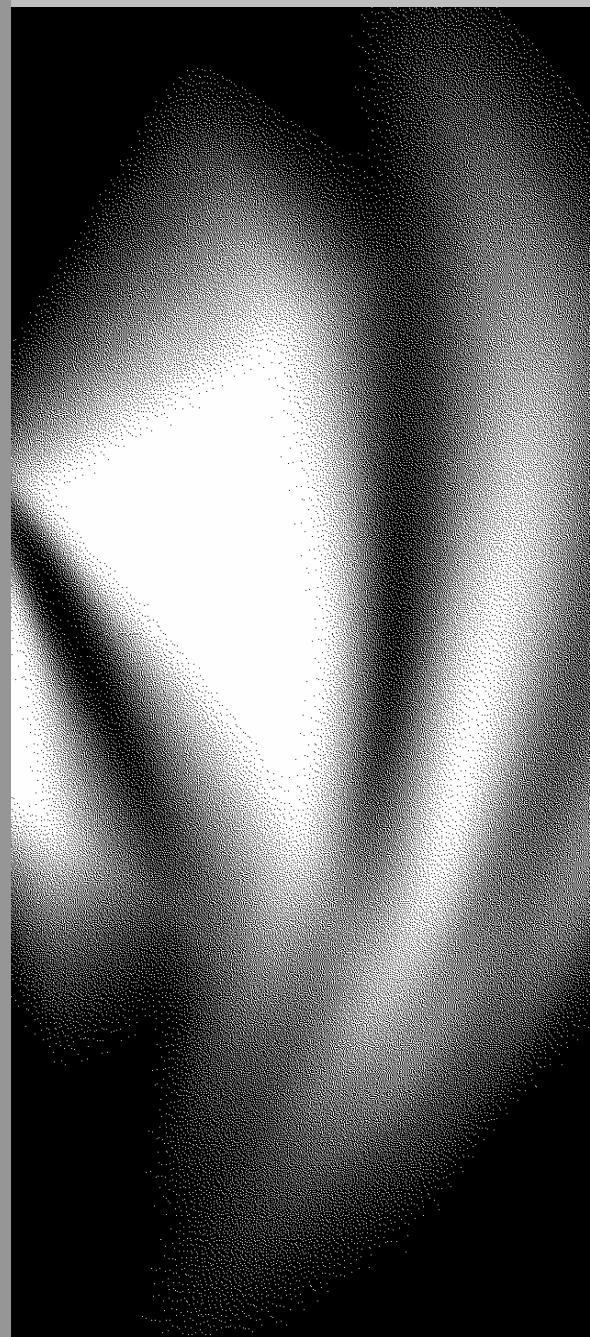




Performance Benchmarking of Australian Business Regulation

Productivity
Commission
Research Report
Overview

19 February 2007



OVERVIEW

Key points

- While much business regulation is essential, it can involve unnecessary compliance costs. Such burdens are compounded for firms operating across Australia.
- Benchmarking compliance burdens could help identify where costs could be reduced, and complement other regulatory reform initiatives.
- Such benchmarking is technically feasible and could yield significant benefits. However, there are methodological complexities and uncertainties about data, requiring a careful, staged approach to implementation.
 - Benchmarking across jurisdictions would need to be confined to areas of regulation with comparable objectives and benefits, and rely mainly on indirect indicators that would not be definitive about performance gaps.
- Benchmarking *compliance costs* of key regulatory areas should include the costs of:
 - *becoming and being* a business, arising from one-off activities such as licensing and ongoing activities such as meeting OHS standards;
 - the delays, uncertainties and compliance activities associated with obtaining government approvals in *doing business*; and
 - regulatory duplication and inconsistencies in doing business *interstate*.
- In addition, benchmarking the *quality and quantity* of regulation across jurisdictions and over time (including for specific business categories) would provide complementary insights into cumulative burdens and systemic problems.
- It would be desirable to follow a limited and targeted program over the first three years, that would allow 'learning by doing'.
 - The first year would focus on benchmarking the quantity and quality of regulation, as well as compliance costs for a single area of regulation, and developing data sets for other areas. Progressively more regulation would be benchmarked in subsequent years.
- Based on the likely significance of compliance burdens and other criteria, suggested priorities for inclusion in the initial three year program are OHS; land development assessments; environmental approvals; stamp duty and payroll tax; business registration; financial services regulation; and food safety.
- Data for many indicators is obtainable from published sources and governments, but face-to-face surveys of individual businesses would also be needed.
 - Survey costs, including for business, can be reduced by targeting 'reference businesses' with appropriate attributes.
- The cooperation and support of governments and business – in advising on indicators and supplying comparable data – would be crucial to the success of any regulatory benchmarking program. Advisory panels would facilitate necessary interaction.

Overview

Regulation is essential for the effective functioning of our society and economy. However, most regulation involves costs as well as benefits. In recent years, business groups have been increasingly vocal in their concerns about the costs of complying with regulation ('red tape'). This concern has not been mostly about the objectives of regulation, but about perceived unnecessary costs stemming from how regulation is designed and implemented.

The Regulation Taskforce established by the Australian Government concluded that benchmarking across jurisdictions could assist in identifying unnecessary regulatory burdens. The Council of Australian Governments (COAG) subsequently agreed in-principle to the development of a common framework for benchmarking, measuring and reporting on the regulatory burden on business (COAG 2006a).

This study was commissioned to assist COAG with its benchmarking initiative. It comprises two stages. In this first stage, the Productivity Commission has been asked to assess the feasibility of performance indicators and framework options for benchmarking, measuring and reporting on business regulatory burdens. Subject to COAG's endorsement, the Productivity Commission would proceed with the benchmarking in the second stage of the study.

Why benchmark regulatory regimes?

Compliance burdens are substantial

While difficult to estimate with any precision, evidence from the Regulation Taskforce and other sources indicates that business red tape burdens are substantial and have grown over time. Significant costs arise for businesses operating within individual jurisdictions, but costs are compounded for firms operating across jurisdictional boundaries.

Modelling work undertaken by the Productivity Commission for COAG suggests that the economic gains from reducing such compliance burdens could be large. For example, if regulatory reforms lowered compliance costs by one-fifth from

conservatively estimated levels, a cost saving of around \$7 billion (and a greater resultant increase in GDP) could be achievable.

Red tape reduction programs overseas are also estimated to have yielded substantial benefits. The Ministry of Finance in the Netherlands, for example, estimated cumulative savings of €900 million (approximately A\$1.5 billion) over 2003 and 2004 from reduced administrative burdens on business. In the United Kingdom, it is claimed that reductions to administrative burdens obtained through the use of the Standard Cost Model will potentially increase GDP by £16 billion (approximately A\$35 billion).

Benchmarking would assist regulatory reform

Consistent with the maxim that *what is measured gets managed, and what is managed gets done*, a carefully designed and implemented benchmarking program could complement other regulatory reform efforts in pursuit of more cost-effective and efficient regulation.

There is evidence that significant differences in compliance cost levels exist across jurisdictions. For example, the Housing Industry Association claims that Occupational Health and Safety (OHS) regulation is more onerous in New South Wales than in any other Australian jurisdiction. And a survey by the Royal Australian Institute of Architects revealed considerable variation in average processing times for planning approvals across and within jurisdictions. Moreover, there is evidence of jurisdictional differences in areas of regulation where governments have already agreed that national consistency is desirable (such as building regulation).

Benchmarking could shed light on where and how such differences might be reduced. Differences in compliance costs across jurisdictions, where they are not the outcome of differences in regulatory objectives, would constitute *prima facie* evidence that unnecessary burdens are being imposed on businesses in those jurisdictions with relatively high costs.

The increased transparency afforded by benchmarking would also increase government accountability for the design, administration and enforcement of regulation. Indeed, it could help promote greater ‘yardstick’ competition among jurisdictions, whereby there is more careful assessment of regulation to ensure that it is efficient and does not disadvantage a jurisdiction’s performance.

Participants in this review were generally strongly supportive of benchmarking and the role it could play in promoting the reduction of unnecessary compliance costs on business (box 1).

Box 1 **Business support for regulatory benchmarking**

The Business Council of Australia is strongly supportive of a benchmarking process that would identify the regulatory burdens on business. Such a process should provide better information about the regulatory burdens on business and would also demonstrate the effectiveness of regulatory reform over time. (BCA, sub. DR35, p. 1)

The costs to the Australian community and to industry of current regulatory inconsistencies among jurisdictions must be addressed. For the minerals industry alone, they amount to millions of dollars every year. Benchmarking is a fundamental tool for identifying these costs and setting the agenda for nationally consistent regulatory reform. ... the Minerals Council of Australia strongly submits that your project should proceed to Stage 2. (MCA, sub. DR37, p. 2)

The Australian Bankers' Association believes that benchmarking regulatory burden and compliance cost potentially offers considerable net benefits for government, regulators and businesses. However, the costs of undertaking a benchmarking exercise would be significant. (ABA, sub. DR39, p. 5)

The Australian Financial Markets Association stated that the Commission's work on this project would be valuable and supported a prompt conclusion to enable the benchmarking process to begin in 2007. (sub. DR30, p. 1)

What are the framework options?

In principle, two types of regulatory benchmarking could be undertaken — namely, *performance* and *standards* benchmarking.

Performance benchmarking involves measuring and comparing indicators of compliance costs across jurisdictions and over time, without reference to any specific 'best practice' standard. Differences in cost-related indicators, for regulations with similar objectives, would signal the potential existence of unnecessary burdens in those jurisdictions for which the measures are significantly above the minimum.

This benchmarking technique could be used to identify potentially unnecessary burdens, and changes over time, associated with:

- administrative costs of *becoming a business*, arising at start-up from one-off activities such as entry licensing;
- administrative costs of *being a business*, arising from ongoing activities such as paying taxes and meeting OHS standards; and
- the time taken, degree of uncertainty and complexity of obtaining approvals for project-related business activity — that is, regulations that have to be met in *doing business*.

Such an approach could also be used to identify changes to the *quantity* of regulation over time, which could in turn be indicative of trends in overall levels of regulatory burden and changes to the forms of instruments being used.

Standards benchmarking involves the comparison of indicators against ‘best practice’ standards or policy targets. It can be used to identify:

- the extent and materiality of duplication and inconsistency in regulation that firms face when *doing business interstate*, particularly where governments have accepted the case for national consistency or mutual recognition; and
- the potential for unnecessary costs to arise by comparing indicators of regulatory design, administration and enforcement against accepted ‘best regulatory practice’.

In each case, a variety of indicators can be used to reflect the resource needs, timeliness, predictability and other features of regulation that give rise to compliance costs. The main benchmarking options and broad indicator categories are set out in figure 1.

Choosing specific indicators

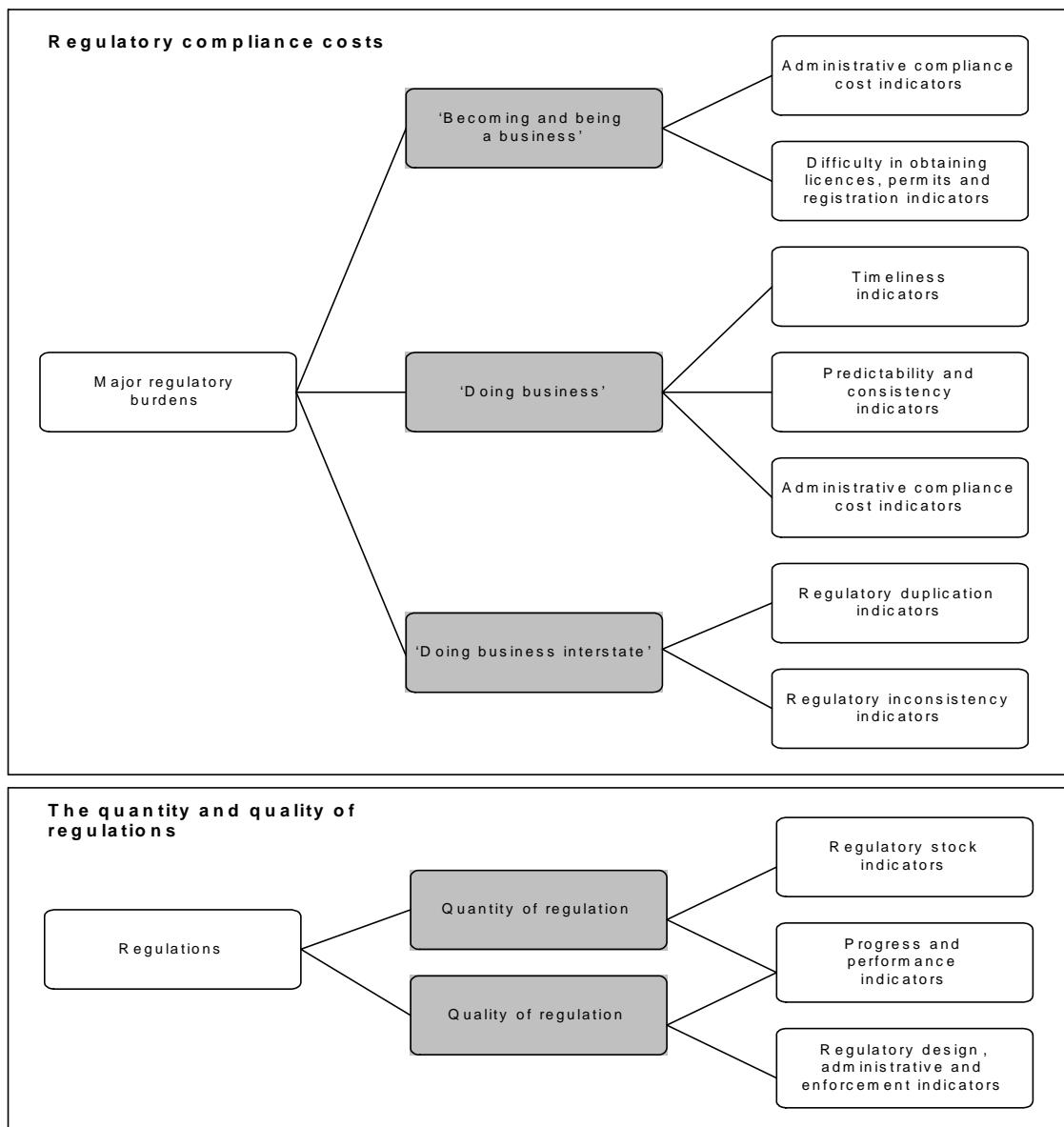
A sample of possible indicators for each of the identified benchmarking options is contained in box 2. These are drawn from a wider set of indicators outlined in this report based on their ability to reflect key aspects of potential compliance costs, while limiting data collection costs.

In practice, the final selection of specific indicators would need to be made in consultation with government and business whenever a regulation is to be benchmarked for the first time. The indicators would have to be well-defined so that they can be measured consistently. Similarly, criteria would have to be developed to assist those making subjective assessments in the case of qualitative indicators. It is also likely that indicators would have to be modified in different ways for each benchmarked regulation. Not all would be appropriate for each case and others might be needed. The aim is to identify the smallest possible number of indicators necessary to make reasonably robust comparisons.

How feasible?

There are no exact precedents internationally for a benchmarking exercise of the kind contemplated for Australia’s federation. However, a range of studies are relevant, and provide useful insights and lessons about the feasibility and value of different approaches.

Figure 1 A regulatory benchmarking framework



Surveying business effectively is crucial

A critical determinant of the robustness of the results from such an exercise is the ability to obtain meaningful, reasonably accurate data from individual businesses. In the Commission's view, personal interview surveys, while significantly more expensive than self-enumeration surveys, would be essential for some indicators of compliance costs.

Box 2 A sample of relevant indicators

Becoming and being a business

- Estimated administrative compliance costs, obtained through business interviews.
- Number of licences, permits and registrations required for business; number of agencies involved; availability of online lodgement; existence of statutory time limits on processing.

Doing business

- Time taken to process different aspects of required approvals.
- Project specific compliance costs; scope for and use of pre-lodgement procedures; speed of appeals processes.

Doing business interstate

- Number of inconsistent and duplicate requirements relative to national standard or mutual recognition.
- Expert assessment of the materiality of inconsistency and duplication.
- Activity-specific cost of having to meet additional requirements.

Changes in the quantity of regulation in total and affecting specific business types

- Number of regulations; net number of new regulations; and the number of reporting requirements.

The quality of regulation

- Use of regulatory impact statement and/or business cost calculator (or equivalent) in developing regulation; complexity that requires expertise to comply; existence of a sunset clause or other review mechanism.
- Administrative reporting requirements; accessibility to appeals processes; separation between regulation setting and administration.
- Degree of enforcement; existence of risk-based enforcement strategies; publication of enforcement outcomes.

In order to limit the costs of this approach, it is proposed to benchmark selected *reference businesses* — for which the relevant characteristics would be carefully specified to enhance comparability (box 3). While the individual businesses involved would incur costs in responding to surveys, the impost on business generally would not be great.

Box 3 **What is a ‘reference business’?**

The quantity of business regulation, and the resulting burdens, vary with types of business and their economic, financial and operational characteristics. Consequently, benchmarking comparisons of compliance burdens will only be robust if the basis of comparison effectively controls for these differences.

The characteristics of the reference businesses have to be well-specified to ensure that differences in measured indicators represent unnecessary burdens, and not merely differences in the impact of the regulation as a consequence of differences in the size or other characteristics of the business. To account for this variability in business characteristics and the impact of regulation on them, a *range* of reference businesses would have to be selected to provide insights into the ‘sensitivity’ of collected burden information. For example, data on administrative compliance costs for reference businesses would be obtained from actual businesses that have the same or similar specified characteristics.

Reference businesses would not necessarily be statistically representative of the total business population. Nonetheless, they would account for those characteristics that are considered to be typical, or common, of businesses affected by the regulation under consideration.

In undertaking these interviews, the international Standard Cost Model framework and its Australian Government elaboration, the Business Cost Calculator, could be used for data collection. Further, the Business Cost Calculator, now the responsibility of the Office of Best Practice Regulation, would be a useful tool for storing data by administrative compliance activity.

Much information would come from government and published sources

Information could be collected for many indicators from government agencies, although this is likely to require efforts to improve data quality and align definitions in many areas. Experts with specific knowledge of regulatory requirements and their impact on business could also provide useful input. For example, in benchmarking the burdens facing businesses operating interstate, experts could examine regulations in each jurisdiction to identify inconsistencies and duplication, and then rate the materiality of these differences.

Much of the information for the proposed benchmarking of regulation against ‘best practice’ principles of regulatory design, administration and enforcement, could be obtained from government agencies and regulatory publications. It could be more difficult to obtain information in some jurisdictions on the extent to which regulations are enforced in accordance with the procedures outlined in regulations or guidelines.

There are some inherent limitations

Performance benchmarking would not, of itself, necessarily reveal ‘best practice’, or whether particular regulations are appropriate. All that can be measured are differences that point to unnecessary costs. To complement such indicators, therefore, it is important to identify potentially systemic problems in regulatory design, administration and enforcement by benchmarking the quality of regulation. Ultimately, more detailed investigation would generally be required, however, before any definitive findings could be made about reform needs.

Secondly, such benchmarking cannot account for the benefits of regulation. It is therefore necessary to limit the comparison of indicators of the paperwork and associated costs of compliance activities to regulations with similar *objectives*. In this case, large differences in indicators are more likely to be reflective of unnecessary burdens, rather than differences in desired regulatory outcomes. Where objectives differ only slightly, and their associated administrative compliance activities are separable, such costs may be able to be netted out before making inter-jurisdictional comparisons.

Generally, *indirect* measures have to be used as indicators of the additional or incremental compliance burdens related to specific regulations. It is not feasible to attempt to measure incremental compliance costs directly, because business accounting systems do not identify these separately. Also, the counterfactual situation of what would be done in the absence of regulation is usually very hard to determine. However, such shortcomings are inherent to all regulatory assessments and reviews.

Regulations that affect production costs, such as requirements to install safety equipment or construct pollution mitigation works, could not be benchmarked, even if they fell within the scope of the study. This also applies to the burdens imposed by regulators’ requests for information on price and service quality oversight. The impacts of these burdens are typically specific to market circumstances and the activities of each business.

It is also not possible to construct a satisfactory ‘meta’ indicator of relative jurisdictional performance. There is insufficient information on business demographics and the reach of regulations to establish the weights necessary to construct a composite indicator of a set of regulations for each jurisdiction.

Case studies of each form of benchmarking proposed in this report were undertaken to get a preliminary sense of the scope for performance to be compared through different indicators (box 4). These studies were not entirely conclusive, because in the time available, it was necessary to rely on published data. However, the

outcomes provide evidence that benchmarking is technically feasible. Further, there were sufficient differences in the indicators across jurisdictions to suggest that benchmarking results would provide useful evidence of potentially unnecessary burdens.

Box 4 **Some case studies**

A preliminary application of some of the possible indicators suggested in this report was undertaken through brief case studies in the following areas. The aim of the case studies was to explore the feasibility of benchmarking and, in particular, to identify possible difficulties and challenges in measuring the suggested indicators.

Restaurant and cafe licensing

For 'becoming a business', it was found that measuring indicators of the difficulty in obtaining licences, permits and registrations is relatively straightforward. Further, differences in these indicators across the surveyed jurisdictions were apparent. In addition, it was possible to identify the administrative compliance activities involved in establishing a business. However, the associated administrative compliance costs could not be estimated because of time constraints.

Environmental approval processes

For 'doing business', it was confirmed that if the information available in some jurisdictions were available in all, it would be possible to construct comparable indicators with the cooperation of relevant government agencies. The case study trial highlighted the importance of consultation with relevant agencies and industry experts to develop indicators that are both robust and comparable before benchmarking commences.

Personal property security registration and regulation

For 'doing business interstate', it was possible to measure the suggested indicators of the extent of duplication and inconsistency. The next step would be for industry experts to rate the materiality of the identified additional compliance activities arising from having to operate or trade interstate.

Indicators of the 'quantity of regulation' were measured, displaying significant differences across jurisdictions. Similarly, the suggested 'quality of regulation' indicators were measured and assessed against generally accepted principles of best practice. Although a different set of indicators would be applicable for other areas of regulation, most of the suggested indicators appeared relatively robust.

Advantages of a staged approach

In the Commission's view, therefore, regulatory benchmarking, as raised by COAG, is feasible and would complement other government initiatives directed at achieving appropriate, cost-effective regulation. That said, there are a number of complexities

and challenges to achieving robust results, including uncertainties about data provision.

With these in mind, the best way forward, in the Commission's view, would be to adopt a staged approach, commencing in a first three year period with a limited number of regulatory areas and indicators. Benchmarking also should be sequenced such as to allow necessary development of methodologies and data collection in the initial phase. This would also enable learning by doing. Following an assessment at the end of such a three-year program, the extension and potential expansion of the exercise could be considered (see below).

Which regulations should be benchmarked first?

A range of regulatory areas has been identified in this report as potential candidates for benchmarking. These include areas of regulation identified by COAG as 'hotspots', as well as additional regulatory problem areas identified by the Regulation Taskforce (2006) and by participants in this study. However, it would not be possible to benchmark all of these regulatory areas in the initial phase, and some further prioritisation is necessary. The final choice of regulations was made on the basis of a number of criteria, including the likely extent of unnecessary burdens and the ability to collect data and to undertake comparisons without imposing undue costs on business and government.

On this basis, the Commission would propose benchmarking the following areas of regulation in the first three years of Stage 2 of the study:

- *Occupational health and safety* (Commonwealth, State and Territory) — performance benchmarking of administrative compliance costs (*becoming and being a business*) and standards benchmarking of consistency across jurisdictions (*doing business interstate*). This area of regulation was identified by many participants as imposing considerable burdens on a range of businesses, and has been identified as a priority for reform by COAG and the Regulation Taskforce.
- *Land development assessment* (local government) — performance benchmarking of approval processes (*doing business*). Land development approvals were widely seen by participants in this study as a major area of regulatory concern. They were also nominated by COAG as a 'hot spot'. They are likely to involve significant variations in compliance costs across jurisdictions.
- *Environmental approvals* (Commonwealth, State and Territory) — performance benchmarking of approval processes (*doing business*) and standards

benchmarking of consistency across jurisdictions (*doing business interstate*). Environmental approvals were identified by many participants as a priority for benchmarking, and COAG identified bilateral agreements under the *Environment Protection and Biodiversity Conservation Act 1999* as a priority area for reform.

- *Stamp duty and payroll tax administration* (State and Territory) — performance benchmarking of ongoing administrative compliance costs (*becoming and being a business*). These taxes feature extensively in many business studies on regulatory burden and were identified as a priority for reform by the Regulation Taskforce and participants in this study.
- *Business registration* (Commonwealth, State and Territory) — performance benchmarking of start-up and ongoing administrative compliance costs (*becoming and being a business*). Registration processes affect nearly all businesses, and have been identified by COAG as a priority for regulatory improvement.
- *Financial services regulation* (Commonwealth, State and Territory) — performance benchmarking of administrative compliance costs (*becoming and being a business*). This area of regulation was identified as a priority for reform by the Regulation Taskforce and was identified by many participants as a significant area of regulatory burden.
- *Food safety* (Commonwealth, State, and Territory and local government) — performance benchmarking of approval processes (*doing business*) and standards benchmarking of consistency across jurisdictions (*doing business interstate*). Food safety regulations involve all tiers of government and affect a number of businesses. They were commonly cited by participants as an area requiring improvement and were identified by the Regulation Taskforce as a priority for reform.

A proposed program

The Commission is proposing a three-year program, in which each of the above areas would be benchmarked once in the first period. Follow-up benchmarking could then occur at intervals as appropriate. This would allow time for any changes to be detectable, and the process would be more cost-effective and manageable than attempting to benchmark the same areas of regulation every year.

It is envisaged that the first year of the proposed program would:

- focus primarily on benchmarking the quantity and quality of those regulations that have been identified as priorities;

- benchmark administrative compliance costs for one of the more straightforward areas of regulation, such as business registrations, in order to develop and test methodologies; and
- undertake preparatory work regarding other priority regulatory areas, to pave the way for subsequent benchmarking.

The program for the next two years could be confirmed after the results of the first year's work are assessed, following further consultations.

An indicative program that could meet these requirements is as follows:

- *Year 1:* Business registrations; quality and quantity/form of regulation.
- *Year 2:* OHS; stamp duty and payroll tax administration.
- *Year 3:* Environmental approvals; financial services; food safety; land development assessment.

Some flexibility would be appropriate to maintain complementarity with other regulatory reform initiatives. If major reforms emerge in any of the selected areas of regulation within the three-year time frame of the initial program, consideration could either be given to establishing a baseline to benchmark progress, or selecting another area of regulation to benchmark. For example, baselines for initiatives such as the Standard Business Reporting project, overseen by a committee of Australian and State Government officials, could be established.

Before commencing, the Commission would need to consult with governments and the affected business community to obtain broad agreement on the approach to be taken, including the indicators to be used, their measurement, and the supply of necessary data. In particular, government support would be required for the selection of indicators and in the provision of comparable data from their agencies and local government authorities. In some cases, this might involve reaching agreement on data standards and adjusting data collection activities accordingly.

Advisory panels would be established for this purpose and would be convened at strategic points to provide advice and support, as well as a mechanism for feedback on preliminary results. They would help ensure that benchmarking remains focussed over time on generally perceived priority areas.

In the longer term, the benchmarking program could potentially include New Zealand for some areas of regulation, given the similarity in institutional arrangements between the two countries and the emphasis placed on trans-Tasman harmonisation in recent years. This would facilitate greater benchmarking of regulation, including at the Commonwealth level.

The commitment of governments and business will be crucial

The program has been designed to encompass all the main forms of compliance cost, as well as indicators of regulatory quality and cumulative burden, in a way that would be manageable and cost-effective for governments and business. Nevertheless, significant resources would be needed both to administer the program and to support its data needs. Failure to adequately resource the project would seriously compromise its success.

Estimates are difficult to make in advance. However, based on other relevant studies and the Commission's own experience as secretariat to the Government Services Review, budgetary resources of some 2 to 3 million dollars per annum would be required to cover necessary staff and survey costs. In addition, costs would be incurred by participating government agencies and business.

The Commission's proposed program is summarised on the next page (*see over*). The program necessarily entails a degree of flexibility, with scope for it to be modified in the light of experience. As noted, the Commission would ensure that governments and business were consulted closely as the exercise proceeds. Ultimately, the utility of such regulatory benchmarking will crucially depend on governments' own commitment to it and on the extent to which they utilise the results.

The Productivity Commission's key proposals

The Commission proposes for COAG consideration a benchmarking program comprising the following elements:

- *In the first three years, compliance costs, and the quantity and quality of regulation, would be benchmarked across jurisdictions for a limited number of regulatory areas.*
- *Compliance costs to be benchmarked would include those relating to establishing and running businesses within jurisdictions as well as across jurisdictions.*
- *The regulatory areas proposed to be benchmarked and their possible sequencing are as follows:*

Year 1	Year 2	Year 3
<i>Business registrations</i>	<i>Occupational Health and Safety</i>	<i>Environmental approvals</i>
<i>Quality of regulations</i>	<i>Stamp duty and payroll tax administration</i>	<i>Financial services regulation</i>
<i>Quantity and form of regulation</i>		<i>Food safety regulation</i>
		<i>Land development assessment</i>

- *The Commission would consult further on methodology and data availability in year 1 and before finalising the structure of the program in years 2 and 3.*
- *The choice of specific indicators to use would be made in consultation with governments and relevant business groups, drawing from those identified in this report.*
- *The Commission would establish specialist advisory panels to assist it in these activities, comprising representatives of governments and relevant businesses.*
- *Preliminary results would be made available to governments to provide opportunities for scrutiny and comment. There could also be provision for each jurisdiction to include a commentary in the Commission's reports.*
- *The first report would be provided 12 months after commencement of Stage 2.*
- *At the completion of the initial three-year program, an evaluation report would be prepared for consideration by governments. It would include any suggestions for modifying the benchmarking, or extending it to additional areas of regulation or to other countries.*