

The **Allen Consulting** Group

Red Tape Review of Pay-roll Tax E-Business Offerings

26 March 2007

Final Report to State Revenue Office

The Allen Consulting Group

The Allen Consulting Group Pty Ltd

ACN 007 061 930

Melbourne

Level 9, 60 Collins St

Melbourne VIC 3000

Telephone: (61-3) 8650 6000

Facsimile: (61-3) 9654 6363

Sydney

Level 12, 210 George St

Sydney NSW 2000

Telephone: (61-2) 9247 2466

Facsimile: (61-2) 9247 2455

Canberra

Level 12, 15 London Circuit

Canberra ACT 2600

GPO Box 418, Canberra ACT 2601

Telephone: (61-2) 6230 0185

Facsimile: (61-2) 6230 0149

Perth

Level 21, 44 St George's Tce

Perth WA 6000

Telephone: (61-8) 9221 9911

Facsimile: (61-8) 9221 9922

Brisbane

Level 9, 379 Queen St

Brisbane QLD 4000

Telephone: (61-7) 3016 3500

Facsimile: (61-7) 3221 7255

Online

Email: info@allenconsult.com.au

Website: www.allenconsult.com.au

Disclaimer:

While The Allen Consulting Group endeavours to provide reliable analysis and believes the material it presents is accurate, it will not be liable for any claim by any party acting on such information.

© The Allen Consulting Group 2007

Executive summary

Introduction

Under its *Reducing the Regulatory Burden* initiative, the Government has made a commitment to reduce the administrative burden ('business red tape') of State regulation by 15 per cent over three years, and 25 per cent over five years from the 1 July 2006.

This study assesses the impacts of the State Revenue Office's (SRO's) Pay-roll Tax e-Business initiatives on the reduction of red tape for businesses. This suite of e-Business initiatives, which has been introduced progressively from 2002, allows for processes that were previously undertaken manually to be undertaken electronically. These initiatives include Electronic Annual Adjustments, Electronic Returns, Online Payments, Electronic Records, Electronic Registration and Password Reset, and the Direct Credit Allocator.

As of 2005-06, 11 per cent (23 661 businesses) of Victorian businesses paid Pay-roll Tax and therefore the related compliance costs do not apply to most Victorian businesses. Further, the majority of the records and data to be kept by these businesses would need to be collected to comply with the requirements of other state and or federal regulators. Accordingly, Pay-roll Tax compliance costs in Victoria must be seen in this context.

Summary of findings

Relative to the previous manual lodgement and payment system, the key benefits that have arisen from the e-Business system include:

- (i) red tape reduction to businesses;
- (ii) broader benefits to businesses; and
- (iii) reduced costs for the SRO.

Red tape reduction to businesses

In total, the e-Business initiatives implemented by the SRO have resulted in red tape savings of approximately \$10.3 million per annum — as shown in Table 1 (page 2) below. This represents a red tape saving of 52.6 per cent relative to a base case scenario where the e-Business system did not exist.

The key administrative benefits to businesses stem from the time savings (\$6.3 million) associated with the preparation of the Annual Adjustments. Less effort is required by businesses to complete Annual Adjustments due to the pre-population of data by the system and the ease with which forms can be completed and lodged. Businesses consulted during this study also indicated that they have saved time by using the system as a mechanism to manage and verify tax records.

Other key administrative benefits that have accrued to businesses include time savings associated with:

- the ability to make tax payments using the Online Payment option (\$3.3 million);
- record updating (\$0.3 million); and
- the preparation of Monthly Returns (\$0.3 million).

The savings are consistent with the results of a web-based survey conducted by the SRO in 2006. Of the 769 respondents, almost 50 per cent rated the time savings conferred by the e-business system to be excellent. Overall, 96.4 per cent rated the savings as satisfactory or better.

Table 1

SUMMARY OF RED TAPE REDUCTION TO BUSINESSES

Savings in...	Value of savings	% saving relative to base case
Preparation of annual adjustments	\$6 342 132	49.3%
Preparation of monthly returns	\$291 664	25.0%
Making payments	\$3 271 629	67.0%
Registration and password update	\$41 052	32.5%
Record updating	\$318 875	64.1%
Follow up of suspense payments	\$10 728	95.8%
Total	\$10 276 081	52.6%

Note: The reference year for the analysis was 2006-07, although some of the data was obtained from the preceding years, as this was the latest available data. It should be also noted that the assumptions used in this analysis was based on estimates provided by a small sample of businesses, SRO internal data and ACG estimates. The SRO notes that further survey work can be conducted if required.

As a result of greater ease in preparing Monthly Returns, approximately 16 300 businesses that were not previously submitting their paper based Monthly Returns forms are now submitting e>Returns. That is, the implementation of the e-Business system has made it easier for businesses to now meet the Monthly Return requirements. This has clear benefits for the SRO in terms of enhanced capacity to monitor and enforce Pay-roll Tax obligations. For these businesses though, they incur new costs in lodging an e-Return, given that previously, they were not filing their returns manually. The increase in costs associated with lodging an e-Return (versus not complying) is estimated to be \$0.7 million. This is effectively the cost associated with 'new' compliance.

After taking these additional costs into account, the net red tape savings associated with the e-Business system amounts to \$9.5 million, or a 48.9 per cent saving relative to the manual system.

Broader benefits to businesses

For many businesses, the e-Business initiatives allow for greater certainty of tax data, better record management, and improved tax compliance.

For some businesses, namely those who received a refund as a result of the Annual Adjustment process, the e-Business system has cut the time it takes to process claims. It is estimated that this results in benefits to business equating to \$0.25 million per year. The SRO is now receiving information that is more accurate and provided in a timelier manner, which enables business refunds to be processed more quickly.

Businesses also benefit as the SRO no longer needs to carry out as many full audits of businesses. This is due to the ability of the e-Business system to capture data, which the SRO uses to match and verify against data stored in third party databases. The SRO now undertakes more issue specific audits, which takes on average 56 per cent less time relative to a full audit. Since the introduction of the e-Business system, the proportion of audits that are full audits has declined from 86.65 per cent to 26.02 per cent. This in turn saves effort for businesses that are subject to an audit.

Reduced costs for the SRO

The e-Business system has reduced administrative costs to the SRO. Many processes are now automated, and savings to the SRO have arisen through reductions in:

- data entry tasks;
- tasks associated with sorting and matching EFT payment data;
- follow up calls to businesses; and
- Call Centre call time.

The richness and accuracy of the data now collected by the SRO has also resulted in greater efficiency in auditing and compliance activities.

Conclusion

The SRO's e-Business initiatives have resulted in red tape savings to businesses amounting to \$10.3 million in 2006-07. Taking account of the additional compliance costs incurred by businesses — as required by the Standard Cost Model — the *net* red tape saving for businesses is estimated to be \$9.5 million in 2006-07, or a 48.9 per cent saving relative to the manual system.

In the context of the *Reducing the Regulatory Burden* initiative, the SRO's e-Business initiative represents best practice in what can be achieved both in cutting red-tape and improving the effectiveness and efficiency of regulation.

Chapter 1

Government's commitment to reduce red tape

In 2006, the Treasurer made a commitment to cut business red tape. Under its *Reducing the Regulatory Burden* initiative, the Government has committed to:

- reducing the administrative burden of State regulation as at 1 July 2006 by 15 per cent over three years and 25 per cent over five years;
- offsetting simplifications to any new or additional administrative or compliance burdens imposed by regulation made after 1 July 2006; and
- reviewing key areas of compliance burden.¹

Victoria's Pay-roll Tax regime imposes a number of administrative burdens on businesses whose payroll exceed \$550 000. In 2002, the SRO began implementing a suite of e-Business initiatives for Pay-roll Tax to improve the efficiency and operation of the SRO and to reduce the burden on businesses. These initiatives include:

- *Electronic Annual Adjustments* — allows customers to access and complete their Annual Adjustment via a secure online website;
- *Electronic Returns* — allows customers to access and complete their Monthly Returns via a secure online website;
- *Online Payments* — allows the SRO to deduct tax payments from a customer's bank account;
- *Electronic Records* — allows customers to change their details online without needing to call the SRO;
- *Electronic Register* — allows businesses to register online for Pay-roll Tax;
- *'Password Required'* — allows businesses to reset their e-Business password online without needing to call the SRO;
- *Direct Credit Allocation* — assists the SRO in identifying and matching electronic payment receipts to payees.

While not forming part of the Reducing the Regulatory Burden initiative (as most occurred prior to 1 July 2006), the e-Business initiatives nonetheless have resulted in a reduction in administrative costs. The purpose of this review is to estimate those administrative savings to businesses as if they did form part of the *Reducing the Regulatory Burden* initiative, thereby highlighting the SRO's long-term commitment to reducing red tape.

¹ The Victorian Government 2006, *Reducing the Regulatory Burden: The Victorian Government's Plan to Reduce Red Tape*.

Chapter 2

Red tape reduction impacts

2.1 Overview of approach

The analysis of red tape impacts uses the Standard Cost Model, drawing on the Treasurer's interim guidelines.² Given that the guidelines refer solely to estimating future impacts (that is, impacts that arise after 1 July 2006) rather than historical impacts, this report is prepared using the principles of the Standard Cost Model rather than adhering to specific requirements of the guidelines *per se*.

The Standard Cost Model is an activity based costing approach for measuring administrative costs. The general framework for estimating administrative cost involves multiplying the 'price' of an administrative activity by the frequency (quantity) of that activity. The price of the activity is simply the labour cost multiplied by the time it takes to perform that activity (plus any other significant costs), while the frequency is the number of times this activity is conducted throughout the population. The Standard Cost Model looks at the *marginal* impacts of an administrative change.

As mentioned above, the Standard Cost Model is intended for measuring future impacts. For this analysis however, we will be measuring the savings that have accrued due to past initiatives introduced.

As such, the analysis requires the development of a base case, which is the situation if the e-Business offerings did not exist. Under the base case, businesses would need to complete adjustments and return forms manually and mail them to the SRO for processing. The time saved completing processes in an online environment relative to completing forms manually represents the 'benefit'.

The reference year for this analysis is 2006-07, and the general assumptions used in the analysis (such as the labour rates and on-costs) are detailed in the Appendix.

2.2 Annual Adjustments

In 2005-06, 23 351 Annual Adjustments were lodged using the e-Business system. These Annual Adjustments would have been lodged manually if the e-Business system had not been developed.

The SRO estimates savings of 30 minutes to businesses per Electronic Annual Adjustment lodged relative to the manual lodgement process. This estimate is based on the time it took the SRO officers to complete an Annual Adjustment in the test database (20 minutes) relative to the estimated time to complete and lodge an adjustment manually (50 minutes).

² Victorian Government 2006, *Measurement of Changes in Administrative Burden: Interim Guidelines issued by the Treasurer*, 2 October 2006.

In discussions with members of the SRO's Business Reference Group and one other business outside of this Reference Group, savings ranged from 1 hour to 16 hours (see Table A.1). The wide range of responses appear to be due to the different in-house systems and processes that businesses use for processing and recording Pay-roll Tax. For instance, one business indicated e-Business benefits associated with savings in record keeping:

...the biggest bonus is record management. There is no need to duplicate things for auditing and we are now printing records off the screen...

Given the diversity of estimates, a median (and conservative) time saving estimate of 4 hours per Annual Adjustment has been adopted in this analysis. Applying an estimate of the cost of labour plus the oncost rate (\$67.90),³ and multiplying this by the time saved (4 hours) and the current number of Annual Adjustments completed online (23 351), the total time saving benefit arising from this element of the e-Business system is estimated to be:

$$23\,351 \text{ Annual Adjustments} \times 4 \text{ hours} \times 67.90 \text{ p/h} = \$6\,342\,132.$$

A number of businesses (310 in 2005-06) continue to use manual forms due to the unavailability of Internet access. Their costs are included in both the base case and current cost estimates. However, these businesses do not accrue Annual Adjustment benefits associated with the e-Business system.

2.3 Monthly Returns

Businesses subject to Pay-roll Tax are required to complete 11 Monthly Returns annually. Over the last six months from February 2007, the number of Monthly Returns lodged averaged 18 999 per month.

The SRO estimates the time saved in completing an e-Return versus a manual return to be 2.5 minutes per return. This is based on an estimate from a sample of actual taxpayer lodgement times and time taken to lodge a return in a test database (3.5 minutes) versus the estimated time taken to lodge a return manually (6 minutes).

During discussions with the SRO Business Reference Group, the estimated time saving associated with the e-Return ranged from having no noticeable impact to savings of 3 hours. As with the Annual Adjustment process, the disparity in responses appeared to be due to the different reporting processes for each business. Those businesses that indicated greater savings are likely to have saved more time as a result of:

- the record keeping ability of the system;
- the system's calculator, which assists customers in calculating their Pay-roll Tax liability; and
- the ease of the system in assisting businesses to meet their Monthly Return obligations under the legislation.

³ For further discussion of hourly rates and the on-cost multiplier, see Appendix A.3.

One business, however, indicated that they already had internal systems in place and that the e-Business system did not result in additional record keeping benefits:

We already have a system which calculates our payroll tax due each month anyway. All we do now is insert the figures into e-business.

For this analysis, the median estimate from the sample of estimates of 10 minutes per return was used as a point estimate for the analysis (see Table A.1). Savings only apply to businesses that were already compliant and lodged Monthly Returns prior to the introduction of the Electronic Returns system. In March 2005, only 2343 manual returns were lodged (or approximately 10 per cent of businesses that were required to pay Pay-roll Tax). Thus, administrative savings only accrue to these 2343 businesses. Applying the hourly labour rate (plus on-costs) and savings of 10 minutes per return to these 2343 businesses, and multiplying this by 11 monthly returns per business per annum, the estimated savings amount to:

$$2343 \text{ businesses} \times 11 \text{ returns} \times 10 \text{ minutes} \times \$67.9 \text{ p/h} = \$291\,664.$$

Since the introduction of the Electronic Monthly Return system, more businesses are now completing and lodging their Monthly Returns. As indicated above, the number of Monthly Returns is now averaging 18 999 per month. This increase in compliance can be attributable to the simplicity in the lodgement process created by the Electronic Returns system. Nevertheless, this represents additional administrative costs for these businesses — that is, more businesses are incurring costs as they are now complying with the requirement to lodge their Monthly Returns.

The Standard Cost Model requires an estimate of the increase in administrative costs arising from changes to the compliance rate. The change in compliance is effectively the difference between the 18 999 businesses currently complying and the 2343 businesses that were compliant prior to e>Returns — that is, an additional 16 656 businesses are now complying and incurring new administrative costs associated with lodging Monthly Returns.

In all likelihood, these newly complying businesses do not incur additional costs associated with the collection and calculation of monthly salary data — they would already have this information to calculate their monthly payments.

The only additional cost to these businesses relates to inputting and submitting data on the website each month. The SRO estimates that this takes approximately 3.5 minutes per Monthly Return.

Using this assumption, the additional administrative costs incurred by newly complying businesses equates to:

$$\begin{aligned} &16\,656 \text{ businesses} \times 3.5 \text{ minutes} \times 11 \text{ monthly returns} \times \$67.9 \text{ p/h} \\ &= \$725\,668. \end{aligned}$$

2.4 Online Payment

Prior to the introduction of Online Payment in 2005,⁴ businesses making monthly payments used a variety of payment methods. As Table 2 indicates, the most popular method was electronic funds transfer (EFT) followed by payment at the bank, and mailing a cheque to the SRO. With the introduction of the Online Payment option, it appears that this has reduced the proportion of businesses paying at the bank (down from 19.79 per cent to 1.48 per cent) and using the cheque payment option (down from 19.2 per cent in 2004-05 to 8.29 per cent in 2006-07).

Table 2

PAYMENT TYPE: PROPORTION OF TOTAL TRANSACTIONS

Payment method	2004-05	2006-07
Paid at the SRO	6.41%	6.11%
Mailing a cheque	19.2%	8.29%
Paid at bank	19.79%	1.48%
BPAY	11.98%	13.25%
Online Payment	Not applicable	29.79%
Electronic Funds Transfer (EFT)	42.62%	41.07%

Source: State Revenue Office. Figures for 2006-07 are year to date figures only but the trend is expected to continue.

The introduction of Online Payment does not appear to have had a noticeable impact on those businesses that were using EFT and BPAY payments. Presumably, the benefits of Online Payment are not too different from EFT or BPAY payments to warrant a change in payment behaviour for these businesses.

Based on the most recent figures for the last 12 months, there are approximately 240 000 payments per year. Of these, 29.79 per cent, or approximately 71 500 payments are made using the Online Payment method each year.

Based on the above data,⁵ in the absence of the Online Payment option, it is assumed that:

- 36.67 per cent of these 71 500 payments would have been made using a cheque; and
- 63.33 per cent of these 71 500 payments would have been made by visiting a bank.

For cheque payments, the SRO estimates that businesses will take 8 minutes to fully process and issue a cheque. By comparison, the SRO estimates that it will take businesses 30 seconds to make a payment via Online Payment — equating to savings of 7.5 minutes per payment.

⁴ For a summary of the Online Payment system, see Appendix.

⁵ Table 2 shows that approximately 30 per cent of payments are now made using Online Payment, and that approximately 11 per cent of payees have migrated away from the cheque payment method, and approximately 19 per cent of payees have migrated away from paying at a bank. It is assumed that these payees have migrated to Online Payment.

As for visiting a bank, the Allen Consulting Group considers 1 hour to be a reasonable estimate of the time it takes to travel to and from a bank branch, wait in a queue, and transact with a teller. On this basis, the Online Payment option is estimated to result in savings of 59.5 minutes per payment for those businesses that would have made their payment at the bank.

Using these inputs, it is estimated that the value of time saved by businesses that used the Online Payment option (as opposed to mailing a cheque or visiting a bank or the SRO) is:⁶

$$\begin{aligned} & (36.67\% \times 71\,500 \text{ payments} \times 7.5 \text{ minutes} \times \$67.9 \text{ p/h}) + \\ & (63.33\% \times 71\,500 \text{ payments} \times 59.5 \text{ minutes} \times \$67.9 \text{ p/h}) \\ & = \$\,3\,271\,629. \end{aligned}$$

For the remaining 70.21 per cent of businesses that are continuing to use alternative payment methods (mostly EFT and BPAY), they do not accrue savings from the Online Payment function. Businesses that continue to use alternative payment method are assumed to take 45 seconds per payment. That is, EFT and BPAY payment is assumed to take about the same amount of time as an Online Payment — otherwise, businesses would have used Online Payment. However, an additional 15 seconds is assumed as the EFT and BPAY process involves logging in to another website. These costs are included in both the base case and current cost estimates.

2.5 Registration and password

For the last 12 months up to February 2007, 3780 businesses registered for Pay-roll Tax using the online system. In the absence of the online system, businesses would have had to complete the registration process manually.

The SRO estimates that it takes 20 minutes to complete the registration process manually. This includes the time taken by businesses to contact the SRO for registration instructions.

The SRO estimates that it now only takes 7 minutes to complete the online registration process. This is because the Electronic Register system is designed with a user-friendly interface, making it easier for businesses to submit registration details.

These assumptions were not tested with businesses (as the businesses contacted were already registered before the introduction of the e-Business system). However, the Allen Consulting Group does not consider the SRO's estimates to be unreasonable. Moreover, during discussions with the SRO customer support staff, they notice fewer customers are now making enquiries about legislative matters associated with the registration process. They attribute this to the availability of online help links and definitions to guide and simplify the registration process. Indeed, the SRO's website usage statistics indicate that over 212 500 hits were made to the 'Pay-roll Tax Express Help' web page between March 2006 to February 2007.⁷

⁶ It should be noted in the calculation that the assumptions of 36.67 per cent (11÷30) and 63.33 per cent (19 ÷ 30) are fractions that have a recurring decimal.

⁷ Data provided by Paul Duffer, Manager, ICT Applications Services, SRO, 19 March 2007.

Using the above time saving and frequency assumptions, the value of time saved by businesses using the online registration process is estimated to be:

$$3780 \text{ registrations} \times 13 \text{ minutes} \times \$67.9 \text{ p/h} = \$55\,610.$$

Over the same period, 1808 businesses used the manual process to register for Pay-roll Tax. The SRO indicates that businesses under investigation have been required to complete a manual registration form. These businesses did not accrue savings from the Electronic Register system and are assumed to take 20 minutes to complete the manual registration process. These costs are included in the base case and current cost estimation. However, the SRO has recently implemented an enhancement to allow investigation registrations to be completed online.

The Electronic Registration process includes the time associated with retrieving a password. However, businesses that misplace their password would need to reset their login details. The process of resetting a password involves time, and therefore, a cost to business. The SRO estimates an average of 6432 password resets per year.

Prior to the introduction of the 'Password Required' function, which allows for passwords to be reset online, businesses would have had to contact the SRO to obtain an activation code. The SRO estimates that this process took about 8 minutes. Thus the total cost to business to reset their password, without the 'Password Required' function, is estimated to be:

$$6432 \text{ password resets} \times 8 \text{ minutes} \times \$67.9 \text{ p/h} = \$58\,231$$

With the 'Password Required' function, the time it takes businesses to reset login details is estimated to be only 2 minutes. The estimated business cost associated with resetting misplaced passwords has therefore declined to

$$6432 \text{ password resets} \times 2 \text{ minutes} \times \$67.9 \text{ p/h} = \$14\,558.$$

While, this represents a saving of \$43 673 relative to the situation before the 'Password Required' function, the need to reset a password still represents a business cost relative to the base case of not using an online environment at all. That is, if the e-Business system did not exist, businesses would not need to reset their password.

In total, the net benefit to businesses per annum arising from the e-Registration and password requirements of the e-Business system is estimated to be \$41 052 (or \$55 610 less \$14 558).

2.6 Records update

Prior to the availability of the Electronic Records function, businesses that wanted to update their Pay-roll Tax records had to do so manually by either writing a letter or transmitting a facsimile to the SRO.

The key reasons for contacting the SRO with regards to record changes include:⁸

- 'de-grouping' (that is, removing a company from a group of companies) — this occurs on average 344 times per year;

⁸ These statistics apply to online transactions only relating to 'de-grouping', cancellation of registrations, and data maintenance.

- cancellation of registration — this occurs on average 353 times per year; and
- data maintenance (such as changing an address and contact details) — this occurs on average 22 441 times per year.

With the Electronic Records functionality, the SRO estimates savings of:

- 25 minutes per ‘de-group’ change (down from 30 minutes to 5 minutes);
- 11 minutes per cancellation change (down from 15 minutes to 4 minutes); and
- 12 minutes per data maintenance operation (down from 15 minutes to 3 minutes).

These assumptions were not tested with businesses. However, the Allen Consulting Group does not consider the SRO’s estimates to be unreasonable. On the basis of the above assumptions, the Electronic Records function saves businesses time equivalent to:

$$\begin{aligned} & 344 \text{ ‘de-groups’} \times 25 \text{ minutes} \times \$67.9 \text{ p/h} + \\ & 353 \text{ ‘cancellations’} \times 11 \text{ minutes} \times \$67.9 \text{ p/h} + \\ & 22\,441 \text{ ‘data maintenance items’} \times 12 \text{ minutes} \times \$67.9 \text{ p/h} \\ & = \$318\,875. \end{aligned}$$

In February 2007, the SRO received 484 manual record changes for the month (equating to 5808 per annum) mainly from larger businesses. These businesses do not accrue savings through the e-Records function. It is assumed that these manual record changes take on average 15 minutes per change to complete. These costs are included in the base case and current cost estimation.

2.7 Follow up of suspense payments

Currently, approximately 1100 tax payments per month made through the EFT payment method go into ‘suspense accounts’ — these refer to the EFT payments where the payee cannot be identified.

Prior to the introduction of the Direct Credit Allocator (DCA), the SRO estimates that approximately 15 per cent of payments in suspense account would require follow up with customers to verify payment (this equates to approximately 165 transactions requiring follow up). The follow up work typically involves a 5 minute phone call to the customer.

With the introduction of the DCA, the number of suspense payments that require additional follow up work has reduced. The SRO estimates that 20 per cent of EFT transactions in suspense accounts would now require additional follow-up work but only 3 per cent of this amount requires contact with the customer — this equates about 7 transactions per month requiring customer follow up).

Thus, the DCA system has reduced the amount of follow up calls, to an average of 158 calls per month, or 1896 calls per annum.

Given that it takes approximately 5 minutes per follow up phone call to confirm whether a business has made payment, the annual time savings to businesses associated with the reduction in follow up phone calls equates to:

1896 telephone calls × 5 minutes × \$67.9 p/h = \$10 728.

While this is a relatively small saving for business, the saving for the SRO is significantly higher. It is just that the savings for the SRO are not relevant for the Standard Cost Model estimates.

2.8 Other costs to businesses

Members of the SRO Business Reference Group indicated that they did not incur additional business costs in using the e-Business system. That is, additional training and IT infrastructure was not required to use the system.

2.9 Summary of red tape savings

A summary of the total administrative costs to businesses without the e-Business system (the base case) and with the e-Business system (the current situation) is presented in Table 3 below. Without the e-Business system, businesses would have incurred \$19.5 million in administrative costs to comply with Pay-roll Tax obligations in 2006-07. With the e-Business system, current red tape costs are down to \$9.3 million, or a red tape reduction totalling \$10.3 million (or approximately 52.6 per cent) over this period. Most savings (over 90 per cent) accrue as a result of the Electronic Annual Adjustment and Online Payments functions.

Table 3

SUMMARY OF ADMINISTRATIVE COSTS TO BUSINESSES, 2006-07

Item	Without e-Business (Base case)	With e-business (Current)	Value of savings
Preparation of annual adjustments	\$12 852 655	\$6 510 524	\$6 342 132
Preparation of monthly returns	\$1 166 658	\$874 993	\$291 664
Making payments	\$4 885 110	\$1 613 481	\$3 271 629
Registration/password	\$126 475	\$85 423	\$41 052
Record updating	\$497 198	\$178 322	\$318 875
Suspense payments	\$11 204	\$475	\$10 728
Total	\$19 539 299	\$9 263 218	\$10 276 081

As a result of greater ease in preparing Monthly Returns, approximately 16 300 businesses that were not previously submitting their paper based Monthly Returns forms are now submitting e>Returns. This has clear benefits for the SRO in terms of enhanced capacity to monitor and enforce Pay-roll Tax obligations. It also means that those businesses now incur compliance costs that were not previously incurred (\$0.7 million).

After taking these additional costs into account, the net red tape savings associated with the e-Business initiatives amounts to \$9.5 million in 2006-07, or a 48.9 per cent reduction.

Chapter 3

Other impacts

In addition to the administrative cost savings to businesses, the e-Business system generates other broader benefits particularly for the SRO as well as for businesses.

3.1 Quicker refunds to businesses

The e-Business system has enabled refunds to be issued in a timelier manner. This is because information is being submitted more quickly and more accurately.

Under the manual system, processing delays arise through:

- Annual Returns being posted but not received;
- businesses making inadvertent errors in their Annual Adjustments (such as including ATO payments etc); and
- delays in receiving and processing the data.

Prior to the e-Businesses system, follow up and investigation work was required on some 500 Annual Adjustments — some of these took more than 6 months to resolve. With the e-Business system, refunds are now being processed more quickly.

The SRO data shows that the percentage of refunds being completed within 3 months of lodgement has dramatically increased — from 5.21 per cent in 2001-02, to 74.7 per cent in 2005-06. Most returns are now completed within one month. The ability to receive returns more quickly represents a benefit to businesses — as there is time value attached to money.

Assuming that approximately 70 per cent of the value of refunds in 2005-06 (\$16 million) is now being returned to businesses 3 months earlier than was the case previously, and applying a rate of 9 per cent representing the opportunity cost of capital,⁹ this equates to benefits of roughly:

$$\$16 \text{ million} \times 70\% \times 9\% \times 3/12 = \$252 \text{ 000.}$$

3.2 Audits by the SRO

The SRO indicates they are now receiving information that is more complete, more accurate and provided in a timelier manner.

In particular, they note that:

- more businesses are now submitting Monthly Returns; and
- more businesses are now completing optional data fields (currently 80 per cent of businesses complete itemised salary details in their Annual Returns, previously the response rate for these fields were low).

⁹ Based on the real risk free rate of 3 per cent plus a market risk premium of 6 per cent (which is the default rate used by the ACCC). That is, if businesses received their refunds earlier, and invested this money in a diversified portfolio on the stock exchange, they would expect returns of 9 per cent per annum.

The increased ability of the e-Business system to capture data has had a flow on impact on the SRO's compliance activities. The SRO is able to use this information to match and verify against data stored with third party databases. As a result, the SRO does not need to conduct as many full audits on businesses. Instead, the SRO are undertaking more issue specific audits that take less time on average.

As Table 4 indicates, the proportion of audits that were 'full audits' has declined from 86.65 per cent (in 2000-01) to 26.02 per cent (in 2005-06). The SRO also indicates that it takes approximately 56 per cent less time to conduct an issue specific audit versus a full audit.

The reduction in the proportion of audits that are full audits represents a saving for the SRO and for businesses. However, it is difficult to quantify the extent of these savings, as:

- the absolute number of total audits (full and issue specific) has increased since 2000-01 (from 337 audits to 1518 audits in 2005-06); and
- the extent to which the increase in the number of audits was attributable to the e-Businesses system (as a result of freeing up resources) or to other policy changes can not be ascertained.

As such, audit cost savings for businesses are not quantified.

Table 4

FULL AUDITS VERSUS SPECIFIC AUDITS

	2000-01	2005-06
Full audit	86.65%	26.02%
Issue specific audit	13.35%	73.98%
Total	100%	100%

Source: SRO data.

3.3 Reduced costs for the SRO

A key benefit of the e-Business system is the cost savings to the SRO. Cost reductions to the SRO have stemmed from:

- not needing to manually enter data into the SRO database (previously this was contracted out to a data entry organisation. With the e-Business system, requirements for a data entry specialist are no longer needed);
- not needing to manually sort and match EFT payment data;
- reductions in follow up calls to businesses arising from the reduction in processing errors and payments in suspense;
- reductions in Call Centre call time — SRO data shows that the average time taken for an Annual Adjustment has declined from 2:52 minutes in 2001-02 to 2:37 in 2005-06; and
- greater efficiency in auditing and compliance activities due to better and more accurate information.

Moreover, since the inception of the e-Business system, the SRO has been able to shift more resources towards compliance activities.

Appendix A

Appendix

A.1 Pay-roll Tax in Victoria

In Victoria, employers or groups of employers are required to pay Pay-roll Tax if their annual salaries and wages exceed \$550 000. The State Revenue Office (SRO) administers Victoria's Pay-roll Tax regime.

Pay-roll Tax is a self-assessing tax that is payable on the 7th day of each month based on a percentage of total wages paid to employees.¹⁰ At the end of the year, businesses are required to lodge an Annual Adjustment to ensure any shortfall or overpayment of tax is paid or refunded.

As of 2005-06, 23 661 businesses paid Pay-roll Tax in Victoria,¹¹ which roughly equates to 11 per cent of all businesses.¹²

A.2 Summary of the SRO's e-Business initiatives

Electronic Annual Adjustments

Pay-roll taxpayers are required to reconcile their Pay-roll Tax with the SRO each financial year. Prior to the development of Electronic Annual Adjustments, businesses were required to complete their Annual Adjustment reconciliation return manually on a form sent to them prior to the due date.

In the manual Annual Adjustment form of 2001-02, employers were requested to fill in:

- customer details (name, customer number and reconciliation periods);
- total taxable wages paid for the financial year (this included salaries, wages, superannuation, and other breakdown categories);
- estimated wages for the next financial year;
- details of employment agents and the amount of tax paid via agents;
- the history of tax paid to the SRO over each of the last 11 months through the month return process;
- calculated tax liability;
- declaration and contact details; and
- apprentice and trainee wages information.

Completed forms were either mailed or faxed back to the SRO.

¹⁰ In some instances (e.g. businesses close to the \$550 000 threshold), this tax may be paid as a lump sum at the end of the year. Taxable wages include gross wages plus allowances, bonuses, director fees, superannuation, fringe benefits, contractor payments and agency wages.

¹¹ Based on the number of Annual Adjustments submitted.

¹² Based on Australian Bureau of Statistics 2004 data (and inflating this by 1 per cent per annum), we estimate approximately 216 923 businesses in Victoria in 2006. Australian Bureau of Statistics 2004, *Australian Bureau of Statistics Business Register, Counts of Businesses*, Catalogue Number 8162.0.55.001.

In July 2002, the SRO introduced the Electronic Annual Adjustment, where customers can access and complete their Annual Adjustment via a secure online website. The Electronic Annual Adjustment simplified the adjustment process for businesses by:

- having pre-populated fields (such as customer details and other records held by the SRO's databases);
- automatically calculating the amount of tax payable;
- automatically displaying the history of previous monthly payments made to the SRO;
- having user friendly help screens that are hyper-linked to each field for quick referencing and definitions; and
- enabling forms to be submitted electronically.

In 2001-02, 87.47 per cent of Annual Adjustments were completed electronically. By 2005-06, the take up rate increased to 98.69 per cent. The SRO notes that a small percentage of businesses that are still preparing Annual Adjustments manually do so because they do not have Internet access.

Electronic Returns

All monthly Pay-roll taxpayers are required make a payment on their liability each month and they are required to complete a Monthly Return. Eleven Monthly Returns are to be completed each year by taxpayers.¹³

Prior to the introduction of Electronic Returns, taxpayers were sent a form in the mail each month. This form contained instructions on how to calculate their liability and make payment.

The Monthly Return forms requested businesses to calculate and provide their:

- customer number;
- gross taxable wages;
- deduction amounts;
- taxable wages; and
- tax payable.

The lodgement rate of Monthly Returns was low prior to the introduction of Electronic Returns, even though the payment of the monthly amount remained high. In March 2005, the SRO received only 2561 returns from roughly 24 000 taxpayers.

With the introduction of Electronic Returns in 2005-06, businesses are now able to submit their returns electronically using the SRO website. After logging on, businesses simply enter their monthly wages and deductions. The e-Business system automatically calculates taxable wages and the tax payable.

¹³ The twelfth month is rolled into the Annual Adjustment process.

Since its introduction, usage has increased from 8.51 per cent of Monthly Returns (in March 2005) to 96.43 per cent of Monthly Returns (in February 2007). The introduction of Electronic Returns has also resulted in a greater number of customers submitting monthly returns — increasing from 2561 in March 2005 to an average of 18 999 (last six months from February 2007).

Online Payments

Prior to Online Payment, customers had the option of paying Pay-roll Tax using Electronic Funds Transfer (EFT), BPAY, via a cheque, or making payments at the SRO or at a bank.

Since 2005, customers have the option of making a secure payments though the SRO's Pay-roll Tax website ('Online Payment'). Customers can do this by giving the SRO authorisation to deduct monies directly from their bank account. The system prompts customers to authorise a payment when submitting their Monthly Return electronically.

The benefit of the Online Payment process is that the Monthly Returns and payment process can be completed together. Customers are able to save time by not having to undertake separate processes for lodgement and payment — such as logging on to another banking website (to transact by EFT) or mailing a cheque.

The SRO notes that the proportion of customers using the Online Payments function has increased from 9.78 per cent (in August 2005), to 30.86 per cent (in February 2007). The majority of businesses still use EFT payments (41.07 per cent).

During discussion with businesses, it was indicated that EFT payment was preferred because customers want to prepare Monthly Returns in advance of the due date, but do not want to pay tax before the due date. The current Online Payment function only allows payments to be made when Monthly Returns are submitted, not after. Businesses have therefore used alternative payment methods. The SRO has recently implemented an option for 'future dating' of payments to encourage greater take up.

Electronic Records

In July 2005, the SRO implemented an online Electronic Records (e-Records) function that enables businesses to update and check their records online including their legal name, ABN, employer type, entity type, employing period, estimated wage figures, address details, contact details and grouping details.

The availability of this function removed the need for businesses to contact the SRO by letter, fax or telephone every time a change is required. Since implementation, the SRO notes that, on average per year, it has received the following record updates from businesses using e-Records:

- 353 cancellations;
- 344 grouping changes; and
- 22 441 data maintenance updates.

Electronic Register

Also in July 2005, the SRO also implemented the Electronic Register (e-Register) functionality on their website. This enabled businesses to register for Pay-roll Tax online.

Prior to 2005, businesses registering for Pay-roll Tax had to fill in a paper-based form and submit this to the SRO. Businesses are requested to complete the following details:

- customer type;
- legal name;
- employer type;
- date in which the company began employing;
- ABN;
- business activity;
- contact details; and
- address;

The SRO believes that the e-Register function makes it easier for businesses to complete their registration. The process was simplified through the use of drop down fields where the applicants can make a selection using pre-populated data — this eliminates some of the ‘guess work’ involved and improves the data accuracy of the registration. The need for taxpayers to contact the SRO has also been reduced.

Password Required

Since inception, the e-Business system required taxpayers to use a password and username to gain access. Originally these details were mailed to taxpayers but this later changed to internal activation through the online registration process.

As a consequence of this password requirement, the SRO found that a large number of calls to its Help Desk related to customers losing their password and needing password resets. In October 2006, the SRO launched the ‘Password Required’ function that enables customers to reset their password online without needing to call or email the SRO. On average, approximately 6432 password resets are conducted each year.

Direct Credit Allocator (DCA)

Currently, customers making EFT payments are requested to enter the receipt number (customer reference number) on their monthly returns — this allows the SRO to identify who made the EFT payment. Banking institutions issue a unique reference number every time an EFT is made.

Some customers, however, do not enter their customer reference number on their Monthly Returns, or enter the wrong number. As a consequence, time and effort is required to match returns with payments. For the payments where the SRO cannot identify the payee, these payments are moved into a ‘suspense account’.

In 2006, the SRO implemented a new tool — the Direct Credit Allocator (DCA) — to address some of the above EFT issues. The DCA uses business rules to automatically identify and match payments to customers. Since the inception of DCA, the number of tax payments in suspense accounts has been trending downwards.¹⁴

A.3 Key assumptions

Hourly wage rate

The Australian Bureau of Statistics' (ABS) most recent wage statistics indicate that average total weekly earnings for a full time adult in Victoria was \$1086 — or \$56 472 per annum.¹⁵ This is similar to the SRO's estimate of average Victorian wages for businesses subject to Pay-roll Tax (\$54 565).¹⁶

In all likelihood, the salaries paid to staff involved in administering business Pay-roll Tax are different from the State average. For this analysis, the average weekly wages for full-time staff employed in the 'Finance and Insurance' industry sector is used as a proxy for the unit labour cost associated with administering Pay-roll Tax. ABS data indicates that salaries for this industry sector averaged \$1346 per week, or \$69 992 per annum.

In order to convert this to an hourly rate, it is assumed that full-time employees work 44 weeks per year (after annual leave, public holidays and sick leave entitlements), and that the average working week is comprised of 41 hours.¹⁷

The hourly labour cost employed in this analysis is therefore:

$$\$69\,992 \div 44 \text{ weeks} \div 41 \text{ hours} = \$38.80.$$

On-cost ratio

The Victorian Competition and Efficiency Commission suggest an on-cost multiple of 1.75 to be applied to labour costs to take account of overhead costs.¹⁸

These overhead costs include building costs (floor space, fixtures and fittings maintenance, services, etc), equipment, consumables, IT and other support services, administrative support and corporate overheads (senior management, corporate finance, HR, legal services, etc). This assumption is applied to the above labour cost that is adopted in the analysis.

Therefore, the full hourly wage rate including on-costs is \$67.90 per hour

¹⁴ State Revenue Office 2007, Suspense Payments Report, January 2007.

¹⁵ Australian Bureau of Statistics 2007, *Average Weekly Earnings, Australia November 2006*, Catalogue Number 6302.0.

¹⁶ Of the employers that provided employment data to the SRO in 2005-06, the average wages they paid was \$3 764 986 and the average number of full time employees was 47.19; and the average number of part time employees was 25.39.

¹⁷ The 41 hour week is suggested in Victorian Competition and Efficiency Commission 2006, 'Guidance Note: Suggested default methodology and values for staff time in BIA/RIS analysis', which is based on actual ABS data. We note that the average hourly rate would be higher if the maximum weekly hours (37.5 hours per week) as provided in the Commonwealth *WorkChoices* legislation was used.

¹⁸ As suggested in Victorian Competition and Efficiency Commission 2006, 'Guidance Note: Suggested default methodology and values for staff time in BIA/RIS analysis'.

Time savings survey

On 14 March 2007, the Allen Consulting Group met with three members of the SRO's Business Reference Group to discuss the benefits of the e-Business system. The time savings for Annual Adjustments and Monthly Returns, as indicated by these businesses, is presented in Table A.1 below. Also presented are the savings, as estimated by the SRO, and by another business ('Business 4') that is not a member of the Reference Group.

Table A.1

ESTIMATED SAVINGS

	Business 1	Business 2	Business 3	Business 4	SRO internal estimate
Annual Adjustments					
Manual	2 days	3 to 4 days	1 day	2 hours	50 minutes
e-Business	0.5 to 1 days	1.5 days	0.5 days	1 hour	20 minutes
Savings	8 hours	16 hours	4 hours	1 hour	30 minutes
Monthly Returns					
Manual	3 to 4 hours	2 hours	2 hours	40 minutes	6 minutes
e-Business	10 to 15 minutes	2 hours	1 hour	30 minutes	3.5 minutes
Savings	3 hours	No noticeable impact	1 hour	10 minutes	2.5 minutes

Note: 'Business 4' was not part of the SRO Business Reference Group.

Avoidable costs

This analysis only considers those information collection costs that are unique to the Pay-roll Tax regime. In the absence of the Pay-roll Tax regime, the collection of Pay-roll Tax data such as wages and employee information would still be required by federal agencies such as the Australian Tax Office, ASIC and other regulators. As such, these general accounting and data collection costs are not included in the base case analysis as they are not avoidable costs attributable to the Pay-roll Tax regime.