

creating opportunity



Government of South Australia

Department of Trade and Economic
Development

Guidelines for Quantifying Savings from Red Tape Reduction Initiatives

**Office of the Economic Development Board
Revised April 2009**

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1. Introduction

In light of the success of the initial Red Tape Reduction Program, the Competitiveness Council recommended to the Treasurer that the program be extended to allow the government to cut deeper into the stock of red-tape, and to effect further positive change on the competitiveness of the SA business environment.

In response to the Economic Development Board's (EDB) Economic Statement the government has announced a new target of a further \$150 million reduction in red tape over three years. A key part of meeting this target will be a rolling five-year review of all business regulation.

With this in mind, these guidelines have been revised to assist agencies in planning and delivering a second phase of reductions. Specifically, the changes include revised savings calculations (e.g. hourly rates of pay), and the inclusion of an overview of the more generic strategies pursued across the sector during phase one.

As in the first round, our focus is on ensuring a consistent and objective approach to savings calculations, and as such, the Business Cost Calculator (BCC) should continue to be used to calculate cost savings wherever possible.

Additional methodologies have again been included, in recognition that the BCC is not always appropriate.

2. Background

On 5 March 2006, the Premier made a public commitment that by July 2008 the government will have reduced State Government red tape by at least 25% and markedly reduced business compliance costs.

The Competitiveness Council was established in June 2006 as a sub-committee of the Economic Development Board (EDB) to identify, develop and champion practical initiatives to enhance South Australia's competitiveness, both nationally and internationally. In its first term, the council focused its attention on State Government achieving the red tape reduction target.

As a result of the significant efforts of agencies across the sector, we were in a position to report that the government had demonstrably reduced red tape and in fact, exceeded the 25% / \$150m target set for July 2008.

Following this success, and consistent with recent feedback from Business SA that red tape remains a key issue for SA business, the government has recognised the benefit of conducting another round of the program and establishing a new target.

For this round, DTED intends to utilise the existing plan formats to document agency initiatives and monitor their progress. Again, plans are expected to clearly identify objectives, timeframes and measurable outcomes, including the cost savings to business in terms of reductions in time or cost, for each initiative within the plan.

3. Definition of red tape

As a first step it is important to understand what is to be measured. A broad working definition of 'red tape' adopted by the Competitiveness Council is:

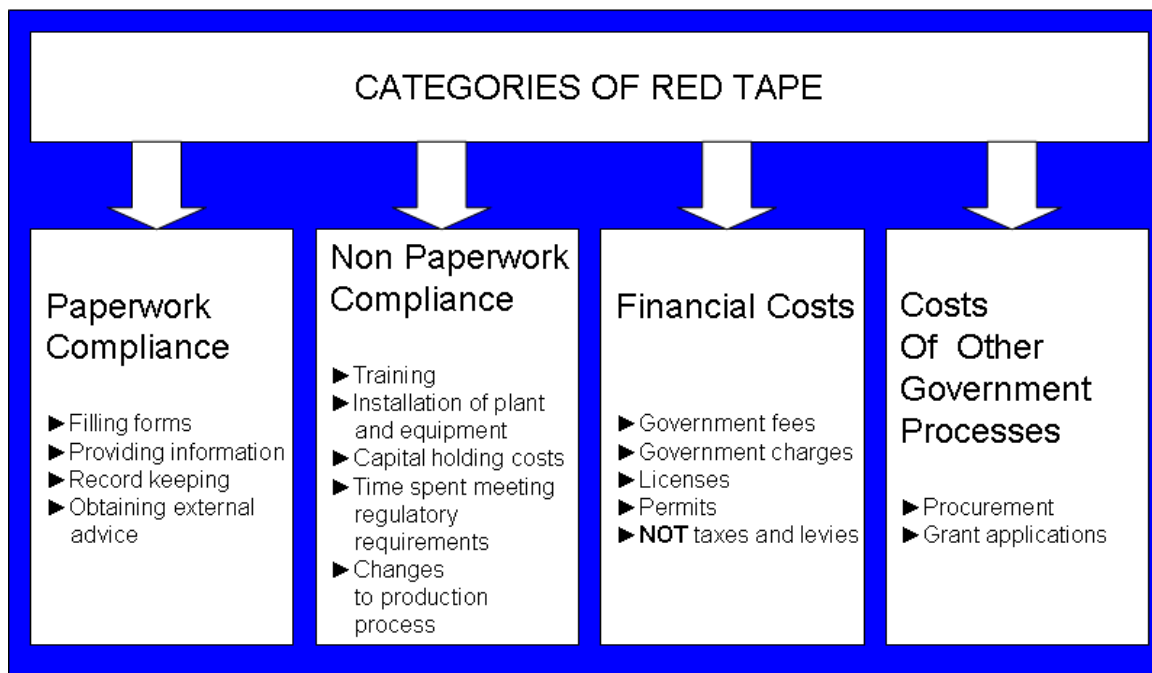
"The time and money spent by businesses to understand and comply with government regulations, and related processes, that are above and beyond the daily costs of running a business."

Importantly, the Competitiveness Council acknowledges that 'regulation is essential for the effective functioning of our society and economy'¹ and that measures that are demonstrably delivering benefits to the community which outweigh the costs of the regulation are not within the scope of the program.

For the purposes of implementing the Red Tape Reduction Program, the Competitiveness Council is once again asking agencies to identify regulation that is redundant, non-essential or inefficient, including mandatory requirements, procedures, processes, forms, licences and regulations that add to the cost of doing business and dealing with government. This could include anything obsolete, redundant, cumbersome or confusing that diminishes South Australia's competitiveness and stands in the way of job creation

In recognition of the contribution of not-for-profit organisations (NFPs) to the SA economy, the measurement of the impact of red tape on the business community will be formally expanded in this round to include the impact on NFPs. This group is further defined in Appendix B

There is some variation in the scope of regulatory reform across jurisdictions, and the term 'red tape' is often used interchangeably with the term 'regulatory compliance burden'. For the purposes of the SA Red Tape Reduction Program, figure 1 below shows the main cost categories defined by the Productivity Commission. Further detail on each of these categories is contained in sections 3.1 - 3.4:



3.1. Paperwork compliance costs

These costs include:

- ▶ The costs imposed on the administrative structures of a business due to filling out forms and providing information.

¹ "Performance Benchmarking of Australian Business Regulation", Productivity Commission Research Report, 19 February 2007

- ▶ Also included are other administrative costs, such as record-keeping and obtaining advice from external sources (such as accountants and lawyers), which arise in the course of providing information in accordance with regulatory requirements.

3.2. Non-paperwork compliance costs

Non paperwork compliance costs are those costs associated with any non paperwork activities undertaken as a result of having to comply with regulations. Examples of such costs include:

1. Changes to production processes that increase costs such as mandatory labelling requirements, building rules etc.
2. Higher input prices.
3. Additional human capital investment (staff training and education) and physical investment costs (re-configuration of plant and equipment), as well as the costs of modifying output, to conform with regulations;
4. 'Capital holding' costs associated with regulation-induced delays in business activities and projects;
5. Time spent in meeting regulatory requirements, such as undergoing audits and inspections of premises or processes; and
6. Costs associated with dealing with inconsistent and duplicative regulation across jurisdictional boundaries, or within SA itself.

Non-paperwork compliance costs that impact on administrative costs, together with paperwork compliance costs can be defined as the **administrative compliance costs** attributable to regulation.

It is recommended that the Productivity Commission's categorisation, as defined above, be used to the extent that it is practical, to ensure consistency between the SA Government's Red Tape Reduction Program and the Productivity Commission benchmarking program.

However, the following compliance costs and activities are also included within the above definition of 'red tape' and are therefore within scope for the current exercise.

3.3. Financial costs

In addition to the above compliance costs, there are also costs that are the result of a concrete and direct obligation to transfer a sum of money to the government or relevant authority. Such costs include government fees and charges, including permit and licence fees, but not taxes and levies. Licence fees and other charges are required to recover the costs incurred by Government in regulating activities. If a regulatory activity is no longer required or can be made to operate more efficiently than any consequent reduction in the need for cost recovery should flow through to business as a reduction in the extent, nature or level of fees and charges imposed.

3.4. Costs associated with other government processes

Requirements on businesses that stem from administrative processes set by government that are unnecessarily burdensome - e.g. procurement processes, grant applications, payments systems. These costs also include the accessibility of government information insofar as the difficulty in obtaining necessary information creates a barrier or delay for business.

The Business Cost Calculator can be used to measure all regulatory costs as described above, as well as other administrative costs. However, guidance is required for measuring savings to business from improvements associated with 'other government processes' in particular.

4. Guiding principles

Overall feedback from the auditors involved in the first round of reductions was positive in relation to agencies application of the methodology for reduction value measurement, hence the guiding principles will be retained:

1. The methodology should be able to be justified by the individual agencies on the basis of reasonableness. However, particular emphasis should be placed on the maintenance of objectivity and independence.
2. Where possible, independent (eg ABS) or industry body figures should be used for any assumption or baseline figures. This also allows for an objective measure to be used. Where the auditor identifies differing methodologies used to value similar activities, the auditor will give DTED guidance as to which methodology is the most appropriate. Using this advice, DTED will decide upon the most appropriate methodology and that methodology will be applied consistently across the whole program.
3. The methodology should be applied consistently within an agency, and preferably across all agencies.
4. Where an estimated benchmark figure is used, it should, where possible, be based on historical figures and adjusted, where appropriate, for the forward trend. The basis of forward projections needs to be documented and retained for audit purposes.
For example, if the growth in applications over the past 5 years was a consistent 5 per cent per annum, then it would be reasonable to use an assumption of 5 per cent growth for the upcoming year, unless there is awareness of a specific factor that will otherwise influence the outcome.
5. Only costs directly attributable to a cost saving initiative should be counted.
6. Additional costs to business associated with any new related initiatives should be factored into the overall cost savings to derive a net amount.
For example, where a fact sheet is produced to explain a new process, the time taken for a business to read, understand and conform to the process should be factored into cost saving calculations.
7. Amounts reported should be exclusive of GST unless savings can clearly be demonstrated
8. The end of the assessment period is April 2012. Savings will be captured from initiatives that are fully implemented by this date.
9. Where savings are being calculated for new activities and are based on a 'take-up' rate (eg. for online transactions), savings should be forecast initially using appropriate assumptions. As soon as take-up commences and real data is available, the forecast savings should be re-calculated using actual volume data.
10. Agency targets will again be annual targets. Where the effect of regulatory change is temporal, its value should be annualised over the period affected by the change. Where the effect is distributed unevenly over a period of time, the effect shall be annualised using a base of 5 years.
11. Where appropriate, a risk assessment should be conducted to ensure cost saving initiatives comply with an agency's risk management framework.
12. Finally, documentation and other evidence (eg. reports generated by the Business Cost Calculator) should be retained for audit purposes.

Where a methodology is not provided in these guidelines, then an agency should adopt a methodology which embraces the above elements. Please note - given the wide variety of initiatives undertaken in the first round, it is possible that a suitable precedent for a specific costing methodology may already exist in another agency. DTED staff are willing to assist in identifying a suitable agency contact. Please also see table 2 under section 5.1.

In selecting hourly labour rates for costing savings, the "Occupation Rates" (Table 2) should be used in the first instance. Where an agency determines that an industry rate is more appropriate, it should keep evidence to justify its determination.

5. Methodologies

5.1. Measuring administrative compliance cost per activity

Administrative costs (and therefore savings) can be calculated using the following formula:

Administrative activity cost = price x quantity

Price = tariff x time

Quantity = population x frequency

Tariff - there are two types of tariffs: internal and external:

1. internal tariff is the hourly costs (gross wage costs plus on-costs and overheads) for activities done internally
2. external tariff is the hourly costs for external service providers.

Time is the amount of time (in hours) taken to perform the activity or activities which are no longer required to be undertaken as a result of the red tape reduction initiative.

Population is the number of businesses and not-for-profit organisations affected. This may include multiple business outlets that form part of a single business entity, where the regulatory activity impacts at that (lower) level.

Frequency is the number of times that an activity must be performed each year.

Essentially this means that the administrative costs are related to the time and wage costs that a business spends in carrying out a particular activity. This is multiplied by the number of businesses affected and the frequency with which they have to perform that activity.

The BCC does this calculation by requiring the following information to be entered:

1. The number of businesses that will undertake the particular compliance activities
2. The number of employees per business that will undertake the activity
3. How long the activity will take and how often it will have to be done
4. Who will perform the task and the associated labour cost/purchase cost

As noted above, the BCC does allow for other regulatory costs to be entered to estimate the total compliance costs associated with a particular compliance activity.

Key areas that can be considered when trying to reduce administrative costs are summarised in Table 1.

Table 1: Four main areas to be considered when trying to reduce administrative burden

Areas	Definition	Options for reducing the burden	Key questions
Population	The number of businesses as to which the regulation applies	<ol style="list-style-type: none"> 1. Raising the threshold for a particular requirement 2. Changing the coverage of a regulation, e.g. by taking a particular group out of scope 3. Using a risk-based approach to regulation to minimise scope of affected parties 	<ol style="list-style-type: none"> 1. Can obsolete regulations or information obligations be removed altogether without affecting the policy outcomes? 2. Can better targeting be used to remove information obligations from businesses of a particular size

			particular sector or particular risk profile?
Frequency	The number of times that business has to respond to a data requirement during a year	<ol style="list-style-type: none"> 1. Reducing the frequency when data must be submitted by a business 2. Reducing the frequency for certain groups (by adopting a risk-based approach to inspection) 	<ol style="list-style-type: none"> 1. Can intervals be increased across the board? 2. Can certain groups be targeted less often?
Time	Amount of time that it takes business to perform a certain activity	<ol style="list-style-type: none"> 1. Making a form easier to fill out, pre-populating forms or e-enabling 2. Clarifying requirements in plain English 3. Producing guidance that informs business of the minimum requirement - ensure that they are not over-complying with the regulation due to a lack of clarity about what is expected (known as regulatory creep) 4. Identifying synergies between existing processes to reduce duplication of effort 5. Reducing the amount of information requested 6. Implementing a streamlined process for lodging nil returns 	<ol style="list-style-type: none"> 1. Can data requirements on a given form be reduced or can forms with overlapping data requests be merged or reduced in length to avoid duplication? 2. Can forms be simplified, better designed or pre-populated, to make them easier to complete? 3. Can online submission and/or transactions reduce the burden? Are there other options to facilitate transactions (eg. Austpost, Bpay etc) 4. Can better advice or guidance be used to reduce the time taken to understand regulations and data requirements? 5. Can pro-formas be issued to help business comply with regulations? 6. Can standard data definitions be introduced to allow departments to share data and businesses to use the same information more than once? 7. Is all information requested actually used and if so how and why? 8. Could the information requested be obtained elsewhere?
Tariff	The wage of the employee who performs the admin activity, cost of outsourcing activity, including on-costs and overhead costs	<ol style="list-style-type: none"> 1. Changing the seniority of who is required to perform the admin activity. 2. By simplifying the requirement and providing clear guidance, someone within the business may be able to perform the activity, without the need to engage a specialist. 	<ol style="list-style-type: none"> 1. Can simplification of the administrative activities associated with an information obligation reduce the need for involvement of specialists or key staff? 2. Is there scope to remove the need - real or perceived- for business to bring in specialist contractors (such as legal experts or accountants) to comply with an information obligation?

Source: UK Cabinet Office (2006), Administrative Burdens - Routes to Reduction (amended)

Consistent with Table 1, the experience of the first round of reductions highlights a series of generic initiatives that have significant potential for application across multiple agencies, and/or provide opportunities to further scrutinise practices within those agencies that have already undertaken some reform.

With a view to encouraging collaboration and information sharing across agencies, the following brief summary highlights the nature of these initiatives, and some of the agencies that were successful in implementing them. In the first instance, Appendix 2 of the report from the initial phase may provide further detail of the specific initiatives implemented.

Please note that this list is not exhaustive.

Table 2 - Round 1 agency initiatives with potential for wider application

TYPE OF INITIATIVE	PARTICIPATING AGENCIES
REGULATORY APPROACH	
Review regulation to implement a risk-based approach.	<i>DFC DECS DH EPA JUSTICE WorkCover</i>
Review fees to ensure they are 'user-pays' based, and identify current cross-subsidisation practices.	<i>EPA</i>
E-FACILITIES	
Expansion of the extent of agency information provided online.	<i>DEH DTEI DFEEST DH DTED DWLBC SAWater</i>
Expansion of processes (including tendering and transactions) that are able to be completed online. This also included the modernisation of supporting systems. It is worth noting the JIBS project within Justice, and opportunities provided by Bizgate and potential Federally-brokered access to PDF-based smartforms.	<i>DEH DFC DTEI DECS DH PIRSA DTED DTF JUSTICE SAWater WorkCover</i>
Simplified Grants funding, including online applications.	<i>DFC DH DTED</i>
Expansion of other options for payment.	<i>DH DTF</i>
ACCESSIBILITY, AWARENESS & TIMELINESS	
Review of external presence (documentation, websites, forms) to ensure the use of plain English and simple location of information.	<i>DEH DTEI DECS DPC DWLBC</i>
Creation of tailored 'packages' designed to efficiently inform businesses of their obligations or the procedures they must undertake.	<i>DEH DPC DTED</i>
Process re-engineering to reduce waiting times/duplication.	<i>DTEI PIRSA EPA</i>
Increasing the duration of licenses or the time between audits.	<i>DECS DH PIRSA EPA</i>
Reducing duplication by using business supplied data for multiple related processes, or for pre-populating forms.	<i>DTEI PIRSA JUSTICE</i>
Harmonising processes with other jurisdictions and/or the Commonwealth to reduce delays/duplication.	<i>DH PIRSA</i>
PROCUREMENT	
Website publishing of forward procurement plans.	<i>DFC</i>
Increasing thresholds applying to different procurement activities, including purchasing and tendering.	<i>DECS DH DTED JUSTICE LMC</i>
Standardising Tender and Contracting Processes, (including simplified processes for repeat purchases).	<i>DFC DTEI DECS DFEEST DH DTED DWLBC LMC</i>
Increased use of purchase cards.	<i>DFC DFEEST DPC DTED</i>

In the case of land developers, delays mean a longer development phase and either payment of more interest on borrowed funds or loss of the opportunity to earn interest on their own capital.

There are three possible cost categories in relation to land subject to a development approval:

1. **Land holding costs** - if a project costs \$10m and \$5m of this has already been incurred, then if the development application takes two months longer than reasonable, there is a holding cost on the \$5m already borrowed and/or spent.
2. **Administrative costs** - additional professional and management time associated with extra detailing of plans, amendments to plans and following up on the status of an application. This extra labour time input is often part of the time delay as government officers seek detailed explanations or changes, which may be quite costly.
3. **Cost of uncertainty** - extra time may imply extra uncertainty and could raise the price of debt (interest rate) to developers. Savings to business from removing the cost of uncertainty should only be calculated where agencies can demonstrate a direct link between a red tape reduction initiative and reduction in the price of debt. DTED is available to provide assistance in determining if there is a direct link.

Savings in holding costs achieved through initiatives to reduce unnecessary delays will need to be assessed on a case by case basis. However, they can be measured using variations of the following formula:

$$\text{Annual savings in land holding costs} = \frac{(\text{annual capital value of approvals} \times \text{estimate of percentage borrowed/spent prior to approval} \times \text{annual interest rate}) \times \text{reduction in time (in days) to process or gain approvals}}{365}$$

Where an interest rate is used to calculate costs, the average of the "Reserve Bank weighted-average interest rate on credit outstanding for small businesses" and the "Reserve Bank weighted-average interest rate on credit outstanding for large businesses" will be used as the benchmark interest rate.

As at December 2008, the benchmark interest rate = the average of the "Reserve Bank weighted-average interest rate on credit outstanding for small businesses" (8.5%) and "Reserve Bank weighted-average interest rate on credit outstanding for large businesses" (6.5%).³ Therefore a benchmark rate of 7.5% should be used for all valuations. This rate will be updated before the final round of reporting and at that point, all calculations using interest rates will have to be updated to reflect those rates.

This methodology should be applied consistently within an agency, and preferably across all agencies.

Measuring capital costs and amortisation

Where capital costs are necessarily incurred to specifically meet government requirements, they should be costed separately and not included as overhead costs. The capital costs should also be amortised over the expected life of the capital item. For simplicity, agencies should apply a straight-line method of amortisation.

One-off costs

"One-off costs" should be differentiated from capital costs. One-off costs are not capital in nature and would not result in an asset which has a long-term useful life for the purchaser. These are only incurred once by a business, generally when complying with a regulation for the first time. An example of such a cost would be a one-off registration fee.

³ <http://www.rba.gov.au/Statistics/Bulletin/F05hist.xls>

Opportunity costs

Opportunity cost is the cost of an opportunity foregone, or the cost of giving up Option A, to pursue Option B. There are numerous potential opportunity costs to business, for example, the costs associated with delays in government approval processes. Improving timeframes for approvals, such as issuing a licence, may allow a business to open or expand quickly and generate revenue as a result.

In principle, opportunity costs are legitimate costs. In practise, it is difficult to estimate and apply an accurate and consistent measure across the business sector due to the number of assumptions, variables and unknowns.

Where an agency is able to identify and measure opportunity costs, they should be included and labelled as such. Agencies should assess this on a case by case basis.

By way of example, the EPA included initiatives in its plans that incorporated the opportunity cost associated with reducing delays in approvals or the availability of factors of production. It used ABS Manufacturing Industry statistics for 'industry value added' to estimate the cost savings presented by a reduction in approval timeframes (Agencies may also consider costs such as 'holding costs' or 'retainer fees' to be pertinent to their estimates, however in this instance the EPA deliberately focussed on 'deferred profits' rather than costs relating to existing financial commitments). In that particular instance, the ABS data was important because of the lack of access to detailed company information. An assessment of the reliability of the calculations and in particular, the suitability of the statistics was undertaken by the EPA as part of the inclusion of the initiative in its plan.

DTED is available to assist with assessing the opportunity costs of individual initiatives.

5.3. Measuring financial costs

A reduction in financial costs can be achieved where the regulatory reform can reduce cost recovery requirements through:

1. Eliminating the need for licenses or permits, and the associated fees
2. Reducing the frequency of licence renewals without increasing the licence fee while maintaining cost recovery
3. Restructuring the licence fee while maintaining cost recovery.

These savings will provide direct benefits to business and are easily measured. They should be identified separately from estimated administrative compliance cost savings. The following formula may be useful in ascertaining financial costs:

Annual financial costs = Cost of fee/licence/permit X number of businesses affected X number of times that the fee/licence/permit is required to be paid per year

5.4. Measuring costs associated with other government processes

Procurement procedures and standardised tender documents

Savings to business suppliers can be achieved through use of simplified and standardised procurement documents, particularly for 'simple purchases'.

Standard procurement documents have been prepared and these will be mandated for use across government from 1 July 2009.

A particularly relevant Procurement Good Practice Guide⁴, developed by the Government Reform Commission was released in August 2007. It should be used to audit current processes for compliance, as experience from the first round of red tape reductions highlights that procurement may yield potentially significant savings.

Savings from tenders

The savings from simplified tender documents and use of standardised contract templates can be measured using the following formula:

$$\text{Annual savings} = \text{number of tenders called per annum (a)} \times \text{estimate number of tender respondents per call} \times \text{estimated time saved per tender respondent} \times \text{hourly rate}$$

A further tender related saving that can be initiated is raising the threshold above which formal tenders must be called. This will have the effect of reducing the number of tenders called per annum (a) above. The formula for calculating this saving is as follows:

$$\text{Annual savings} = (\text{number of tenders called per annum under old threshold} - \text{number of tenders called per annum under new threshold}) \times \text{estimate number of tender respondents per call} \times \text{estimated time saved per tender respondent} \times \text{hourly rate}$$

Agencies will need to test with their suppliers the potential time savings achieved by making it quicker and easier for suppliers to submit a tender. After consultation with its suppliers, one agency has estimated that the potential savings could be as high as eight hours per respondent.

Use of a standard contract could also reduce the need for suppliers to seek legal advice each time they respond to, or win a tender with a resultant saving in legal fees.

The above formula can also be used to calculate the savings from ensuring electronic collection and lodgement of all public tenders.

Providing the facility for businesses to electronically submit tender proposals through the SA Tenders website could also be considered.

Advice to the supply community of forward procurement requirements

It has been suggested that savings may be possible from providing regular on-line updates of forward procurement requirements. This may be a time saving to business, although there would need to be clear evidence that such savings will be generated.

Annual saving = number of annualised acquisitions in forward procurement plan x estimated respondents per acquisition x estimated hours saved per respondent x hourly rate.

Publishing information on a forward procurement plan will give business advance notice of the timing of tender processes and commencement of projects and enabling better workforce and business process planning.

Maximise e-ordering

Savings associated with increased use of electronic catalogues can be calculated using the following formula:

$$\text{Annual Savings} = \text{estimate of transactions processed on line per annum} \times \text{estimated time saved per transaction} \times \text{hourly rate}$$

⁴ <http://www.spb.sa.gov.au/documents/Procurement%20Good%20Practice%20Guide.PDF>

Increased use of purchase cards as a payment mechanism

Use of debit or purchase cards by government agencies may be considered for use for purchases of up to (by way of example) \$2,000. Savings could be accrued on costs of paper, printing, assembly, postage, delivery, filing, storage, following up on outstanding accounts and interest on working capital as a result of immediate payment; although agencies will need to take into account the costs associated with setting up an e-invoice system and training and other costs.

$$\text{Annual Savings} = (\text{number of invoices processed annually with value less than } \$2,000) \times (\text{increase in the percentage of payments to be made by purchase card}) \times (\text{dollar savings per transaction}) + (\text{Cost of capital saved through receiving immediate payment}) - (\text{Bank merchant fees})$$

Increase the payment options for business

Consideration could also be given to introducing B-pay and credit cards to provide business customers with additional payment options.

Other e-application processes

Improve agency websites to make them more accessible for business, including:

- ▶ Providing on-line information on government programs and grants and allowing businesses to apply for grants on-line:

$$\text{Annual Savings} = (\text{number of grant applications per annum} \times \text{estimated on-line take up rate}) \times (\text{time saved through on-line searching per application}) \times (\text{hourly rate}) - (\text{Cost of setting up E-application process} \times \text{amortisation rate})$$

The amortisation rate should be based on the e-application's useful life which can be calculated based on the length of time the e-application is anticipated to operate before a major upgrade is required.

- ▶ Provide for seminars, workshops and other bookings to be made on-line.
- ▶ Allow licence and permit fees to be paid on-line.

Plain English initiatives

Ensure all documents (e.g. publications and fact sheets) and forms issued to customers/suppliers or published on websites are written in plain English. Ideally, documents and forms should be 'road tested' for plain English before release.

$$\text{Annual Savings} = (\text{saving in time/form}) \times (\text{estimate of forms received per annum}) \times (\text{hourly rate})$$

Improving communication with business

Make information more accessible and easy to understand. This could include telephone and internet services, programs to enhance awareness, and process improvements to reduce time spent handling interactions with customers. Extend the term and allow for multiple renewals, where appropriate.

Reduce data and information demands from business and the community, by developing central reporting tools and increasing the sharing of information (subject to privacy issues).

Simplify funding and submission processes for business and NFPs, by the development of standard templates, policies and procedures.

Appendix A: Methodology for deriving default hourly labour rates

Purpose of this note

The purpose of this note is to provide a suggested default methodology to be used in developing an hourly labour rate for use in valuing staff time, in the absence of more specific data.

The default methodology will help agencies to value staff time in a more objective and consistent manner when using the Business Cost Calculator to estimate compliance costs and savings. The most up to date statistics available from the ABS have been used for these calculations, with catalogue numbers noted accordingly.

Suggested default methodology

The suggested methodology for calculating the hourly labour rate is to divide the estimated annual cost of employing labour (including wages and on costs) by the estimated hours worked per year. Each element of the methodology, suggested default values and other alternative values are discussed below.

Formula

$$HR = AE / (AW * AH) * ON * OH$$

HR = hourly rate

AE = average annual earnings

AW = number of weeks worked per annum

AH = average weekly working hours for full-time adult workers

ON = on-cost multiplier

OH = overhead multiplier

Earnings

Detailed and more precise data on earnings for certain industries and/or employment types is available from a number of sources, such as internal accounting systems, industry salary surveys and detailed ABS earning data on specific industries/occupations. Wherever feasible specific data sourced from these areas should be used.

Appropriate economy-wide average weekly earnings data is available from the Australian Bureau of Statistics (ABS). This data is based on business surveys that provide quarterly statistics on average weekly earnings classified by sector (private and public) and state or territory for males, females and persons.⁵

In the absence of detailed earnings information it is suggested that latest data from ABS Catalogue No. 6302.0, *Average Weekly Earnings Australia* be used as a default measure. For example, the latest estimate of Average Weekly Earnings for November 2008 (South Australia, persons, full time, adult, ordinary time earnings, trend series) was \$1,100.40; so average annual earnings (AE) equals \$57,220.8.⁶

Weeks worked

To get a figure for the number of hours worked per annum it is necessary to identify: first, the number of weeks worked per annum; and secondly, the standard hours worked per week. The number of weeks worked per annum can be derived by removing annual leave, public holidays, sick leave and any other leave entitlements from the number of weeks in a calendar year.

⁵ ABS Cat. No. 6302.0 "Average Weekly Earnings" trend series.

⁶ Using average annual earnings (SA, persons, full time, adult, ordinary time earnings) assumes that the ratio of male: female employees in the average entity is identical to that in the wider economy. Given differences in male and female earnings, if an entity/industry had a significantly different ratio of male: female employee this assumption may under or over state the wage cost for that entity/industry.

The ABS release, *Labour Price Index: Concepts, Sources and Methods 2004*,⁷ notes that the legislated minimum paid annual leave entitlement is 4 weeks (although this can vary across jurisdictions and casual workers are excluded). In SA, there are 10 statutory public holidays which is equivalent to 2 weeks. While acknowledging that paid sick leave is a legitimate component of total labour costs, numerous attempts by the ABS to construct the annual quantity of sick leave taken by the 'average' employee have failed. Additionally, a business is not usually required to provide the full entitlement of sick leave.

The assumption used here is that the average use of sick leave entitlement is 1 week per annum. Other types of paid leave such as maternity/paternity leave and long service leave are not applicable to every employee and difficult to average out, thus being excluded.

The assumption used for **average number of weeks worked per annum** is therefore **45 weeks**.

Hours worked

The hours worked by employees in a particular sector or firm should be used to estimate staff or individual time wherever possible. The ABS publication, *Australian Social Trends 2006*,⁸ defined a "standard week" as between 35 - 40 hours per week. It found that the average weekly hours worked by all Australian workers in 2005 was 34.7 hours and the average weekly hourly worked for full-time workers in 2005 was 41.9 hours. In the absence of any specific data, the assumption used for **average weekly working hours** is **41 hours**.

On-costs

On-costs are additional non-earnings labour costs borne by employers and include employer superannuation contributions, payroll tax, workers compensation premiums and fringe-benefit tax. Internal accounting systems should provide comprehensive information on on-costs for individual entities.

More generally, based on data in the ABS *Labour Costs 2002-03*⁹, superannuation, payroll tax, workers compensation and fringe benefit tax costs in South Australia in 2002-03 were 15.7% of earnings.

Overhead costs

Overhead costs include items such as building costs (floor space, rentals etc), telephone costs, electricity, IT equipment and support, and administrative support.

Based on the experience of a number of European countries who use the Standard Cost Model to determine the administrative burden imposed by regulation, the auditors for round 1 recommended adopting an overhead percentage of 25% to cover on costs.

For consistency, an overhead percentage of 25% can be applied to default hourly rates. An alternate overhead percentage may be adopted by an individual agency where that agency can demonstrate clearly and reasonably that it is appropriate to adopt an alternate overhead percentage.

⁷ ABS Cat. No. 6351.0.55.001

⁸ ABS Cat. No. 4102.0 "Trends in Hours Worked"

⁹ The most recent published data with on-costs broken down by state/territory. ABS Cat. No. 6348.0.55.001

Labour rate calculation example

If using the May 2008 ABS data from *Average Weekly Earnings*, the hourly labour rate for a given activity is:

$$\begin{aligned} \text{HR} &= \text{AE} / (\text{AW} * \text{AH}) * \text{ON} * \text{OH} \\ &= \$57,220.8^{10} / (45 * 41) * 1.157 * 1.25 \\ &= \$31.01 * 1.157 * 1.25 \\ &= \$44.85 \end{aligned}$$

Where:

AE = average annual earnings (persons, full-time, adult, ordinary time earnings)
= \$1,100.40 * 52 weeks
= \$57,220.80

AW = number of weeks worked per annum = 45

AH = average weekly hours for full-time workers = 41

ON = on-cost multiplier = 1.157

OH = overhead multiplier = 1.25

Table 3 provides alternative hourly rates by occupation and industry in the State by adjusting the above default hourly rate based on national occupational and industrial relativities.¹¹

¹⁰ Or use of "detailed earnings" if available.

¹¹ Using ABS Cat. No. 6306.0 Employee Earnings and Hours May 2006 data to calculate national occupational and industry relativities.

Table 3: Alternative hourly rate by occupation and industry

Economy-Wide	Default Hourly Rate	
	Excluding Overheads	Including Overheads
	\$35.88	\$44.85
By Occupation	National Relativity to Default Hourly Rate	Alternative Hourly Rate
Managers	141%	\$63
Professionals	119%	\$53
Technicians and trade workers	96%	\$43
Community and personal service workers	85%	\$38
Clerical and administrative workers	82%	\$37
Sales Workers	74%	\$33
Machinery operators and drivers	94%	\$42
Labourers	79%	\$35
By Industry	National Relativity to Default Hourly Rate	Alternative Hourly Rate
Mining	162%	\$73
Manufacturing	97%	\$44
Electricity, gas and water supply	128%	\$57
Construction	102%	\$46
Wholesale trade	94%	\$42
Retail trade	73%	\$33
Accommodation, cafes and restaurants	73%	\$33
Transport and storage	103%	\$46
Communication services	110%	\$49
Finance and insurance	124%	\$56
Property and business services	105%	\$47
Government administration and defence	103%	\$46
Education	107%	\$48
Health and community services	101%	\$45
Cultural and recreational services	93%	\$42
Personal and other services	91%	\$41

► Figures have been rounded

Appendix B: Definition of not for profit organisations (NFPs)

In accordance with the ABS (8106.0), Not-for-profit organisations (NFPs) are legal or social entities, formed for the purpose of producing goods or services, and whose status does not permit them to be a source of income, profit or financial gain for the individuals or organisations that establish, control or finance them.

Some broader discussion which may assist in the practical application of this definition: (taken from ABS 1301.0)

Non-profit organisations are, first of all, organisations. This means that a non-profit organisation will have a set of rules or a constitution that gives it a life beyond the group that began it. Non-profits may be incorporated, a legal term meaning that the organisation has a legal identity independent of its members. Larger non-profits, which employ people, are incorporated in most instances. However, the great majority of non-profits, which are small and rely entirely on volunteer behaviour, are not incorporated.

Secondly, non-profit organisations are private organisations; that is, they are not directly subject to government control or direction. This does not mean that governments do not try to regulate and direct their behaviour. They do, especially when they provide a large component of a non-profit's operating revenue. However, governments try to regulate the behaviour of for-profit organisations as well. The key tests of whether an organisation is private or part of government are whether it is subject to ministerial direction and whether its actions are subject to the same parliamentary scrutiny as are the actions of government departments.

Thirdly, as the name indicates, they operate on a 'not-for-profit' basis. While in some respects they are like private, for-profit companies, they differ from the latter in that they do not distribute any surplus or profit they might make to their members. This characteristic, part of the definition of a non-profit, does not mean that non-profits do not finish each financial year with a small excess of income over expenditure, or profit; most of them do. Like any private organisation, if a non-profit did not make a surplus in most years it would soon cease to exist. It does mean, however, that making the largest possible profit is not, and should not be an objective of the organisation.