from compulsory levies paid by producers. The issue addressed in this chapter is whether commercial activities and investments should be supported by statutory levy-collecting powers.

In the past, the boards have undertaken commercial functions directly, such as the purchase and sale of wool or meat to support prices to producers. Boards also act in a commercial capacity through companies in which they have interests. Considering the commercial roles of the boards is important for two reasons:

- the investments by the boards directly affect the return that producers receive from their levies; and
- the commercial activities of the boards can affect the broader competitive environment in the industry sector. This effect can be either positive or negative. The adverse effects of commercial activities previously undertaken directly by the boards, such as direct intervention to support minimum prices, are generally recognised. Commercial investments in subsidiary companies can also have a potential effect on the competitive environment.

The key objective in respect of the boards' commercial activities is taken to be to provide a greater return to producers by its commercial investments than if the producers invested that money themselves. This objective is broader than simply "putting more than one dollar back" for each dollar of levy income used to finance commercial ventures. Each dollar of levy paid by producers has an alternative use - as investment on the farm (fencing, herd development) or off-farm (including direct equity investment by farmers in other companies). How can producers be satisfied that boards will provide a higher return than they could get if they invested the assets directly themselves? This raises two issues:

- the impact of board activities in the wider competitive environment; and
- the accountability of boards to producers. The boards are investing producer funds in commercial activities on behalf of producers. They act as agents of the producers in this respect.

The reasons commonly advanced for boards to invest in commercial subsidiaries are to:

- promote technological and marketing development and innovation through direct investment;
- provide better information to producers on market conditions and outlook; and
- promote competition.
The key questions upon which a judgement is necessary are:

- the extent to which direct investments in subsidiaries further the above goals; and
- to the extent they do, whether such investments are the best means of doing so, taking into account the potential costs.

It might also be argued that commercial investments by boards are appropriate provided they yield good returns. The argument is that a board should withdraw from commercial investments if it makes losses but continue to invest if it makes gains. However, investors rarely make investments expecting to make losses. It could be expected that each investment undertaken by the boards was with the expectation that a positive return would result, even if substantial losses were the outcome. Advocacy of board involvement in commercial activities based on the view that “if successful, keep doing it - if not, stop” is likely to result in the mistakes of the past being repeated.

**Options for Investment in Commercial Activities**

**Option 1: Statutory Power to Engage in Commercial Activities**

The role of boards in commercial activities cannot be divorced from their other statutory roles and powers. Boards are funded by way of compulsory levies and have other powers, such as the compulsory acquisition of product, and the power to control trading activities and to impose grading or certification requirements. These powers are not available to companies which are voluntarily formed by shareholders.

The issues surrounding the commercial activities of the boards are therefore not the same as whether any listed company should invest in a particular area. In particular, the power of a board to levy its income and its other statutory powers means that its commercial activities may have a significant effect on the competitive environment.

Involvement in commercial activities may "crowd out" potential investors, reducing competition and the quality of provision. Potential investors may demand a higher return than otherwise for investing in an activity where a competitor is not subject to the same commercial disciplines. The higher minimum return reflects potential risks from competing with an organisation that may face lower costs of funds or weaker incentives for management performance. For example, boards investing in commercial subsidiaries face a lower cost of capital than other new entrants. That is because investments by the boards have been funded either from government grants previously received by the boards or from income from activities which were funded by compulsory levies. The boards as owners and investors continue to be funded through compulsory levies. The cost of raising funds through compulsory levies is obviously lower than equity or debt finance.

Involvement in commercial activities may defer necessary restructuring. Boards may be prepared to invest in companies which do not yield returns sufficient to attract other investors. "Strategic" reasons, such as market development or the retention of adequate competition may represent the motivation for
investments. If other investors perceive a readiness by boards to invest for non-commercial reasons, they may be less concerned about monitoring and supervising their own investments in the expectation that, should returns fall below acceptable levels, the boards will acquire their investments. Investors in the meat and wool sectors may therefore make riskier investments or accept lower returns than they would otherwise. This can result in excess capacity, excessive costs and lower overall returns from the sectors. Both the Meat Board and the Wool Board have invested in companies that were experiencing commercial difficulties at the time they were acquired. Examples include the Meat Board’s investments in Waitaki International Ltd and the Wool Board’s investment in Wool Services International Ltd which has incurred losses, although is now reported to be trading profitably.

Involvement in commercial activities may reduce the ability of boards to play a facilitating role in reducing information costs. The involvement by the boards in commercial activities is likely to have reduced the willingness of other players in the market to share information with the boards in carrying out their facilitative roles. That is because the other players may also be competitors with the boards’ subsidiaries.

Investment through boards may distort information received by producers. Investment in commercial activities by producers through boards can lead to either of two outcomes:

- the investments fail, or yield less than market returns, in which case producer money is wasted; or
- the investments succeed. If producers are rewarded for the commercial success of board ventures through lower levy payments they will receive information that will cause them to make inappropriate choices. By receiving a higher price for their milk, wool or meat, net of levy costs, they would be encouraged to increase milk, wool or meat production, other things remaining equal, even though international prices for meat or wool remain unchanged.

This information problem has become known as bundling. The commercial returns to the boards, however, are only indirectly related to actual agricultural production, if at all. They might arise from the successful export of wool processing machinery of investment by the Diary Board in Lada cars, for example. If producers owned shares in such a venture directly and were rewarded for its success through higher dividend payments, they are less likely to respond by increasing production.

Conflicting objectives reduce accountability of the companies to the boards and the boards to producers. Conflicting objectives mean that the boards are placed in positions of deciding policies which might yield wider benefits to the industry but which may result in a commercial loss to their subsidiaries. Boards have shown a willingness to make decisions contrary to the commercial interests of companies in which they have an interest (the recent withdrawal of sole marketing rights held by Anzco in Japan are an example). The question arises, however, whether conflicting objectives may have delayed changes with the results being adverse to the interests of producers. Managing conflicts may also divert the boards from more important priorities. In addition, requiring managers to trade-off one objective against another (eg., effective market development through opening up access compared to safeguarding the viability of board investments) makes it more difficult to establish a benchmark against which the performance of the boards can be assessed. Conflicting objectives reduce accountability in the following ways:
the objectives of the boards may differ from those of the subsidiaries. The subsidiaries may be charged with the obligation to provide a minimum threshold rate of return on investments by the boards by vigorously pursuing commercial objectives. In most businesses, shareholders share the same goals. However, the boards may also wish to pursue broader goals through their investments, such as the pursuit of innovation or maximising competition in the industry. Sometimes these goals might conflict with commercial objectives; and

- the objectives of producers may conflict with the commercial objectives of the boards. Producer interests may be served by the boards pursuing objectives that are sometimes not in the interests of the boards' subsidiaries. An example might be boards conferring under their statutory powers certain marketing rights on a board subsidiary (for example, the exclusive rights Anzco have held for eleven years in the Japanese market which terminated in September 1994). This may be contrary to the wider interests of producers but may be in the direct commercial interests of the boards.

Were the boards to retain their statutory power to engage in commercial activities, accountability could be improved by making them mimic more closely the function of companies by:

- setting clear and unambiguous objectives for managers;
- ensuring that lines of responsibility are transparent and do not overlap;
- ensuring that agents (the boards) have similar incentives to the principals (producers);
- requiring managers to disclose specified information;
- monitoring the performance of managers; and
- constraining the actions of managers and directors.

However, the ultimate accountability mechanism, that of allowing shareholders (producers) to terminate their relationship with the company (board) is not available if commercial subsidiaries are retained within the board structure. Unlike shareholders who hold shares directly in a widely-held company, producers cannot signal their approval of commercial performance by buying shares or their disapproval by selling shares.

Option 2: Statutory Power to Fund Commercial Activities

Grounds commonly given for the involvement by boards in commercial activities are to promote competition, innovation and technology development. If involvement by the boards in trying to further these goals is considered appropriate, there are alternatives to direct investment in commercial activities to achieve them.

The most obvious alternative would be for the boards to specify the nature of the services they seek to acquire (such as the development of feedlots for beef or innovative ways to market wool). The board would then invite tenders for the provision of such services for a specified period. For example, tenders to operate a feedlot might be called where the successful tenderer would bid for the amount of subsidy they required to undertake such a project.

The advantages of this approach are that: 

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the costs of subsidising the provision of the services are made explicit, unlike the case for direct commercial investments;
the benefits of contestable provision are captured by the boards, and therefore by producers. Contestable provision is not available if these services are provided solely by the commercial subsidiaries of the boards; and
many of the problems of ensuring accountability referred to above (such as managing conflicting objectives) are lessened.

Option 3: Spinning off Commercial Activities

This option represents a “half-way house” between ownership of commercial ventures by the boards and the complete disposal of the subsidiaries. The commercial activities of the boards would be spun off either individually or under a holding company structure. Individual levy payers would receive shares which they could sell or retain. If desired, producer control of entities could be ensured by:

- specifying that producers only could hold shares. Shares would be tradeable independent of land; or
- defining a “golden share” or a special class of shares for producers which would retain producer control.

However, restricting share ownership to producers has a risk of reducing the value of equity by limiting competition for shares in the entities.

Under this option, producer shareholders would have a more direct influence on the objectives of commercial entities. The directors of the companies would be accountable to producer-shareholders under the terms of the Companies Act. The companies would be required to disclose information to shareholders in accordance with the Act. Shareholders would be able to signal their disapproval of the companies’ performance by selling their shares. Good performance by companies would be rewarded with higher share prices and a greater willingness by shareholders to invest additional funds.

Separation of commercial activities from the boards would:

- eliminate the ability of the boards to directly influence the policies of the subsidiaries;
- remove any residual concerns that may affect the wider competitive environment of the meat and wool sectors. These concerns relate to the willingness of private investors to invest in activities in which an organisation funded by compulsory levies also invests or the willingness of competing investors to cooperate and share information with the boards; and
- assist in clarifying the role of the boards in respect of their other objectives, such as promoting and facilitating research and development. The boards would more clearly be seen as vehicles for the funding of those activities, not their provision. Funds would be allocated on a contestable basis.
Possible disadvantages of this option include:

- the administrative complexity of allocating shares to individual producers, including developing a means of distribution. Shares could for example, be allocated by reference to levies paid by producers over the last few years; and
- the small size and value of many parcels, particularly if shares in each subsidiary are parcellled out. One means of overcoming this problem would be to consolidate the commercial interests of the Wool and Meat boards respectively into two companies. Shares in the holding companies would be allocated.

**Option 4: Sale of Commercial Activities**

This option involves the complete withdrawal of the boards from commercial activities. The sale of subsidiaries is potentially the easiest means of withdrawal administratively. However, it might not be possible for the boards to achieve best value from a sale of their commercial interests, if they were obligated to sell those interests within a certain time period with no minimum reserve price.

The key management issue under this option is how and when to sell the subsidiaries to maximise returns for producers. On the one hand, the optimal strategy may be to start afresh and sell the interests for whatever they will realise. On the other hand, returns might be higher if a staged programme of sale were to be adopted.

**Conclusions**

More than one of the above options could be followed. For example, the boards could choose to sell one subsidiary or issue shares to producers in another. The merits of a statutory prohibition of investments in commercial activities by entities funded from compulsory levies contained in the Commodity Levies Act should be considered, however. Such a prohibition would mean that the boards need never get into a position where they must trade-off objectives which compete with the interests of their commercial subsidiaries or have the requirements of managing commercial operations detract from their focus. The services the boards seek to acquire through the ownership of commercial subsidiaries could be more effectively and explicitly provided through competitive tendering. If commercial investments are retained, weaknesses in the current accountability structure noted above could be addressed by:

- greater disclosure of financial information on commercial activities, such as profit and loss statements and balance sheets; and
- requiring the boards to publicly articulate a clear policy on commercial ventures. This would include the reasons for their acquisition or retention, a capital charge or minimum dividend requirement on equity, realisable values and annual statements of corporate intent agreed with shareholders. These requirements could be included in the governing legislation of the boards.
10. CONCLUSION

The Key Issue

The critical issue for New Zealand agricultural industries is the appropriate balance between voluntary and statutory activity in various aspects of marketing and processing. The following considerations arise in addressing this issue:

- *producers purchase a wide range of services in conducting their businesses.* These include marketing services provided by the boards which producers are compelled to acquire by virtue of the levies they pay. Some or all of the services provided by the boards are, or could be, provided by the private sector;
- *producers therefore have a legitimate interest in the extent of statutory powers, if any, that apply to the provision of marketing services, such as domestic and international promotion, transport, grading and quality control, market development and provision of economic information;
- *most markets are complex and are becoming more complex as global deregulation takes place.* This means that arrangements which allow market participants to pursue their respective interests in the light of the information they have are, in general, likely to be superior to attempts to regulate trade; and
- *the onus is on the proponents of statutory powers to establish the case for intervention.* The case for intervention must be constantly reviewed in the light of changing circumstances.

Range of Statutory Powers

There are two principal approaches to statutory power:

- *"prescriptive" industry-specific statutory powers.* These are powers which can be exercised by the boards without the mandate of producers, as embodied in the existing Meat Export Control Act and the Wool Industry Act. The initiative for setting and amending statutory powers rests in the political process, in particular the Minister of Agriculture. Producers exercise influence and control by electing board members, but cannot directly alter either the rules governing the boards, their activities or levies; and
- *"enabling" generic statutory powers.* These are statutory powers which facilitate "bottom-up"arrangements where producers may voluntarily elect to form together to provide services (by establishing a company, for example). Likewise, producers can elect to levy themselves for particular purposes for a limited, renewable period.

The contrasting approaches of "prescriptive" and "enabling" approaches to statutory intervention are summarised in Table 10.1.
Table 10.1: "Prescriptive" and "Enabling" Approaches to Legislation

<table>
<thead>
<tr>
<th>&quot;Prescriptive&quot; Industry-Specific Legislation</th>
<th>&quot;Enabling&quot; Generic Legislation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Options A and B</strong></td>
<td><strong>Options C and D</strong></td>
</tr>
<tr>
<td>Industry Specific.</td>
<td>Less specific in relation to industry boundaries (e.g., between wool and meat sectors).</td>
</tr>
<tr>
<td>Less flexible. Legislative changes in powers, roles and functions occur through the political process. Operational changes within those powers can be made without reference to producers.</td>
<td>Very flexible. Functions of industry organisations can be specified and altered on a referendum of producers.</td>
</tr>
<tr>
<td>Non-reviewable.</td>
<td>Reviewable every six years.</td>
</tr>
<tr>
<td>Roles, functions and powers politically determined and enshrined in legislation and regulations.</td>
<td>Organisations must have certain objectives and meet certain minimum criteria. Within these limits producers are free to set and change the constitutions of the organisations and levies without the need to change the governing statutes.</td>
</tr>
<tr>
<td>Perpetual.</td>
<td>Automatic termination after 6 years unless renewed.</td>
</tr>
<tr>
<td>Accountability is to producer-funders through voting for directors/board members and formal monitoring and reporting, as well as to government.</td>
<td>Accountability is primarily to producer-funders.</td>
</tr>
<tr>
<td>More suitable where the producer-funded agency has powers which can adversely affect others.</td>
<td>More suitable where the agencies have little or no powers to make decisions which could be adverse to non-producer interests.</td>
</tr>
<tr>
<td>Complex legislation specifies powers roles and functions. Private arrangements are simple.</td>
<td>Simpler &quot;enabling&quot; legislation which accommodates more complex private arrangements. These arrangements can be tailored to meet changing circumstances.</td>
</tr>
<tr>
<td>Mandate of boards is politically determined without direct reference to producers.</td>
<td>The mandate of the agencies relies on either voluntary contributions or, if funded by compulsory levies, periodic producer referendums.</td>
</tr>
<tr>
<td>Producers cannot &quot;opt out&quot; and terminate relationship with the board, elect not to contribute levies or choose not to engage in certain activities of the boards.</td>
<td>Producers can sell shares in companies where these are constituted. Under voluntary arrangements producers can choose not to contribute. Under Commodity Levies Act producers are compelled to contribute for a specific, reviewable period.</td>
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*Source: Jacobsen, Scobie and Duncan (1995)*

**The Options for Statutory Intervention**

The last decade has seen a significant shift in the approach to statutory intervention in economic activity. In the past, reliance was placed on "prescriptive" legislation setting out particular goals, specifying how activities were to be controlled and disputes settled. The raft of producer board Acts are of this type.

There is a growing awareness that granting powers to a monopoly board, with extensive reliance on accountability to Ministers through the political system may not be either necessary or efficient. In contrast, the use of "enabling" legislation provides a framework within which individuals and groups have greater flexibility to develop mutually beneficial arrangements for allocating resources and resolving disputes. This approach is reflected in the Employment Contracts Act 1991, the Companies Act 1993, and the Commodity Levies Act 1991. This type of legislation has the potential to provide a stable framework in...
which voluntary transactions can take place. The evidence mounts that such an approach could enhance efficiency and accountability in the provision of marketing services for New Zealand's agricultural exports.

The persistence of inefficient statutory power can only be explained as a reflection of gains to special interests. However, the new domestic and international operating environment will increase the costs of intervention over time, and make them ever more obvious. There are several sources of pressure that signal change. Potential entrants, such as Applefields, seek to compete with statutory authorities. Producers appear to be increasingly disillusioned with the performance of the boards. A lobby group, Farmers for Change, have sought changes to the electoral procedures for grower representatives, in an attempt to enhance accountability. Meanwhile, growers of fine wool have been attempting to have the Wool Board reflect more of their interests. Consumers who have benefited from the freeing up of the domestic apple market and the town milk supply are increasingly aware of the benefits of deregulation.

The inherent efficiency of markets makes them irrepressible. At the same time, inefficient legislation is unsustainable and is subject to continuing litigation or political forces for changes. As the costs become apparent, pressure by lobbyists becomes irresistible. The Boards are creatures of political markets. It will be economic forces operating through those same political markets that will result in change.

This report develops a conceptual framework for determining the preferred structure of institutional arrangements for agricultural marketing. Although the case studies presented in this report have been drawn largely from the meat and wool industries, this framework is more widely applicable, and is thus presented in general terms.

The grounds for statutory intervention in the areas of market development, market access, promotion, R&D, education and training and commercial activities are summarised in Table 10.2.

There are four fundamental options for statutory intervention in New Zealand agriculture. They span the range between the existing statutory powers of the boards to the repeal of all industry-specific legislation and reliance on enabling legislation. These options are examined in detail in the remainder of the chapter.

Option A: Prescriptive Legislation: Statutory Marketing Boards. The existing system could be retained. The governing statutes of the boards represent a "prescriptive" approach to statutory intervention.

Option B: Prescriptive Legislation: Statutory Marketing Boards with Limited Powers. This option retains the boards and their existing functions but narrows the range of (mainly unexercised) powers they can use. The meat and wool boards themselves have proposed such changes to their respective Acts. Under this option, the governing rules
### Table 10.2: Statutory Implications for Agricultural Marketing

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<th>Activity</th>
<th>Need for Statutory Power</th>
<th>Comment</th>
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<tr>
<td></td>
<td>Prescriptive Legislation</td>
<td>Enabling Legislation</td>
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<tr>
<td>Market Development</td>
<td>No</td>
<td>No</td>
</tr>
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<td></td>
<td></td>
<td>The unimpeded pursuit of commercial goals by competing firms best serves the interests of producers in developing markets. Producers, as purchasers of marketing services, would be free to choose the strongest sellers.</td>
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<td></td>
<td></td>
<td>No</td>
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<td></td>
<td>The agency/ministry requires statutory standing in order to be recognized as a representative of the New Zealand Government. The prime responsibility for negotiating currently lies with the Ministry of Foreign Affairs and Trade. Producers, as representatives, would participate in and inform the process.</td>
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<td></td>
<td></td>
<td>Yes</td>
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<tr>
<td></td>
<td></td>
<td>No specific legislation related to a producer-funded organization is needed in order to allocate quota rights. An independent authority or Ministry, such as Commerce, could administer the allocation of quota. The payments for quota could accrue to either producers or the Crown. Legislation would be necessary to define quota rights and the process of allocation.</td>
</tr>
</tbody>
</table>
|                                    |                          | Perhaps                                                                                  
|                                    |                          | Promotional activity can be funded either commercially or by voluntary contributions. If reliance on purely voluntary contributions is demonstrably impractical, or those choosing not to contribute receive unearned benefits, the Commodity Levies Act can be invoked by a majority of affected producers. |
| Standards, Grades and Quality Assurance Classifications and Standards | No                       | Yes                                                                                                                                     |
|                                    |                          | Legislation governing intellectual property rights (trademarks, patents etc) could apply. Existing classifications and grades could be progressively commercialised, converted into branded “quality marks” and licensed on a voluntary basis. |
|                                    |                          | No                                                                                                                                     |
|                                    |                          | Statutory standing is necessary to meet international obligations. However, public and private agencies which receive accreditation from MAF Regulatory Authority, should be able to provide inspection services on a contestable basis. The only exception should be where this is inconsistent with the requirements of a foreign importing country. |
| R&D                                | No                       | Yes                                                                                                                                     |
|                                    |                          | Legislation governing intellectual property rights. Commodity Levies Act provisions would be available. Similar considerations apply as for promotion. |
|                                    |                          | No                                                                                                                                     |
|                                    |                          | Firms will invest in the creation of skills among employees where they can reap the benefits. Existing legislation caters for industry-wide training initiatives. In addition, the Commodity Levies Act could be used to create a training fund. |
| Education and Training             | No                       | Perhaps                                                                                  
|                                    |                          | Companies Act.                                                                                                                                 |
|                                    |                          | There can be no justification for the use of statutory powers to coerce producers to invest their earnings in commercial ventures where they might not have otherwise chosen to do so. |

*Source: Jacobsen, Scobie, and Duncan (1995)*
of the boards would continue to be set by either statute or regulation without a regular mandate from producers. It therefore represents a variant of the "prescriptive" approach.

Option C: Enabling Legislation: Producer-Initiated Boards. Under this option enabling legislation would provide for the boards, or broadly equivalent organisations, to be preserved. However, referendums would be held periodically to establish whether producers wish to retain the organisations. These referendums would be similar to those provided for in the Commodity Levies Act. Producers would be able to alter the constitution and functions the organisations within limits set by the governing statutes. The way in which levies are set could be altered. Since producers would have the right to regularly decide whether, and in what form, the boards are retained, this option is consistent with an "enabling" approach to conferring statutory powers.

Option D: Enabling Legislation: Producer-Controlled Industry Organizations. Under this option, specific legislation relating to marketing boards would be repealed. If producers wished the organisations (or their functions) to continue, they could either by voluntarily funded or the provisions of the Commodity Levies Act could apply. It is also an example of "enabling" statutory powers.

Option A: Prescriptive Legislation: Statutory Marketing Boards

General Features
The existing system could be retained. The governing statutes of the boards represent a "prescriptive" approach to statutory intervention. The existing roles and functions of the boards would be retained, including their involvement in commercial activities.

Advantages
Any costs of structural changes would be avoided.

Disadvantages
The disadvantages of this option are that:

- it would fail to address the inherent weaknesses of the current system;
- producers will continue to be exposed to risks from board commercial investments and marketing decisions;
- legislation is likely to "lock-in" existing weaknesses;
- these weaknesses are likely to lead to the eventual reform of existing arrangements in any event. The delay is likely to mean that reforms cause greater dislocation;
- it is likely to be increasingly difficult to achieve changes in governing legislation;
- there will be no greater flexibility to change the structure and functions of the agency to remain responsive to producer interests; and
- the extensive powers of the boards will continue to mean that they will be accountable to political as well as producer interests. They would also have multiple objectives. These factors weaken accountability.
Option B: Prescriptive Legislation: Statutory Marketing Boards with Limited Powers

General Features
This option retains the boards and their existing functions but narrows the range of powers they can use. The functions of the boards would be limited to those areas where voluntary collective action was unlikely to be effective. The governing rules of the boards would continue to be set by either statute or regulation without a regular mandate from producers. Commercial investments would be spun-off by issuing shares directly to producers or sold. The allocation of export rights to restricted markets would be governed by separate legislation and administered by a separate entity or ministry. There would be merit in incorporating processor/exporter interests more transparently, so that the organisation could thus assume the characteristics of an “Industry Board”.

The statutory powers of the boards would be narrowed in the following areas:

- the power to acquire product would either be repealed or substantially constrained;
- the power to set conditions on export licences, in particular controls on the quantities, classes and form of products which may be exported and the countries to which they may be exported;
- the power to licence exporters would be repealed; and
- controls which govern shipping contracts would be repealed.

Advantages
The major advantages of this option are that:

- any costs of structural changes would be low, including disrupting the profile of the boards in overseas markets;
- producers would be less exposed to risk in respect of the boards’ commercial investments. If they wished, producers could sell their interests in such ventures;
- the boards would be able to focus on a narrower range of objectives. This would enhance accountability;
- there would be a better matching between the boards day-to-day activities and their statutory powers; and
- reduced powers to the boards would foster an environment where greater cooperation is possible where this is in the collective interests of producers, processors and exporters.

Disadvantages
The major disadvantages of this approach are that:

- any future changes to the structure and functions of the boards would still require either a change in their governing statutes or in regulations. This will impede the flexibility to change the structure and functions of the boards to remain responsive to producer interests;
- producers will be confined to exercising influence and control through voting for members. They will have no right to “opt out” or to engage in referendums to decide whether to retain the boards and if so, what their roles and level of levy funding should be; and
* the boards would not be precluded from expanding their activities in ways that may not necessarily be in the interests of all producers.

**Option C: Enabling Legislation: Producer-Initiated Statutory Marketing Boards**

**General Features**

Under this option:

- the commercial investments of the boards would be sold or spun off;
- legislation would provide for a producer-funded agency to cover the meat and wool sectors respectively;
- the legislation would specify in general terms the aims and roles of those agencies. It would also spell out prohibited activities which would include engaging in trading activities, investing in commercial ventures, or controlling commercial enterprise through restrictions on export licenses or shipping contracts;
- while a role of the agency might be to promote quality and product development, it would not be able to set minimum grading standards. The agencies could inherit the existing classification systems for meat and wool and could be permitted to licence their use. The agencies could be permitted to register (but not licence) exporters, if appropriate;
- for the producer organisation covering meat or wool to be recognised:
  - a majority of producers would need to agree to the imposition of the levy and to the level of the levy;
  - voting procedures similar to those contained in the Commodity Levies Act would need to be followed; and
  - the constitution or rules of the producer-funded organisation would need to meet certain minimum requirements, such as adequate representation of levy payers, protection of minorities, and disputes resolution procedures;
  - a referendum of producer/levy payers would be held periodically to confirm any levy arrangements (eg., every six years);
  - there would be provision for producers with common interests to strike a separate levy which would be collected through the appropriate meat or wool organisation. This might cover, for example, a special levy on fine wools;
  - producers would agree to a maximum levy by referendum. The levy could be set at a lower level, however. The allocation of that levy between core expenditures (eg., between research, training etc) would be notified each year to producers, in much the same way as the components of a local body rates demand are disclosed to ratepayers;
  - the relevant producer-funded organisation for meat and wool would be constituted as body corporate (eg., a company). Voting rights would be in accordance with the proportion of levies paid by each producer and proxy voting would be allowed. Minority protections for those with relatively small proportions of the total vote would be incorporated into the constitution of the organisations. These protections could be similar to those in the Companies Act 1993;
  - producer/levy payers would vote for directors/board members of the organisations and on major issues, such as changes to the constitution. Directors and levy payers would owe duties to the organisation similar to the obligations contained in the Companies Act;
producers could vote to alter the functions and constitution of the relevant organisation;
the existing boards could be reconstituted under the above arrangements; and
the allocation of export rights to restricted markets would be governed by separate legislation.

Advantages
Many of the advantages of Option B also apply to this option. The additional major advantages of this option are:

- regular renewal of producer mandates will encourage the agencies to remain accountable to producer interests;
- producers would have limited rights to "opt out", by striking special levies where they choose to do so;
- the roles and functions of the organisations could evolve over time without the need for new legislation;
- specific statutory prohibitions on the agencies engaging in certain activities will provide confidence to private investors and producers;
- votes assigned to levy payers in proportion to the levies they pay would mean that those who reap the greatest potential rewards, and bear the greatest potential risks, have commensurate voting power; and
- a system of personal and proxy voting would ensure that those who have devoted most resources to monitoring the performance of the organisations have the greatest influence. At the same time, protections for those with relatively small proportions of the total vote should be incorporated in the constitution of the organisations.

Disadvantages
The major disadvantages of this approach are that:

- the procedures largely duplicate arrangements which would be possible under the Commodity Levies Act but without some of the flexibility possible under that Act; and
- the ability of producers with common interests to "opt out" from a larger group would still be limited.

Option D: Enabling Legislation: Producer Controlled Industry Organisations

General Features
Under this option, enabling legislation such as the Companies Act and the Commodity Levies Act would provide a regulatory backdrop to permit the formation of firms and producer initiated producer organisations to facilitate the operation of the market.

Producers could use the Commodity Levies Act to form a producer organisation to carry out specific functions. A single producer organisation could undertake a range of tasks, such as promotion and R&D. The existing functions of the boards could be reconstituted and funded and administered under the Act. Alternatively, producers could select to fund these activities individually on a purely voluntary basis. The statutes constituting existing boards would be repealed. The commercial investments of the boards would
be sold or spun off under this option. The allocation of export rights to restricted markets would be
governed by separate legislation and administered by a separate entity or ministry.

Under the Commodity Levies Act:

- a levy may only be imposed if more than half of those who will pay the levy support its introduction;
- whether more than half support a levy’s introduction is assessed according to how the voting is organised. For example, if voting is on the basis of the value of a commodity, then producers who produced more than half of the value of the commodity in the 12 months before the referendum would need to support the levy;
- voting papers must specify how the proposed levy would be computed (eg., by reference to value, production etc);
- the organisation to which levies are paid, by virtue of its membership and structure must represent adequately the views and interests of those who will be primarily paying the levy;
- it would be impossible or impractical to undertake the proposed activities other than through a compulsory levy or that otherwise people who chose not to pay voluntary levies would reap unearned benefits;
- any levy orders expire after 6 years, subject to extensions in limited circumstances. Accordingly, a new referendum would be required at least every six years to renew a levy; and
- no amount of the levy may be spent on any commercial or trading activity. A levy order may specify other activities on which levies cannot be spent. The order may specify all or any of a range of purposes for which levies may be spent, such as research, product development, market development, promotion, animal health, quality assurance, education and training and administrative expenses.

Advantages
The main advantages of this approach are that:

- many of the features of the Commodity Levies Act are designed to promote accountability, such as the requirement for those who pay levies to agree to their imposition (and periodically agree to their retention), the limitation of areas where levies can be spent and the requirement for organisations receiving levies to be representative of levy-payer interests;
- the legislation provides sufficient flexibility for the scope and role of organisations to be tailored to the interests of producers. For example, the full range of options from a series of independent agencies each addressing a single objective, to an umbrella organisation undertaking a number of roles is possible. These structures could change over time;
- the roles and functions of the organisations could evolve over time without the need for new legislation;
- specific statutory prohibitions on the agencies engaging in certain activities will provide confidence to private investors and producers; and
- existing legislation could be adopted to serve producer interests. Producer-funded organisations, for example, could be set up under the Companies Act. The accountability and voting procedures under that Act could be employed.
Disadvantages
The disadvantages of this approach are:

- purely voluntary funding may lead to the under-provision of certain services, although the provisions of the Commodity Levies Act are available to address this concern;
- transition to new arrangements would need to be carefully managed. This will be important in respect of the allocation of export quotas and the divestment of assets with a commercial value, such as brands, meat and wool classifications and commercial subsidiaries etc;
- the option to secede may be used as a strategic weapon to distort the activities of a producer organisation for the benefit of the well-organised few against the interests of a majority of levy payers. This is also a risk under the other options, and could be addressed through statutory protections against oppressive conduct;
- higher costs from the duplication of services might result if levy payers who wish to secede do not meet full administration and set-up costs. The range of activities of any producer-funded entity would be defined in its constitution; and
- the Commodity Levies Act retains the power to coerce producers to purchase levy-funded services where they might consider it not worth their while.


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