

Administrative scale

Overview

- 1 On 13 June 2023, the Commission issued a [consultation paper](#) on the administrative scale assessment. The Commission considered changes since the 2020 Review and their implications for the assessment method.
- 2 The Commission proposed to retain the 2020 Review assessment method.
- 3 A summary of state responses to each consultation question is included below, as well as the Commission's draft position and the draft 2025 Review assessment method.
- 4 State submissions can be viewed [here](#).

Consultation questions

Q1. Do states support the continuation of the administrative scale expense assessment in its current form?

State views

- 5 New South Wales, Victoria and Queensland did not support the continuation of the assessment in its current form. They said that the costs are overstated and do not represent the true minimum costs underlying the conceptual case of the assessment. Other states supported the assessment or did not express concerns.
- 6 Victoria said that other assessments, such as schools and health, already account for fixed costs. It said this means the application of the administrative scale adjustment imposes double counting and that these costs should be netted out.
- 7 Western Australia, South Australia, Tasmania, and Northern Territory indicated that there was no evidence to suggest that the minimum fixed costs of running state services had changed since the derivation of the costs in the 2020 Review. These states said that applying indexation annually to the current assessment would sufficiently maintain contemporaneity for the 2025 Review.
- 8 While the ACT did not express concerns about the current methodology, it recommended that the Commission should rederive administrative scale expenses in the future. The Northern Territory was also open to this, although advising that it may not be feasible within this review.

Commission response

- 9 Regarding Victoria's concern about potential duplication of fixed costs, the Commission notes that fixed costs in specific assessments are distinct from those being measured in the administrative scale assessment.
- 10 For example, service delivery scale in schools accounts for the recurrent fixed costs incurred in running individual schools. It accounts for the need to establish smaller schools as a result of dispersed populations. The fixed cost of establishing and running an education department in the administrative scale assessment is a separate cost.
- 11 Regarding the views of New South Wales, Victoria and Queensland that administrative scale expenses are overstated, the Commission accepts that there is uncertainty around the level. However, it is not aware of any systematic bias in its estimates, or evidence to suggest that the minimum fixed costs of running state services have changed since the 2020 Review.

Commission draft position

- 12 The Commission considers the detailed analysis underpinning the assessment remains valid and proposes to retain the current adjustment.

Other issues raised by states

Centralisation

- 13 New South Wales, Victoria and Queensland said the quantum of expenses is overstated and should be rederived with consideration of the potential for cost reduction through the use of shared services and outsourcing.
- 14 These states referenced the consolidation of corporate services, saying that many departments in smaller states pool corporate services (such as payroll, human resources and communications) to generate efficiencies in service delivery.
- 15 Additionally, Victoria said that the design of stylised minimum staffing structures guided by administrative structures in smaller jurisdictions does not capture what states do and allows for policy contamination.

Commission response

- 16 The Commission agrees that shared services and outsourcing can reduce costs. However, even under an outsourcing and shared servicing approach, some minimum corporate service costs remain.
- 17 In the 2020 Review, the Commission examined the prevalence of outsourcing and shared servicing in each core head-office function in different states and factored that into the derivation of the quantum.

- 18 The Commission found that states used shared services differently in different areas. For example:
- First Minister’s Department, *has a Corporate Services (or similar) unit. They are at least branches and are division equivalents in the large States... Some States have shared service providers to provide transactional processing services, but not policy and oversight services.*
 - Public Service Commission, *each Commission has its own corporate services area in most of the larger States, but those services are provided by a parent department or a shared service provider in the smaller States.*
 - Audit Office, *larger States have corporate and support services units. Shared service providers deliver most of those services in Tasmania, the ACT and the Northern Territory, but the Audit offices have resources for managing the services.*¹
- 19 The Commission found that in all cases of shared servicing and outsourcing of corporate services, some staff and resources had to be retained to coordinate and manage those services. The amount of shared services required by an agency are largely proportional to the size of its task. The Commission considers that the fixed costs elements of human resources, information technology and other services are unlikely to be materially affected by the change in the level of centralisation or decentralisation of those services since the 2020 Review calculations were made.
- 20 In the 2020 Review, the Commission adopted a comprehensive process, involving extensive data collection from states, to construct a hypothetical organisation chart reflecting the minimum staffing structures for each state function. The recalculation distributed only an additional \$6 per capita nationally compared to the 2019 Update (which had relied on the quantum derived in the 2004 Review). In the absence of evidence indicating material changes since the 2020 Review, the Commission decided it was impractical to re-estimate administrative scale in this review. It calculated the size of the task in the 2004 and 2020 Reviews, but did not in the 2010, 2015 or 2025 reviews.
- 21 The Commission accepts that what the smaller states do has a stronger bearing on its calculation of the minimum administrative task than what the larger states do. However, it does not consider that this provides any policy neutrality concerns or dominant state effect. The Commission is not aware of any evidence indicating that smaller states are responding to theoretical incentives and creating a bureaucracy for administrative scale type functions that is significantly larger than other states.
- 22 The 2020 Review method assumes departmental structures of smaller jurisdictions more closely represent the underlying concept, which is the theoretical minimum staffing structure. The Commission considers this approach is not policy contaminated and is the most appropriate way to estimate what ‘states do’, or at

¹ [Commonwealth Grants Commission \(CGC\), 2020 Review - Draft assessment paper - Administrative scale, CGC, Australian Government, 2018.](#)

least ‘what states would do’, in the hypothetical scenario of a minimal level of service delivery scale.

- 23 The Commission accepts that state departmental structures may have changed since the collection of data in the 2020 Review. For example, it is possible that states have become more centralised to maximise the efficiency of a centralised system, or less centralised to maximise the responsiveness of a devolved system. No evidence has been provided to demonstrate that any state has systematically changed their approach in one direction or the other since the 2020 Review.

Commission draft position

- 24 The Commission proposes to retain the current methods for assessing administrative scale for the 2025 Review. It plans to include a broader examination of the impact of administrative scale as part of its proposed forward work program.

Wage related costs

- 25 The administrative scale assessment is calculated based on an assumed number of staff required to perform a function. To calculate the associated total spend, the Commission estimates the average wage per employee, and the non-wage costs per employee.
- 26 New South Wales said that labour costs should comprise a larger proportion of total administrative costs. It supported the argument by presenting data that compared departments with the primary organisational objective of policy design and corporate functions (non-service delivery departments) and service-delivery departments. The data suggested that non-service delivery departments have a higher proportion (around 80:20) of labour related costs than the Commission’s 60:40 estimate. It said that service-delivery departments have a lower proportion that is more in line with the Commission’s estimate.
- 27 New South Wales said that non-service delivery agencies more closely align with the concept of administrative scale, the theoretical minimum staffing structure. It suggested that in the absence of service volume, costs in running core head-offices would be overwhelmingly driven by labour costs.
- 28 New South Wales and Victoria said that the labour cost proportion should not be applied to Australian Public Service salaries and that it should instead be applied to each jurisdiction’s salaries, given the substantial differences in public service salaries between states.
- 29 Queensland also disputed the assumption that 60% of costs are attributable to labour.

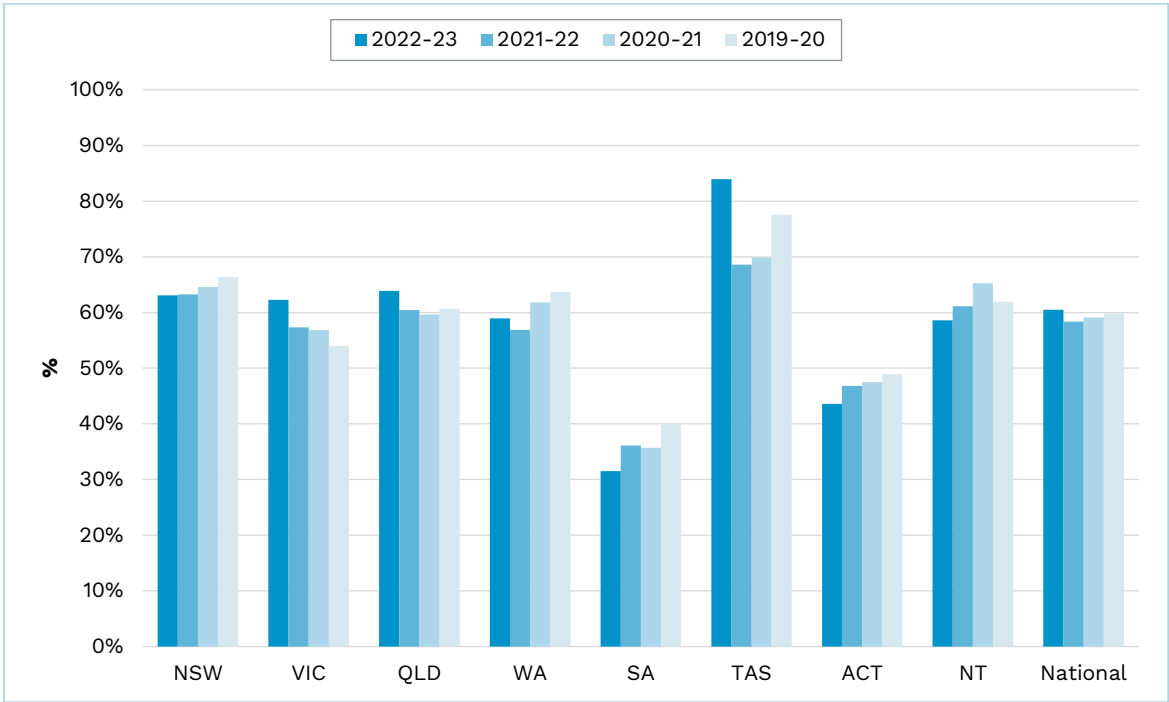
Commission response

- 30 In the 2020 Review, the Commission used Commonwealth public servant classifications and salaries, as there is no single state classification, and no way of

identifying an average state classification. The Commission considers this rationale remains appropriate. Differences between the salaries paid to state and Commonwealth public servants to undertake comparable work are likely to be a minor issue in terms of the overall appropriateness of the assessment.

- 31 The Commission accepts that different departments in different states have variable proportions of labour costs. It also shares a similar view to New South Wales that in deriving this proportion, it should restrict its focus on data representing administrative costs of operating core head office functions. By design, these costs are likely to be dominated by costs attributable to corporate functions and policy development.
- 32 The Commission investigated using those classification of functions of government categories from Government Finance Statistics, but the data across states appeared inconsistent, with some states having 100% labour costs for some functions.
- 33 The Commission has instead used annual report data from First Ministers’ departments in all states for the last 4 years.

Figure 1 Percentage of costs that are wage related for First Ministers’ departments



Source: Annual reports from the First Ministers’ departments for various states.
 Note: Grants, intergovernmental transfers and interest expenses have been excluded. Data for ACT represents the Chief Minister, Treasury and Economic Development Directorate.

- 34 The First Ministers’ departments are primarily a non-service delivery function of each state and part of the core head office functions included in the assessment. The proportion of expenses that are employee related are approximately 60% nationally, supporting the Commission’s estimate of the labour intensity of administration.
- 35 In small states, a high proportion of departmental expenses relate to the core concept of administrative scale. In large states, this is a lower proportion. The

absence of any evident relationship between state size and labour intensity of First Ministers' departments suggests that both administrative scale driven expenses and service delivery scale driven expenses have similar labour intensity.

- 36 Higher non-wage related costs for South Australia were driven by substantial investments in IT, analytics and communications services over this period.
- 37 The Commission considers that using Government Finance Statistics for all state functions is more appropriate than selecting specific government departments, such as First Ministers' departments. It considers the use of First Ministers' departments data to be a validation of its current approach, rather than a superior approach.

Commission draft position

- 38 The Commission proposes not to change the 60:40 wage cost to non-wage cost ratio in administrative scale expenses.

Diseconomies of large scale administration

- 39 Referencing academic literature, New South Wales and Victoria said that large states face diseconomies of scale in administration. They said that assessing unavoidable fixed costs but not assessing unavoidable costs arising from large populations is an asymmetrical approach favouring smaller states.
- 40 New South Wales and Victoria referred to a paper by Chan and Petchey (2024)², which argues that states with larger populations have higher costs per capita attributable to congestion.

Commission response

- 41 The Commission accepts the New South Wales proposition that, relative to smaller states, larger states often have more agencies, more complicated organisational structures, a larger number of senior executives and higher paid senior executives. This increased complexity is captured by the Commission's current model of a linear relationship of service delivery. This reflects that a large state needs more teachers than a small state, and more senior bureaucrats. However, to identify diseconomies would mean that New South Wales (with 17 times the population of the ACT) needs more than 17 times the number of senior bureaucrats. The Commission has seen no conceptual case or evidence for this.

² F. Chan and J. Petchey, *The Cost of Congestion for State and Local General Government Services in Australia*, *The Australian Economic Review*, 2024, vol. 00, no. 00, pp. 1–21, DOI: [10.1111/1467-8462.12543](https://doi.org/10.1111/1467-8462.12543).

Box 1 State population and expenses

The administrative scale assessment considers the relationship between population size and costs of administration. There is the broader question of the range of mechanisms that may influence the relationship between total expenses per capita and population size.

The Commission considers there is a conceptual case that large cities can drive higher per capita costs in service delivery. For example, it assesses needs relating to population density in the transport assessment. There is also a conceptual case in the justice assessment, the evidence for which will be considered by the Commission when it analyses state data (see Justice chapter).

Chan and Petchey (2024) argued that that the complexity of the entire system increases with population, and that an additional 10,000 people in either Sydney or Byron Bay increases the complexity of the New South Wales government system, such that costs per capita increase.

Chan and Petchey (2024), argued that spending per capita increases with increasing state populations. This was based on a finding that the national total state and local government expenditure per capita rose between 1983 and 2024. With Australia’s population growing over this period, they found a correlation between higher population and higher costs per capita. Assuming over this period governments “maintain[ed] the per person benefit provided”, they found a relationship consistent with increases in population driving a reduction in efficiency, or diseconomies of large scale due to increased congestion.

Commission draft position

- 42 The Commission proposes not to assess diseconomies for large administrative systems for the 2025 Review. It will continue to examine the conceptual case and evidence for the range of mechanisms that may influence the relationship between total expenses per capita and city or total state population size.

Draft 2025 Review assessment method

- 43 Table 1 shows the proposed structure of the 2025 Review administrative scale assessment.

Table 1 Proposed structure of the administrative scale assessment

Component	Driver	Influence measured by driver	Change since 2020 Review?
Administrative scale	Minimum size of administration	Recognises that there are fixed costs of administering a state, that do not vary with the size of the state	No
	Wage costs	Recognises the differences in wage costs between states	No

Indicative distribution impacts

- 44 No method changes are proposed for this assessment.