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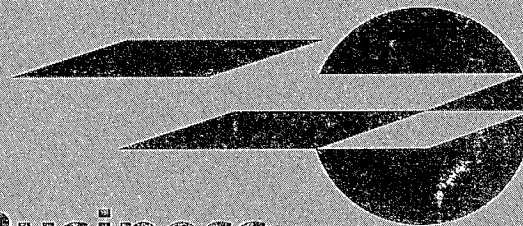
Government
of Canada

Gouvernement
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Guide and Manual for Determining the Impacts of Regulation on Business Activities and Their Costs:

A Functional-Based Approach to Regulatory Costing

Business Impact Cost Analysis Protocol (BICAP)



The Business Impact Test

BICAP

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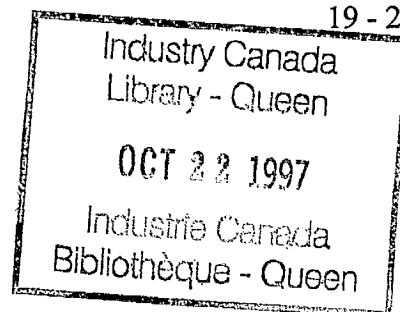
**GUIDE AND MANUAL FOR DETERMINING THE IMPACTS OF REGULATION
ON BUSINESS ACTIVITIES AND THEIR COSTS:
A FUNCTIONAL-BASED APPROACH TO REGULATORY COSTING**

**Developed by: Industry Canada
Treasury Board**

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Preface

The cost of regulations and their potential inhibiting effects on Canadian business have been a central theme of governments throughout the last decade. One of the major impediments to informed discussions has been a lack of hard cost estimates for the regulatory burden. The result has been that there is little information with which to determine which regulatory requirements impose a burden and which do not. One key problem has been the lack of a methodology to systematically gather information on the impact of regulations on the way a company does business, and to determine associated costs.

To find a better way to assess the impact of regulations, the Federal Government turned to the private sector for assistance and advice. The experience that Canadian business has gained over the last decade in their efforts to reduce costs was considered to be an invaluable starting point for this exercise. Specifically, the business community was asked to help in the development of methodologies to identify where opportunities exist - to come up with refined less burdensome regulatory systems which meet government's policy objectives.

The "Business Impact Test" (BIT) was developed as an aid to consultations on the nature of the impacts of regulation on business, and to the design of lower cost regulatory systems. The BIT is based on a formal model of how businesses see regulation impacting on their companies, and of the sources of these impacts in respect to the actual way Canada's regulatory system is designed. While capable of describing regulatory impact, the BIT does not provide information on hard costs or verification of the observations it collects. To meet these needs, the Business Impact Cost Analysis Protocol (BICAP) was developed as a complement to the BIT.

The BICAP provides a formal interview approach to verifying how regulation interacts with business functions, and an accounting standard and formal methodology for estimating the incremental cost of new or improved, as well as existing, regulation. The accounting standard focuses on incremental costs, ie., those which are directly and solely related to regulation. Thus, it provides a formal distinction between normal business activities that incidentally support regulation and the real added cost of regulation.

On behalf of the Canadian Manufacturers Association¹, Mr. John Carlos, Director of Taxation at Dupont, has led a small working group of senior company officials, all professional accountants, who guided the development of BICAP and its supporting costing methodology---the two Accounting Protocols. To a large extent, the methodologies for analysis of business impact and the costing methodologies reflect the experience of the members of the working group in

¹The Canadian Manufacturers Association (CMA) recently changed its name to the "Alliance of Manufacturers and Exporters Canada".

managing major cost reduction projects at their respective companies. Mr. Chris Everingham of Everingham Associates, worked with the working group to develop the Accounting Protocols and the Guides to their use. The Accounting Protocols have now been tested in the Information Technology, Automotive and Forest sectors and approved by Mr. Carlos' working group.

ADVISORY WORKING GROUP FOR COST OF COMPLIANCE PROJECT - BICAP

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Guide to Determining the Impacts of Regulation

Purpose of Guide

This Guide provides information to government regulators and their managers on how to evaluate impacts of existing or proposed regulations on business operations and decisions. It is written specifically for regulators who might not have specialized or in-depth knowledge of business impact analysis or cost accounting procedures.

The "Analysis Protocol" outlined in this Guide is referred to as the Business Impact Cost Analysis Protocol (BICAP). It is one of the components of the Business Impact Test (BIT) Process². BICAP is a formalized approach to conducting business interviews. Through it, business interviews are designed so that they will be able to identify how regulation affects business functions, decisions and incremental costs. The interview process collects both qualitative information and quantitative data on the changes that occur in business practises as a result of regulation. The Guide demonstrates the advantages of using this particular data gathering method, rather than other approaches, to evaluate the impacts of regulations on business operations. It provides accounting standards for determining the true incremental cost of regulation.

Guidance is provided on when the BICAP should and should not be used, and on the advance preparation necessary to ensure that results are effective and useful. The differing roles of regulator and consultant are explained, and the technical and interview skills required by consultants are detailed.

Lastly, estimates of the amount of time an average organization requires to complete interviews are provided. These estimates are based on actual field experience obtained during the development process. The Guide also outlines the range of results that can be derived from the BIT Process.

²The BIT Process is a formal system of consultations designed to collect businesses' observations on how regulation affects the way they conduct and manage their business, and/or the opportunities to reduce costs. The Process involves two components: application of the Business Impact Test to collect observations and; detailed analysis and verification of these observations through formal firm level Business Impact analysis with the Business Impact Cost Analysis Protocol.

Regulatory Impacts on Business

Regulations can impact business in direct and indirect ways. In both cases, impacts are incremental to business activities. Incremental impacts refer to activities that are carried out in a business solely as a result of a regulation and which would not be present in the absence of the regulation.

To comply with a regulation, the activities and practises of a firm are changed, or new activities and practises are introduced. "Business practises" refers to the polices and processes a company follows to determine how activities and decisions are carried out. Both can be changed by regulation, and must be examined to understand how regulations influence business. Direct impacts of regulations can change the "way" businesses do things. They can affect such business activities as hiring, record-keeping, job-training and workplace health and safety practises.

Regulations can also have indirect impacts on the long-term strategic directions and decisions of companies. Indirect impacts affect "how" decisions are made in a company. Indirect impacts can result in a firm not being able to improve its management practises to the industry standard, in market distortions that will cause a firm to exit one market in favour of another, and distortions that lead development and production practices away from those which are most effective. As well, indirect impacts can arise which limit a firm's access to financing, or influence how it expands or establishes business relations. These indirect impacts may not be felt by a business immediately. Rather, as the indirect demands of regulations are internalized, they implicitly become part of the company culture, and in turn influence its long-term strategies and decisions. Regulatory requirements might even force a company to carry out its activities in a way that is not "best business practice".

The Business Impact Test (BIT) is designed to identify the perceptions held by a firm's management regarding how regulation impacts its operations, both directly and indirectly. Understanding these perceptions is important because they influence actions and decisions. Ultimately, there is a need to determine whether the perceived impacts are the true impacts, in order to help determine the best way to improve regulations. In cases where perceptions are false, information and educational programs may be needed. On the other hand, when the impacts are real but unintended, regulatory refinement may be in order. Because of the complexity of regulations and their impacts, and the need to separate perceptions from reality, face-to-face interviews with business managers are often necessary to assess situations with accuracy and confidence.

The BICAP uses in-depth interviews to provide a structured approach to characterizing the types of direct and indirect impacts that have occurred or could occur. Overall, this process supplements and enhances the observations obtained through BIT consultations.

As part of the BICAP interview process, data is gathered to complete a detailed costing of the various impacts using the methodology of two Accounting Protocols. The Accounting Protocols are self-contained procedure manuals for use by a consultant to determine the incremental cost aspects of a regulatory impact. They follow standard accounting practice regarding definitions, cost principles and documentation methods. The Accounting Protocols for measuring the incremental impact of regulations are attached under Tab A and Tab B.

Background to Regulatory Business Impact Analysis And the Business Impact Cost Analysis Protocol (BICAP)

Canada's Regulatory Policy requires that regulatory programs be structured to maximize net benefits to beneficiaries, and that steps be taken to ensure that regulation does not unintentionally impede Canada's competitiveness or the private sector's capacity to generate wealth.

Regulations exist for the most part, to protect Canadians. They create a need for businesses to develop efficient methods to enable their business practises to conform to compliance requirements. Business and regulators can often agree on the objective(s) of regulations, however, they tend to disagree on how the objectives can best be achieved. Much of this disagreement arises when regulators do not understand how businesses operate, and create requirements which appear unnecessary or inefficient from a business perspective.

New and existing regulations pose a fundamental challenge: government and business must improve their communications with each other, in order to balance their needs and concerns. It is only through focussed dialogue that cost effective and efficient regulation can be obtained. To obtain this dialogue, information is needed on the incremental costs of regulation on business: why they arise and how they can be minimized.

Industry Canada, Treasury Board of Canada and the Canadian Manufacturers Association jointly developed the Business Impact Cost Analysis Protocol (BICAP) to assist regulators and business to better understand how regulatory burdens arise and how their impacts can best be minimized. The BICAP is a structured interview protocol, designed to assist government in obtaining authoritative information on the impacts of regulations on business, and to find solutions for problems that might be caused by regulations. It includes two Accounting Protocols to identify the associated costs of regulations.

The BICAP is designed to complement the Business Impact Test (BIT). The BIT consists of a set of detailed questions that identify the actual causes and sources of regulatory problems. It is a process designed to collect business observations, while not creating an unnecessary burden on business. Business played a large role in setting priorities for the subjects covered in this test, and in actual test design.

The BICAP is a tool to verify the nature of the potential incremental impacts identified by the BIT, and to obtain cost estimates for them. While the BIT collects observations and qualitative information, BICAP verifies such information through interviews with those affected and by obtaining quantitative estimates of incremental costs. The BICAP uses standardized

methodology to develop a clear picture of the practises and the activities followed by a firm to comply with regulations. Its methodology uses accounting standards and practises to assign incremental costs to regulatory burdens, while minimizing inconvenience of the BICAP process to participating companies and organizations.

The BICAP uses interviews with hands-on company mangers to obtain a clear picture of how a firm departs form "normal" business practices in order to respond to regulation. Once this is done, costs and benefits are calculated based on estimates of the incremental costs of new activities arising because of regulation.

Advantages and Unique Features of the BICAP Process

Business management practises and accounting procedures are not standardized; nor are they designed to isolate incremental regulatory costs. This can make it difficult to understand why compliance practises related to a particular regulation will vary among companies and to obtain comparable incremental cost data. The BICAP was designed to address these problems. The information it provides identifies normal business practises and costs, as well as those of parallel activities that arise because a firm must meet the requirement of a specific regulation.

The costs of the parallel activities which arise because of regulation are described as incremental since they are incurred directly as a result of compliance with the regulation, and would not be incurred in the absence of the regulation. The concept of incrementality can be used to assess the impact of regulations on a company, as opposed to its on-going normal business activities and costs.

The Accounting Protocols were developed by senior accountants in the private sector, specifically to assign incremental costs to regulatory burdens. They are designed to separate normal business expenses from real regulatory costs. They are based on standard procedures used by business in cost reduction exercises, and well-established cost accounting principles. They provide an accounting standard for obtaining the true incremental cost of regulations. (see Tab A and Tab B)

Regulators need assurance that a methodology for estimating regulatory burden will produce information that accurately represents the true impacts and incremental costs of regulation. The BICAP and its associated accounting protocols provide a high degree of such assurance for four reasons :

1. BICAP is based on functional cost accounting; a specialty within general accounting which requires advanced professional training and experience.
2. BICAP interviews and cost analyses are to be completed by independent consultants, to maintain the confidentiality and integrity of information.
3. BICAP provides a structured and analytical approach to interviewing businesses, in a manner that obtains reliable and substantive information from management personnel who are responsible for a company's compliance activities.
4. BICAP provides criteria for the selection of consultants with appropriate qualifications to use the BICAP. These qualifications include a professional accountant designation and training, as well as practical business experience in functional analysis and cost reduction.

There are benefits to utilizing the BICAP rather than *ad hoc* data gathering methods. The methodology of BICAP can produce consistent analyses of how businesses adjust their activities and practises, as well as estimates of associated costs. As noted, it is designed to distinguish costs which would have occurred anyway and those which truly arise due to regulations. The major problem with most other information gathering techniques is the lack of in-depth interview detail and their inability to compare and contrast the data between companies or industries.

Entity Compliance Model (ECM)

One feature of the BICAP is its requirement for the completion of a detailed written description of the practises and activities that firms have adopted to achieve compliance with the regulatory requirements. This description is called the Entity Compliance Model (ECM). The ECM documents what compliance activities are carried out and where, how they are performed and why they are performed (See Tab C for details).

The ECM is a system flowchart---a series of interconnected boxes that describe all aspects of compliance activities in an organization. Each box represents a function, activity or step required by the organization to comply with the regulation. The description includes the activities of people or their functions, payments for outside services, and tangible or intangible assets used to meet compliance requirements. Compliance activities include the monitoring of regulatory changes, internal administration and accounting, preparation of periodic reports, audits, dispute resolution, etc.

The ECM is initially developed through discussions with regulators and others familiar with common business practices, about how they perceive the ways in which a company achieves regulatory compliance. Their perceptions are then validated or contradicted by interviews with the actual managers within the business who have daily responsibility for compliance activities related to the specific regulation that is being investigated.

The advantage of this two step ECM process is that a very clear picture emerges of the actual compliance activities of a business, of unintended or unexpected changes to business activities, and how these change as business requirements change.

Once a thorough understanding is gained of how regulatory requirements change the practises and activities of a firm, estimates of the incremental cost of these changes are developed. This entails the use of traditional business functional analysis and activity-based costing rather than accounts-based costing. Interviews are used to determine these costs, since simple survey and questionnaire approaches are flawed; for example, the wrong person might provide the information, or might have a lower sense of accountability than when interviews are conducted.

As noted, the key point with the BICAP is that interviews are conducted with company representatives who directly manage the compliance activities and have the requisite knowledge of company management practises and cost structures to provide knowledgeable estimates. In addition, it requires that interviewers have substantial cost accounting experience and be familiar with the business management practises that may be used by the firm. The process draws directly on the well-established methodologies of business function analyses, cost reduction and cost accounting. It requires that interviewers have established track records in using these techniques effectively. All enhance the authority of BICAP results.

When to Use the BICAP

The BICAP can be used to evaluate the impact of existing regulations, or to determine the consequences of proposed regulatory change. The results contribute to cost/benefit analysis and can be used to refine regulation so that it is more effective for government and more efficient for business.

The BICAP can be utilized to establish benchmarks of incremental regulatory costs within an industry. With the BICAP methodology, the impact and incremental cost of regulations can be followed over time in a number of firms representing typical business practises. These firms can serve as markers of incremental regulatory costs, and hence can demonstrate the success or failure of government efforts to reduce regulatory burdens. Such benchmarks can help determine the ongoing effectiveness and efficiency of regulation, as well as the costs of compliance.

Finally, the concepts and methodologies of the BICAP can be applied to determine regulatory impacts and costs in any type of organization (eg., profit or non-profit, public or private). They can be used with reference by any organization regardless of its size, purpose or activities.

A firm's overall response to regulation through the BICAP process will be most evident in organizations that have a hierarchial management structure, with some form of central control and focus, or in those with structurally similar management systems throughout the organization.

In such companies, the results obtained from the study of one branch will be representative of the other entities in the firm. If a firm is made up of relatively independent operations with differing management styles, the results from one area (eg., a division) are much less likely to reflect the firm's overall costs, but rather reflect only those of the entity being studied.

When the BICAP is to be applied to a group of regulations, it is necessary that interviews focus on individual regulations which have a high degree of similarity with regard to how compliance is obtained. In other words, the regulations considered should impact on similar functions or activities in a firm. When this occurs, the functions affected by each regulation will be easier to identify and the associated costs can be determined in one interview. For example, commodity tax regulations and income tax regulations are often managed by the same tax department in a business. Consequently, regulatory changes in the two areas could usually be covered with interviews at one company location, and possibly with the same individual.

On the other hand, environmental regulation is normally managed in different cost centres than taxation. Under this circumstance, regulations impacting on differing cost centres cannot be dealt with under the matrix of the same interview. Thus, multiple interviews could be required during the use of BICAP.

Even if regulations appear to be managed similarly, they should be carefully evaluated in terms of the particular company's actual practice. This is because in some companies, the responsibility for certain regulatory activities might not be found within one cost centre. For example, this could happen if a corporate office accountant handled federal income tax, while provincial income tax activities were delegated to a different provincial operating unit. Multiple interviews would then be required.

When Not to Apply the BICAP

The BICAP does not measure actual incremental costs but rather estimates the incremental costs a company incurs in complying with regulation (i.e., its results are based on estimates of the activities or "work" of individuals). This in-depth costing approach process does not apply when the only impact is a one-time cost that does not create an on-going functional change. This could occur when a regulation only requires a single change in the production process--such as a design change to machinery used in production, or the one time costs of converting unilingual packaging and labelling to meet bilingual requirements.

The indirect impacts that regulations have on the strategic activities of an organization such as forward planning and marketing can be characterized by the BICAP but they cannot be explicitly measured as costs unless a functional change occurs. For example, if a firm restructures itself as a result of regulations, the changes and the reasoning behind them can be detailed but not costed by the BICAP technique.

Since BICAP analysis is function or activity based, a failure to clearly identify the impact of regulations on activities can cause the BICAP interview time and costs to escalate quickly, perhaps even to a point where the entire analytical process might become too burdensome. Not surprisingly, when this occurs an organization will lose interest in participating any further, and/or the benefit of the results can be diminished.

Thus, the BIT Process should not be used in companies where an ECM of compliance activities cannot be developed. This could occur when compliance responsibilities are highly decentralized and individualized. In this situation, the company would likely be unable to identify consistently where impacts due to regulation occur. Too many managers would need to be interviewed and it might be impossible to quantify the incremental costs, or the time required to do so would outweigh the benefit of the entire exercise.

The interviews should not focus on measuring the incremental cost impact of a group of regulations that are not managed similarly. The greater the dissimilarity of managed regulations, the greater the difficulty of determining which functions, activities and cost centres have been affected.

In general, both a government regulator and a consultant should evaluate whether it is practical to use the BICAP in the case of a particular company. Such a decision should be based on a preliminary assessment of the organization's ability to identify and quantify costs, as well as on whether the impact of the regulation, or group of regulations, can be identified within the company's activities.

Application of the BICAP Process to an Organization

As described above, the BICAP is a method for obtaining the incremental costs (both actual and estimates) of regulations from firms, together with qualitative observations regarding the direct and indirect impacts of regulation on the company. A structured interview process consisting of five phases is used to obtain and assess this information.

PHASE 1 Preparation and Cost Driver Identification

This phase comprises two steps. First the consultant must obtain a clear understanding of the requirements of regulatory compliance, and develop an understanding of those factors that will be of concern to business. These factors are called drivers. Drivers are the initial development of an expected ECM. They can be based upon the incremental costs of complying with regulations or they can be the indirect factors that influence strategic planning and longer-term decision making. This preparation is carried out before any contact has been made with a company, and will enable a consultant to understand both the regulation and its expected impacts on a firm.

The second step within this phase will be for the consultant to develop a structured approach to both the questions to be asked during the interviews and to the basic framework of the interviews. This preliminary work is necessary before the consultant goes into the field, because it is particularly important that the interviews be able to determine not just impacts, but how those impacts relate to specific regulatory requirements and business practises.

PHASE 2 Evaluation of the Organizational Structure

As the first step in the actual interview process, it is important to obtain an overall understanding of the company's organizational structure and of where compliance activities are occurring within that structure. This step is to ensure that the preliminary ECM will be confirmed or contradicted by the appropriate level or most knowledgeable person in the organization. This evaluation should examine the normal levels of responsibility in the company to differentiate between strategic corporate roles re: compliance and divisional operational/administrative activities. The inquiry at this point is not directed towards costing regulatory impacts. Rather it is focused on identifying where activities occur, how they are carried out and why.

This evaluation can only be carried out with the assistance of an individual within the company who is both knowledgeable about the management structure and is involved in compliance

activities with regard to the regulations that are being evaluated. The analysis will entail both an examination of the company as a whole, and the company's particular practises and policies. The divisional or functional areas responsible for complying with specific regulations must also be determined and evaluated. Finally, actual activities undertaken to comply with regulations must be identified.

PHASE 3 Application of the BICAP Process to Measure Direct Impacts

To characterize and measure the direct impacts of a regulation, the interviewer must identify all compliance activities, create an ECM for those activities, and relate such activities to regulatory impacts, especially regulatory requirements and business practises. This can be accomplished through the following steps:

1. Identification of company processes and procedures used directly to comply with the regulation, and creation of a model of the company's compliance activities. This will include a determination of how such activities relate to regulatory requirements, and how they reflect business practises.
2. Confirmation with the company of where the impacts of the regulation are occurring for each activity in the model, including what is occurring, why and how the activity relates to business specific practises and regulatory requirements.
3. The impact analyses for each function or activity that is affected are to be categorized within one of three types of costs: personnel, capital and other. These groupings are defined in one of the Accounting Protocols that the consultant will use during the interviews (see Tab A or Tab B).

The personnel impact is expected to be the largest component of a regulatory impact, and analysis should reflect the time required to comply with the regulation, on a recurring and on-going basis throughout the year. It will measure the amount of time required from individuals or functions, either by internal staff or external consultants, that are wholly or partially involved in complying with the regulation.

Capital impacts are to represent the normal annual expenditures for maintenance of equipment and facilities used by the company to comply with the regulation. These could include computer hardware and software as well as monitoring and detecting devices.

Other incremental costs should encompass anything that is neither personnel nor capital based. For example, there could be incremental costs associated with the shut-down of a manufacturing facility, or a special marketing program, or a one-time training program for employees on new safety requirements.

4. The personnel impact is to be valued using an estimate of the annual compensation, including benefits and overheads, for the particular function. Capital and other incremental costs should be valued based on estimates of the invoice prices of the original expenditures.
5. In many cases, the regulatory impact will only be a part of a broader company functional activity or a portion of a larger capital expenditure. For example, compliance with commodity taxation is often part of other responsibilities of the company's tax accountant. Or, environmental effects monitoring equipment may be purchased as a component of a much larger operations machinery upgrade program. In these situations, the regulatory impact must be estimated as a portion of a larger value. The impact on personnel can be expressed as a percentage of their time devoted to the regulation and then multiplied against annual compensation value. In the case of capital or other incremental costs, the impact could be based on the estimated percentage of an asset that is used in compliance versus normal production.
6. Prepare analyses of the regulatory impact on the company. These will cover the nature of incremental costs and dollar values, as well as whether there has been an increase in risk to the company, either directly from the regulation or indirectly through a disruption to the personnel involved. The significance of the regulatory impact in terms of what and who has been impacted, their function and importance to the company may be greater than what the dollar value indicates. For example, an excessive time requirement may be perceived as causing a loss of productive output from talent and capital, or missed business opportunities.

PHASE 4 Identifying and Measuring Indirect Impacts

Using the interview and a list of questions, the consultant must try to determine what indirect effects should be indicated on the ECM. The focus should be on any changes that the company has made, or may make, to adapt to the regulatory compliance requirements. Indirect impacts could be cultural in nature, such as a decision to be more aggressive in tax loss management. Other indirect impacts can be more formal and almost verifiable. For example, new steps may be added to the strategic planning process to cover regulatory changes, or decisions about expansion or reduction may be altered.

Information obtained at this stage by the interviewer can be anecdotal in nature or accounts-based; both types can be relevant. In the former case, the level and qualifications of the individual who is making the comments should be noted. Managers at a corporate level will usually have a more strategic view of an issue, as compared to divisional managers. Both types of information must be assessed in the context of how pertinent the opinion(s) expressed are to the actual management of the issue on a daily basis, and to the long-term or overall scheme of the company.

PHASE 5 Business Suggestions for Regulatory Changes

The BIT and the BICAP processes in general provide complementary and ample opportunities for business to provide comments and suggestions on how better to design the regulation, or find a better way to achieve the objectives of the regulations. In addition, the results of the processes will provide an opportunity for the regulator to learn about business perceptions and their sources, and to identify ways to reduce costs.

Documentation of Findings

Upon completion of the interview and analysis process, consultants should be in a position to deliver the following reports for each company that participated.

- A brief description of the company, its activities and the participants interviewed.
- A clear and concise description of the specific Entity Compliance Model for each regulation under review and how the ECM relates to the business practises of the company.
- A clear explanation as to how the company's operational activities and strategic planning are affected by regulatory change.
- If investigating an existing regulation, there will be a description and summary of the incremental costs related to the functions and activities undertaken for compliance purposes. In addition, there will be a description of how and why on-going activities are affected, the relationship of compliance activities to current business practises, and how strategic planning will be affected.
- If examining a new regulation, there will be a description and summary of the expected incremental costs for the functions and activities affected, as well as explanations as to how activities may change in the future, and how strategic planning will be affected.
- A written report on the significance and relevance of the regulatory impacts on the company. This report will be based on the consultants observations about the relation between the regulatory requirements and their direct and indirect impacts in estimated dollar values, as well as impacts such as the loss of productive output or foregone business opportunities. The report should also provide an understanding of the context of impacts and incremental costs, to explain which issues are important to the company, and why.

Responsibilities of the Regulator in Using the BICAP Process

Since the results of the BICAP will be based principally on estimates and observations from well-informed company managers, the success of the inquiry is largely dependent upon ensuring that the entire process is planned and structured to obtain consistently reliable and credible information.

Normally, government officials do not have the business or accounting expertise which would enable them to apply the BICAP. Therefore, they will have to engage independent consultants to perform the BICAP's detailed analysis, interviews and cost calculations. Since regulators will remain managerially responsible for results, their objectives must be to maximize credibility. In brief, this can be achieved by engaging an appropriate/qualified consultant, who is directed to select companies that are likely to provide useful data, and who is focused on obtaining quality information about all direct and indirect impacts of regulation, as distinct from a company's normal practises or best practises. At times, accountants within a selected company may have the appropriate experience to conduct this work.

The steps required to manage a complete BICAP process for a regulatory analysis are detailed below.

1. Choose consultants who offer expertise in business functional analysis, cost accounting and actual cost reduction exercises, as well as having an understanding of the regulatory subject. Functional cost accounting is a specialty with a requirement for professional qualifications and accountant training. In addition, the consultant should have practical business experience in both functional analysis and cost reduction.
2. Ensure that the consultants have a clear understanding of the purpose, intent and requirements of the regulation, or the proposed changes thereto, by providing background to the creation of the legislation, its implementation and subsequent business reaction.
3. Instruct the consultants to characterize the cost and decision drivers for the affected businesses, including a hypothetical ECM, as the starting point for their examination of the issues.
4. Specifically require that the consultants develop a formal structured approach to the in-depth interviews, including a detailed list of questions to be covered. This is to ensure that all direct and indirect impacts of the regulation are captured.

5. Have the consultants verify their understanding of cost drivers and the regulatory issue through informal discussions with business representatives and regulators.
6. Invite companies to participate in the developmental process by attendance at workshops, by sending an appropriate manager. Select companies that are likely to provide useful data on the impacts of regulation. It is important at the workshop to seek consensus about the range of issues and their priorities, and to obtain preliminary agreement on the cost and decision drivers for the companies. In addition, the participants can assist in identifying the companies that will receive interviews, and the issues to be covered during those discussions.
7. Meet with the consultants after the workshop to review any changes to be made in the initial ECM, the list of questions or the interview strategy before individual company interviews begin.
8. Individual interviews will generally be necessary. Companies will consider some information about their practises and costs to be highly sensitive, confidential, and/or proprietary. In addition, a detailed ECM needs to be completed for each company, because it is necessary to capture individual management practises and decision-making processes to fully understand the regulatory impacts and costs.
9. The regulator should expect to receive a written report from the consultants at the end of the BICAP process. The report should cover the entire project, with a summary followed by detailed reports on each interviewed company. The summary should provide an explanation of the regulations, the interview structure and cost drivers, the nature of the impacts, proposals on how the costs could be reduced and the implications for compliance. Individual company reports should include a detailed analysis of the ECM, an examination of the impact and the nature of regulatory costs as they relate to the company's business practises.

The Role of the Consultant

The consultant is to act as the intermediary between the government and the company to independently determine the impact of the regulation on the company, and provide an assessment of impact, incremental costs and implications for future compliance to the regulator.

A key function of the consultant is to increase the credibility of the results by maintaining an unbiased position relative to both the regulator and the company. The following is a break-down of the consultant's role in using the BICAP.

- To act as an independent interviewer to solicit information from the company on all of the impacts that have occurred, direct and indirect, as well as any relevant anecdotal remarks and perceptions that the company can provide.
- To explain how the ECM relates to the compliance activities required by the regulation and the relevance of the impact to the functional activities of the company.
- To evaluate incremental cost numbers for their "reasonableness", in the context of functional analysis, cost accounting standards and general business experience.
- To summarize all commentary and to complete all cost schedules with information obtained during the interview.
- To facilitate follow-up discussion with the company in reviewing and confirming the accuracy of the data.

Estimated Time to Complete the BICAP Process

The following time estimates are based upon actual field experiences with companies from the Automotive, Information Technology and Pulp and Paper sectors. Actual time required is somewhat dependent on the size and complexity of the company.

Based on actual experience in completing the BICAP, the total amount of time involved for an average company can range from one to three days. An estimate of the time required for consultants to complete their work on the BICAP is as follows:

Phase 1 - Preparation and Cost Driver Identification

- . Meeting with regulators to review the regulations
- . Preparing the estimated cost drivers, the initial ECM and a draft list of questions on the issues to be addressed by the companies
- . Selecting with regulators, potential companies for the workshop and interviews
- . Attending a workshop or meeting with the companies to discuss the issues, prioritize them and identify companies for an in-depth interview
- . **Estimated time - 7 days**

Phases 2, 3, 4 and 5 - Evaluation of the Organizational Structure and Application of the BICAP

- . Meeting with regulators to agree on the post-workshop interview strategy and the questionnaire
- . Completing one interview with one company per day to obtain confirmation of the ECM, the direct and indirect impacts and suggestions for regulatory improvements
- . **Estimated time - one day per company**

Documentation of Findings

- . Preparing a report on the entire process and obtaining the companies' agreement on its content
- . Summarizing the efficiency and cost reduction recommendations of the individual reports to the companies and to the regulators
- . **Estimated time - four days per company**

As consultants gain experience with the interview process, they should be able to combine steps to save time. For example, in the Information Technology sector, the first two steps were combined when dealing with small companies. The time required for completion varied from a minimum two hours to a maximum of three-quarter of a day.

Guide to Determining the Impacts of Regulation

Preface: Accounting Protocols

There are two Accounting Protocols underpinning the BICAP and the choice as to which one to use will depend on the nature of the regulation that is to be examined - whether the regulation exists or whether it is proposed.

Tab A) For Existing Regulatory Requirements

A cost accounting protocol for use by a company to determine the incremental costs of complying with one or more existing regulations. This Accounting Protocol is concerned with measuring the incremental impact on costs that have resulted from proposed Changes.

Tab B) For Proposed Changes to Regulatory Requirements or Proposed New Regulations

A cost accounting protocol for use by a company to determine the incremental costs of complying with proposed new regulations or proposed changes to existing regulations. This Accounting Protocol is concerned with measuring the incremental impact on costs that is expected to result from proposed changes.

TAB A

**ACCOUNTING PROTOCOL
FOR USE TO DETERMINE THE
INCREMENTAL COSTS OF COMPLYING
WITH EXISTING REGULATORY REQUIREMENTS**

**ACCOUNTING PROTOCOL
FOR USE TO DETERMINE THE
INCREMENTAL COSTS OF COMPLYING
WITH EXISTING REGULATORY REQUIREMENTS**

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SCHEDULES AND WORKING PAPERS

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THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

Introduction and Criteria For Use

This Accounting Protocol has been designed to be used by an independent consultant to the government to determine the incremental costs to a company to comply with existing regulations. Of course any qualified accountant, whether independent or not could equally use the Protocol, albeit there are advantages to using an independent consultant. Please refer to the "Role of the Consultant" in the Guide.

It can be used for one regulation, a group of regulations or for all regulations that affect a company. In addition, it can cover one or more levels of government.

A large or complex organization will require the consultant to evaluate its structure before this Accounting Protocol can be applied. The purpose of an evaluation will be to determine the level at which compliance activities occur in the organization and the appropriate application of the Accounting Protocol to measure the resulting incremental costs.

Such an evaluation should consider at least the following general aspects of organizational structures:

- I: Corporate level - what are the Policies for complying with regulations
- II: Divisional level - what are the Practises to comply with regulations
- III: Operational level - what are the Applications to comply with regulations

In less complex organizations, these levels of responsibility may be found in one location and possibly in one individual.

The methodology of this Accounting Protocol, including the instructions and working papers that follow, is written on the presumption that these evaluations have occurred and that the organizational entity or business unit affected by the compliance requirements has been identified for purposes of cost measurement.

The results from the Accounting Protocol can be used by anyone to analyse the current status of the incremental cost of regulations, including work by academics and statisticians as well as businesses and governments.

The concepts and methodologies that support the Accounting Protocol and the various

schedules in this package are neutral enough that they could be equally applied to any type of organization: business, labour or non-profit.

Companies and industry sectors are to be approached by government at a senior executive level to determine whether the companies will participate in this incremental cost compilation study on a voluntary basis.

For each intended use of this Accounting Protocol, all parameters will be jointly developed in advance by government and industry and there will be mutual agreement of all aspects and requirements of the study before its commencement.

These parameters will at least include the period to be studied, the regulations to be considered, the industry sector and the participating companies and the role of the consultant engaged by the government.

The specific regulation numbers, the types of regulation, or the areas of regulatory activities to be considered will be prepared by the government in consultation with business to be of maximum relevance to the industry sector that will be under study. This list will be included under *Schedule 3, Question 2* of the Accounting Protocol.

For purposes of determining the incremental cost of compliance, regulatory requirements ("Regulations") means all types of statutory directives with which businesses must comply, including acts, legislation, regulations, orders, by-laws, proclamations and warrants.

Costs to be measured by the consultant are those incremental costs that are caused by regulation and which would not exist in the absence of regulation.

Incremental Costs are to be categorized as follows:

- 1) Incremental personnel costs to be measured using a functional approach;
- 2) Incremental capital costs, and
- 3) Other incremental costs, neither personnel-based nor capital in nature.

The methodology is not accounts-based and will rely on the consultant to solicit informed business judgment to identify activities or estimate incremental costs that are wholly or partially the result of compliance.

A preliminary step to completing the Accounting Protocol will be for the consultant to develop an understanding of the systems and procedures that the entity currently uses to comply with the regulations being investigated; ie. an "Entity Compliance Model" (ECM).

An Entity Compliance Model (ECM) should document where compliance activities are performed, how the activities are performed and why they are performed.

The model will be important to the evaluation of the impact that the regulations have had on the entity's compliance activities and its incremental costs. This model building should be carried out as part of the Activity Analysis on Schedule 3.

It is also a prerequisite for the consultant to determine with the company whether it is practical to use the Accounting Protocol in its particular circumstances. The impact of the regulation(s) may not be measurable if:

- . the company cannot identify where the impact occurs
- . the incremental costs cannot be quantified

The time required to complete the Accounting Protocol in these cases may be so great as to negate the benefits of the results.

The last step on Schedule 8 for the completion of this Accounting Protocol will be for the consultant to ask the company to assess the relevance of the calculated incremental cost impact to its operations.

This assessment process will enable the company to indicate that the significance of the regulatory activities may be greater than the actual dollars measured. Reference could be to the time used that resulted in a loss of productive talent and capital or foregone business opportunities.

The Working Papers provided here for recording the three types of costs are recommended methods only. Alternative approaches should be used by the consultant as necessary in a particular company circumstance.

Use of the Accounting Protocol may not be appropriate for all business structures and alternative approaches should be discussed.

The completed set of Schedules and Working Papers are to be returned to the government. Other back-up data, calculations or confidential information should be retained by the consultant.

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

Objectives of the Accounting Protocol

To estimate or determine the Cost of Compliance based on the identification of incremental costs incurred under the categories of Personnel, Capital and Other Costs during the period under consideration that are of a recurring nature

and

To determine those Capital and Other incremental Costs that may have been incurred in current, prior or subsequent periods that represent unusual one-time expenditures directly related to compliance activities in the current period.

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

DEFINITIONS

Entity Compliance Model (ECM)

A description of the current processes that the organizational entity or business unit uses to comply with a regulation.

This includes the administrative systems and procedures, identification of the functions involved, as well as the assets used, including computer hardware and software.

Incremental Compliance Costs

Those incremental costs which are caused by regulation and which would not exist in the absence of regulation.

It is intended to include funds deployed or redeployed, the value of services rendered or a liability incurred for the purpose of complying with a regulation.

Incremental Personnel Costs

The principal means to determine the incremental cost of compliance should be based on a functional approach, where a compliance function or activity results in increased incremental costs to the corporation.

Cost reductions due to lowered personnel involvement should be shown separately from cost increases.

That portion of the number of people wholly or in-part involved in compliance is to be multiplied by an estimate of the annual incremental cost per person, including overhead. Fractional people are to be included, subject to materiality.

Incremental Capital Costs

Incremental capital costs due to regulation are to consist of expenditures on tangible and intangible assets that were required to bring the company into compliance with a regulation. Incremental capital cost reductions should be calculated separately from incremental cost increases.

Other Incremental Costs

Those incremental costs that are not due to either personnel or capital changes and will consist of transition costs, consulting fees, unusual or one-time operating costs and measurable

opportunity costs.

Incremental Internal Costs

The on-going expenses borne by companies in complying with the directives and requirements of the various regulations.

These incremental costs may include expenses related to personnel costs of assembling and reporting the data, dealing with subsequent audits and redress situations. In addition, there may be expenses due to monitoring of regulatory affairs, reporting systems, audit fees, legal fees and the costs of public disclosure.

Incremental Internal costs do not include the amount of direct payments to regulatory agencies (e.g. taxes, fees, etc.).

Incremental Transition Costs

The one-time expenses of establishing mechanisms to comply with new regulations or of modifying current systems to meet changes in existing regulations.

Incremental Costs may also be incurred during the de-commission of a compliance system following the termination or relaxation of a regulation.

Incremental Opportunity Costs

The incremental cost of regulation may include losses in productivity of labour or equipment, delays in construction and lost revenue opportunities.

Government Grants and Loans

Grants and loans that have the same characteristics as private sector loans are to be excluded.

Only grants/loans that cause corporate behaviour that would not otherwise have occurred are to be included for cost calculation purposes.

The types of loans that may be excluded could be from the following:

- . Small Business Development Corporation;
- . Federal Business Development Bank;
- . Export Development Corporation;
- . Farm Credit Corporation.

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

COST PRINCIPLES

1. Incremental Costs are to be identified and collected for the current period under review within the following classifications:
 - a) Personnel Costs
 - b) Capital Costs
 - c) Other Costs

2. Incremental Costs incurred, or expected to be incurred, outside of the current period are to be accumulated for the following classifications:
 - a) Capital Costs
 - b) Other Costs

These other period incremental costs should be identified only if they are unusual compared to the current period due to larger dollar values or less frequent expenditure patterns.

3. The incremental costs to be measured are the costs of those actions taken to comply with a regulation that would not have been incurred in the absence of that regulation.

The compliance actions are the deployment of resources to ensure compliance, as well as the redeployment of resources from other activities.

4. Incremental Costs of compliance are to exclude those costs that would have been incurred even in the absence of regulation.
5. Incremental Cost reductions are to be deducted from the compliance cost of regulation. Reductions do not include benefits obtained from improved trade barriers or income tax benefits.
6. Recognition of incremental costs is to follow an accrual basis of accounting approach.
7. The incremental cost data can be determined by informed judgment and, where appropriate, supported by the accounting and financial records.
8. Incremental Costs are to be measured starting at the point in time where compliance

with a regulation is required.

9. Incremental Compliance costs are to include the following:

- a) Internal Costs: the on-going expenses of compliance
- b) Transition Costs: one-time expenses to establish the mechanisms to comply
- c) Opportunity Costs: if measurable, obvious and not ambiguous

10. Where practical, incremental compliance costs are to be identified with a specific regulation or group of regulations.

11. Four types of costs are to be excluded from the calculation of incremental costs:

- a) costs not directly attributable to compliance actions;
- b) payments to the various governments for income, capital and excise taxes, foreign trade tariffs and import duties;
- c) opportunity costs that have not had a measurable impact on the company or are not capable of quantification;
- d) costs of over-compliance where a company decided to meet a more stringent criterion than that actually required by regulation.

12. Immaterial compliance costs do not need to be collected.

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

DATA COLLECTION METHODOLOGY

1. Government and the industry sector jointly determine:
 - . which period(s) to review;
 - . the list of regulations that have the greatest relevance;
 - . companies to be involved.
2. Government meets with the potential companies to solicit their voluntary participation in the study.
3. One company executive should be designated as the contact person for the consultant to identify the correct individuals for the interviews and act as a coordinator with the consultant.
4. Company personnel involved in the interviews should be chosen for their knowledge of the company's operating and reporting structures as well as for their professional training and ability to make informed judgments that would be in accord with the objectives and methodology of the review.
5. A government consultant should perform the following:
 - . explaining the methodology to the participants in advance of the interviews;
 - . making field visits to each company, for on-site interviews and data gathering;
 - . completing the cost calculations subsequent to the interviews.
6. Each participating company should be responsible for the following:
 - . assigning and instructing its personnel for the interview;
 - . assessing what data may be necessary during the interview based on the consultants description, taking into account the company's structure, location of accounting records and other factors;
 - . attending the interview and describing the impacts.

7. The collection of incremental cost data by the consultant at each company will require three steps:
 - . Identifying those activities that have been affected by regulatory compliance;
 - . Identifying the extent to which the compliance actions would have been performed in the absence of regulations;
 - . Determining the incremental cost of each compliance action identified and categorized as Personnel Costs, Capital Costs or Other Costs.

8. The consultant should retain the Schedules and Working Papers and other confidential information and calculations.

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

THE REGULATORY REQUIREMENTS TO BE CONSIDERED

Examples of Areas of Regulatory Activities

1. Corporate Governance
 - . Corporation Legislation
 - . Competition Act
 - . Disclosure Requirements

2. Taxation
 - . Income Tax
 - . Real Estate Tax
 - . Customs Duties
 - . Excise Tax
 - . Business and Property Tax
 - . Goods and Services Tax
 - . Provincial Sales Tax
 - . Commodity Taxes

3. Environmental
 - . General Emission Requirements
 - . Handling and Disposal Requirements
 - . Environmental Assessments
 - . Government User Fees

4. Goods and Services
 - . Market Entry Controls
 - . Price Controls
 - . Product Controls
 - . Production Controls
 - . Information Disclosure

5. Human Resources and Labour Management
 - . Employee Health and Safety
 - . Labour Legislation
 - . Pensions
 - . Remuneration
 - . Entry Requirements
 - . Pay Equity

- . Payroll Deductions
- 6. Transportation
 - . Safety and Distribution Specifications
 - . Rates and Fees
 - . Interprovincial Movement
- 7. Communication Controls
 - . Advertising/Marketing
 - . Broadcasting
 - . Telecommunications
- 8. Consumer
 - . Protection Legislation
 - . Labelling Requirements
 - . Substance Restrictions
- 9. Financial Transactions
 - . Loans and Guarantees
 - . Monetary Regulation
 - . Currency Regulation
- 10. General Reporting
 - . Statistical Reports
- 11. Infrastructure
 - . Land Use and Zoning
 - . Government Supplied Services
- 12. Intellectual Property
 - . Patents and Copyrights
 - . Trademarks
 - . Licences
- 13. Government Programs in Support of Business
 - . Loans and Loan Guarantees
 - . Grants
- 14. Government Procurement Policies
 - . Price Stabilization Objectives
 - . Employment Equity Requirements
- 15. Transfer of Government Technology and Intellectual Property

Licences for Government Patents

**ACCOUNTING PROTOCOL
SCHEDULES AND WORKING PAPERS**

ANALYSIS OF COMPANY ACTIVITIES THAT HAVE BEEN AFFECTED

Schedule Three Completion Procedures

The business Activity Areas and Examples columns are illustrative only and are grouped as they are generally understood by government. Clear separation of these functions may not occur in a specific company.

Make any changes necessary to reflect the individual organization being studied.

For each regulation to be considered, develop an Entity Compliance Model of the systems and procedures currently in place. The Model should cover all aspects of compliance including monitoring of new developments, internal administration and accounting, periodic reports as well as audits and dispute resolution.

The Model should be documented and can be based upon discussions with appropriate company personnel.

Schedule Three questions seek to identify where compliance functions occur in the company that can be directly attributed to regulatory requirements and where the incremental costs of these functional activities appear in the categories of Personnel, Capital or Other Costs.

Against each overall Activity Area, the first question should be answered in either the negative (No) or in the positive (Yes or Not Known).

For each positive answer to the first question, try to add as much detail as possible under the second question using the list of regulations under Columns 1 & 2. The specific regulation is preferred.

For each positive answer to the first question, identify under the third question where the incremental cost impact will be recorded: Personnel, Capital or Other Costs.

For each Activity Area with a cost category identified in question 3, proceed to Schedule 4, 5 or 6 as appropriate.

Schedule 3

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

ANALYSIS OF COMPANY ACTIVITIES THAT HAVE BEEN AFFECTED

ACTIVITY AREAS	EXAMPLES	Have Your Activities in These Areas Been Affected By Compliance Requirements?	Where Possible Identify the Specific Regulation?	Where has the Incremental Effect Been: Personnel, Capital or Other Costs
1. General Administration	<ul style="list-style-type: none"> . Strategic Management\ Shareholder Relations . Information Systems . Regulatory\Legal Affairs . Contracting\Leasing 			
2. Budgeting/Control	<ul style="list-style-type: none"> . Accounting\Auditing . Payments . Cash Flow Management\ Budgeting . Inventory Management 			
3. Financing\Investment\ Taxation	<ul style="list-style-type: none"> . Banking\Financing . Investment . Acquisition\Divestment of Assets . Taxation 			
4. Human Resources Management	<ul style="list-style-type: none"> . Wages\Benefits\Pensions . Recruitment\Training and Skills Development . Personnel Management\ Labour Relations . Employment\Labour Conditions 			
5. Delivery\Distribution\Sales	<ul style="list-style-type: none"> . Product\Service Delivery . Product\Service Distribution . Sales . Pricing 			

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

ANALYSIS OF COMPANY ACTIVITIES THAT HAVE BEEN AFFECTED

ACTIVITY AREA	EXAMPLES	Have Your Activities in These Areas Been Affected By Compliance Requirements?	Where Possible Identify the specific Regulations?	Where Has the Incremental Effect Been: Personnel, Capital and Other Cost
6. Development of Products\Services	<ul style="list-style-type: none"> . Research\Design\Engineering . Produce\Process\Service Development . Acquisition of Intellectual Property . Development of Facilities 			
7. Supply Management	<ul style="list-style-type: none"> . Sourcing . Purchasing . Relations with Suppliers . Accessing Infrastructure 			
8. Marketing	<ul style="list-style-type: none"> . Market Research\Analysis . Marketing . Advertising . Other Promotional Activities 			
9. Production	<ul style="list-style-type: none"> . Production\Provision of Goods\Services . Quality Control . Packaging\Labelling . Health\Safety\Environmental Control 			
10. Customer\Client Services	<ul style="list-style-type: none"> . Customer\Client Relations . After-Sales Service . Customer\Client Support . Warranty\Guarantees 			

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

***INCREMENTAL PERSONNEL COSTS INCURRED FOR
THE PURPOSES OF COMPLYING WITH REGULATION***

Schedule Four Completion Procedures

For each Activity Area identified with Incremental Personnel Costs on Schedule 3, complete one Schedule for each government, legislation and regulation number that is involved.

Personnel with direct responsibility will be those who must comply with the regulation requirements on a recurring annual basis, including the filing of reports or information requests.

Indirect involvement should cover other personnel throughout the company who supply information or services to those that are directly responsible. These could be people involved in operations, information systems and other areas.

Individuals should be categorized within three levels: Management, Administration and Operations. Management would include the senior executives and strategic decision-makers. Administration would cover managers and staff that support the activities of Management and Operations. Development, production and sales staff would be included under Operations.

It is intended that activities affected by regulation be identified and a brief description entered under the first column.

The number of people is calculated as the sum of whole or part individuals, at each level, that are wholly or partially involved in compliance activities.

Compensation, in the case of company personnel, means average salary or wage plus related benefits on an annual basis for each level involved.

Overhead represents an estimate of the company's incremental cost to provide workplace facilities and services for the personnel levels affected by the compliance activities. The amount should be expressed on an annual basis as an increment to the compensation values. Factors to be considered would include equipment costs, computer systems and rent, determined on a reasonable basis such as square footage.

The total annual incremental costs multiplied by the number of people, by level, should be entered in the last column for the section on company personnel.

Total amounts should be transferred to Schedule 7 for summary under the appropriate Activity Area and the Area of Regulation.

It is important to gather data for the functions affected on a time basis as well as dollars. This will provide a first assessment on Schedule 8 as to the significance of the compliance impact.

Eg. Compliance time as a percentage of the total time available

Incremental Compliance cost as a percentage of total compensation

Incremental Costs for external personnel means the annual fees paid to outside professionals for services related to regulatory compliance, including disbursements.

The number of people and annual costs for external personnel are not required.

Enter the incremental compliance portion of external personnel costs in the last column.

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

WORKING PAPER FOR INCREMENTAL PERSONNEL COSTS INCURRED FOR THE PURPOSES OF COMPLYING WITH REGULATION

Activity Area: _____

Area of Regulation: _____

Level of Government: _____

Legislation: _____

Regulation Number: _____

	Activity Description	Number of People	Annual	Incremental	Costs	Total Incurred In the Current Period
			Compensation	Overhead	Total	
1. Company Personnel						
	Direct Responsibility: Management Administration Operations					
	Total Direct Incremental Costs				\$	\$
	Indirect Involvement: Management Administration Operations					
	Total Indirect Incremental Costs				\$	\$
	Total Company Costs				\$	\$
2. External Personnel						
	Contract Services Consultants					
	Total External Incremental Costs					\$
	Total Incremental Impact on Personnel					\$

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

***INCREMENTAL CAPITAL COSTS INCURRED FOR
THE PURPOSE OF COMPLYING WITH REGULATION***

Schedule Five Completion Procedures

- . For each Activity Area identified with incremental Capital Costs on Schedule 3, complete one schedule for each government, legislation and regulation number involved.
- . The examples are illustrative only and more company specific descriptions can be substituted.
- . Incremental Costs in the two columns are to be those expenditures, or portions thereof, that were incurred to ensure the company was in compliance with a regulation, or area of regulations.
- . Incremental Costs can include intangible assets as well as leases capitalized in accordance with generally accepted accounting principles.
- . Applicable planning and incremental design costs, special tooling and other incremental equipment costs that are normally not capitalized for financial statements purposes are to be included.
- . Depreciation is not to be included.
- . The "Other Periods" column is for those expenditures that are outside of the current period but that are directly related to regulatory compliance. They should be unusual compared to the current period due to larger dollar values or less frequent expenditure patterns.
- . Other incremental Period costs could include start-up or decommission costs as well as recurring but non-annual regulatory modification costs.
- . The prior or future period should be noted on the Schedule and the costs should be expressed in dollar values of the affected period, not in current period dollars.
- . Totals from both Other Periods and Current Periods should be transferred to Schedule 7 for Activity Area and Area of Regulation.

Schedule 5

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

WORKING PAPER FOR INCREMENTAL CAPITAL COSTS INCURRED FOR THE PURPOSE OF COMPLYING WITH REGULATION

Activity Area: _____
Area of Regulation: _____
Level of Government: _____
Legislation: _____
Regulation Number: _____

Examples

	Incurred in Other Periods		Incurred In the Current Period
	Period	Total	Total
1. Incremental costs of Acquisition or modifications to buildings, plants and/or equipment			
2. Capitalized value of assets under financial lease arrangements			
3. Incremental costs related to start-up or decommission of facilities			
4. Computer software acquired or developed for compliance use			
Total Incremental Impact on Capital Costs		\$	\$

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

***OTHER INCREMENTAL COSTS INCURRED
FOR THE PURPOSE OF COMPLYING WITH REGULATION***

Schedule Six Completion Procedures

For each Activity Area identified with Other Incremental Costs on Schedule 3, complete one Schedule for each government, legislation and regulation involved.

The examples are illustrative only and more company specific descriptions can be substituted.

The "Other Periods" column should be used for those Incremental costs that occurred in periods other than the current one and were directly related to compliance activities. In addition, these incremental costs should be unusual compared to the current period due to their large dollar amounts or their timing.

The prior or future period should be noted on the Schedule and the costs should be expressed in dollar values of the affected period, not in current period dollars.

Totals from both columns should be transferred to Schedule 7 for each Activity Area and Area of Regulation.

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

WORKING PAPER FOR OTHER INCREMENTAL COSTS INCURRED FOR THE PURPOSE OF COMPLYING WITH REGULATION

Activity Area: _____
 Area of Regulation: _____
 Level of Government: _____
 Legislation: _____
 Regulation Number: _____

Examples	Incurred In Other Periods		Incurred In The Current Period
	Period	Total	Total
1. Operating Incremental Costs			
Marketing and Market Research		\$	\$
Research and Development of New or Modified Products			
Computer communication and transmission of compliance compliance information			
Total		\$	\$
2. Extraordinary Incremental Costs			
	Period	Total	Total
Employee training courses		\$	\$
Environmental protection or clean-up costs			
Pension, health or other liabilities incurred			
Other measurable incremental opportunity costs			
Total		\$	\$
Total Incremental Impact on Capital Costs		\$	\$

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

SUMMARY OF THE INCREMENTAL IMPACT BY GOVERNMENT

Schedule 7 Completion Procedures

- . There should be one schedule for each Activity Area with a positive response on Schedule 3.
- . Incremental Costs, preferably by level of government and specific regulation, should be transferred from the respective Schedules 4, 5 and 6 for each Area of Regulation.
- . Where Other Incremental Period Costs are brought forward, the affected periods should be added to Schedule 7 by footnote or in parenthesis.
- . The amounts in the total columns should be transferred to Schedule 8.

Schedule 7

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

SUMMARY OF THE INCREMENTAL IMPACT BY GOVERNMENT

ACTIVITY AREA: _____

AREA OF REGULATION: _____

Level of Government and Regulation Number(s)	Incurred in Other Periods*			Incurred in the Current Period				
	Incremental Capital Costs	Other Incremental Costs	Total	Incremental Personnel Cost	Incremental Capital Costs	Other Incremental Costs	Total	Other and Current Period Totals
Federal								
Total Federal								
Provincial								
Total Provincial								
Municipal								
Total Municipal								
Total Incremental Impact on Compliance Costs								

* Please Note the affected Periods

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

SUMMARY OF THE INCREMENTAL IMPACT BY COMPANY ACTIVITY

Schedule 8 Completion Procedures

- . There should only be one completed schedule per regulation.
- . Cost amounts will be available from a related Schedule 7 for each Activity Area that had a positive response on Schedule 3.
- . Where Other Period Costs are listed, the affected periods should be added to the Schedule by footnote or in parenthesis.
- . The columns "Is The Impact Significant..." can only be completed with the company as their qualitative comments on the relevance of the Entity Compliance Model to the organization.
- . The objective is to record whether the perceived impact is greater than the annual incremental dollar amounts calculated. This should consider at least the following:
 - the incremental Personnel compliance cost (per Schedule 4) expressed as a percentage, based on either time available or compensation
 - a loss of productive talent or capital
 - the postponing or losing of business opportunities
- . Answers to the Dollar Value column should be Yes or No, strictly on the basis of the calculated annual incremental cost impact to the company.
- . Answers in the last column should indicate the percentage impact and an assessment as to why the impact is, or is not, important. These answers can be the opposite of the Dollar Value column. Eg. a high percentage of a single persons' time may be required by compliance activities.

Schedule 8

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE
SUMMARY OF THE INCREMENTAL IMPACT BY COMPANY ACTIVITY

ACTIVITY AREA	TOTAL INCREMENTAL COST IMPACT			IS THE COMPLIANCE IMPACT SIGNIFICANT DUE TO:	
	Other* Periods	Current Period	Total	Dollar Value?	Changes in Productive Talent, Capital or Opportunities?
1. General Administration					
2. Budgeting\Control					
3. Financing\Investment\Taxation					
4. Human Resources Management					
5. Delivery\Distribution\Sales					
6. Development of Products\Services					
7. Supply Management					
8. Marketing					
9. Production					
10. Customer\Client Services					
Total Incremental Impact on Costs			\$		

*Please Note the Affected Period

TAB B

**ACCOUNTING PROTOCOL
FOR USE TO DETERMINE
THE INCREMENTAL COSTS OF COMPLIANCE
RESULTING FROM CHANGES IN REGULATORY REQUIREMENTS**

**ACCOUNTING PROTOCOL
FOR USE TO DETERMINE
THE INCREMENTAL IMPACT ON COSTS OF COMPLIANCE
RESULTING FROM CHANGES IN REGULATORY REQUIREMENTS**

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THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

Introduction and Criteria For Use

This Accounting Protocol has been designed to be used by an independent consultant to determine the incremental impact on current costs that will result from either proposed **new** regulations or proposed changes to **existing** regulations. Any qualified consultant whether independent or not could equally use the Protocol, albeit there are advantages to the use of an independent consultant. Please refer to section "Role of Consultant" for more details.

It can be used for one regulation or a group of regulations and it can cover one or more levels of government.

A large or complex organization will require the consultant to evaluate the company structure before the Accounting Protocol can be applied. The purpose of an evaluation will be to determine the level at which compliance activities presently occur and the appropriate application of the Protocol to measure the incremental cost impact of the proposed changes.

Such an evaluation should consider at least the following general aspects of organizational structures:

- I: Corporate level - what are the Policies for complying with regulations
- II: Divisional level - what are the Practises to comply with regulations
- III: Operational level - what are the Applications to comply with regulations

In less complex organizations, these levels of responsibility may be found in one location and possibly in one individual.

The methodology of this Accounting Protocol, including the instructions and working papers that follow, is written on the presumption that these evaluations have occurred and that the organizational entity or business unit affected by the proposed changes has been identified for purposes of measuring the impact on costs.

The results from the Accounting Protocol can be used by government or business to assist in evaluating and analysing the future impact of government intervention in the economy.

The concepts and methodologies that support the Accounting Protocol and the various schedules in this package are neutral enough that they could be equally applied to any type of organization: business, labour or non-profit.

Companies and industry sectors are to be approached by government at a senior executive

level to determine whether the companies will participate in this incremental cost impact study on a voluntary basis.

For each intended use of this Accounting Protocol, all parameters will be jointly developed in advance by government and industry and there will be mutual agreement of all aspects and requirements of the study before its commencement.

These parameters will at least include the period to be studied, the proposed regulatory changes, the industry sector and the participating companies and the role of the consultant engaged by the government.

The proposed regulatory changes will be prepared by the government in consultation with business to be of maximum relevance to the industry sector that will be under study. A description of the regulation changes will be included under *Schedule 3, Section 2* of the Accounting Protocol.

For purposes of determining the incremental impact on the costs of compliance, proposed changes in regulatory requirements ("Regulations") will mean new regulations or changes to all types of statutory directives with which businesses currently comply, including acts, legislation, regulations, orders, by-laws, proclamations and warrants.

The incremental impact is to be determined as cost reductions and/or cost increases.

Incremental cost reductions are those savings in the current costs of compliance that are expected to be realized from the proposed regulation changes due to fewer actions being necessary to maintain compliance.

Incremental cost increases are those new costs that are expected to be incurred by an action taken to comply with the proposed regulation changes and which would not exist in the absence of those changes.

Incremental Cost impacts are to be categorized as follows:

- 1) changes in incremental personnel costs to be measured using a functional approach;
- 2) changes in incremental capital costs, and
- 3) changes in other incremental costs, neither personnel-based nor capital in nature.

The methodology is not accounts-based and will rely on the consultant to solicit informed business judgment to identify activity changes or estimate the incremental impacts that are expected to be wholly or partially the result of new compliance requirements.

A preliminary step to completing the Accounting Protocol will be for the consultant to

develop an understanding of the systems and procedures that the entity currently uses to comply with existing regulations; ie. an "Entity Compliance Model" (ECM).

An Entity Compliance Model (ECM) should document where compliance activities are currently performed, how the activities are performed and why they are performed.

The model will be important to the evaluation of the incremental impact that the regulation changes are expected to have on the entity's compliance activities and its costs. This model building will be covered as part of the Activity Analysis on Schedule 3.

It is also a prerequisite for the consultant to determine with the company whether it is practical to use the Accounting Protocol in its particular circumstances. The impact of the regulation changes may not be measurable if:

- . the company cannot identify where the impact may occur
- . the costs cannot be quantified

The time required to complete the Accounting Protocol in these cases may be so great as to negate the benefits of the results.

The last step on Schedule 8 for the completion of this Accounting Protocol will be for the consultant to ask the company to assess the relevance of the calculated incremental cost impact to its operations.

This assessment will enable the company to indicate whether the significance of the regulation changes on its activities could be greater than the estimated dollars. Reference could be to the additional time requirement that may result in a loss of productive talent, a use of capital or foregone business opportunities.

The Working Papers provided here for recording the three types of cost changes are recommended methods only. Alternative approaches should be used by the consultant as necessary in a particular company circumstance.

Use of the Accounting Protocol may not be appropriate for all business structures and alternative approaches should be discussed.

The completed set of Schedules and Working Papers are to be returned to the government. Other back-up data, calculations or confidential information should be retained by the consultant.

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

Objectives of the Accounting Protocol

To estimate or determine the Incremental Impact on the Costs of Compliance based on the identification of cost savings expected to be realized or new costs expected to be incurred under the categories of Personnel, Capital and Other during the period under consideration that are of a recurring nature

and

To determine the incremental impact on Capital and Other costs that may result in subsequent periods that represent unusual one-time savings or expenditures directly related to the regulatory changes in the current period.

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

DEFINITIONS

Entity Compliance Model (ECM)

A description of the current processes that the organizational entity or business unit uses to comply with existing regulation.

This includes the administrative systems and procedures, identification of the functions involved, as well as the assets used, including computer hardware and software.

Incremental Impact On Compliance Costs

Those incremental cost savings or cost increases expected to result from changes taken to comply with new regulations or changes to existing regulations and which would not have resulted in the absence of those new requirements.

It is intended to include the impact on funds deployed or redeployed, the value of services rendered or liabilities incurred for the purpose of complying with the regulation changes.

Incremental Personnel Costs

The principal means to determine the incremental impact on costs should be based on a functional approach, where a change in a compliance function or activity is expected to result in reduced or increased costs to the corporation.

Cost reductions due to lowered personnel involvement should be shown separately from cost increases.

That portion of the number of people wholly or in-part involved in compliance is to be multiplied by an estimate of the annual incremental cost per person, including overhead. Fractional people are to be included, subject to materiality.

Incremental Capital Costs

The incremental impact on capital costs due to regulation changes is to consist of expenditure increases or decreases on tangible or intangible assets that will be necessary to keep the company in compliance with the new regulation.

Incremental Capital cost reductions should be calculated separately from incremental cost increases.

Other Incremental Costs

Those cost impacts that are not clearly attributable to either personnel or capital changes and will consist of changes in transition costs, consulting fees, unusual or one-time operating costs and measurable opportunity costs.

Incremental Internal Costs

The on-going expenses borne by companies in complying with the directives and requirements of the various regulations.

These incremental costs may include expenses related to personnel costs of assembling and reporting the data, dealing with subsequent audits and redress situations. In addition, there may be expenses due to monitoring of regulatory affairs, reporting systems, audit fees, legal fees and the costs of public disclosure.

Incremental Internal costs do not include the amount of direct payments to regulatory agencies (e.g. taxes, fees, etc.).

Incremental Transition Costs

The one-time expenses of establishing mechanisms to comply with new regulations or of modifying current systems to meet changes in existing regulations.

Incremental Costs may also be incurred during the de-commission of a compliance system following the termination or relaxation of a regulation.

Incremental Opportunity Costs

The Incremental cost of regulation may include losses in productivity of labour or equipment, delays in construction and lost revenue opportunities.

Government Grants and Loans

Grants and loans that have the same characteristics as private sector loans are to be excluded.

Only grants/loans that cause corporate behaviour that would not otherwise have occurred are to be included for cost calculation purposes.

The types of loans that may be excluded could be from the following:

- . Small Business Development Corporation;
- . Federal Business Development Bank;
- . Export Development Corporation;
- . Farm Credit Corporation.

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

COST PRINCIPLES

1. Incremental Cost impacts are to be identified and collected for the current period under review within the following classifications:
 - a) Personnel Costs
 - b) Capital Costs
 - c) Other Costs

2. The incremental cost impacts expected to occur in a period subsequent to the current period are to be accumulated for the following classifications:
 - a) Capital Costs
 - b) Other Costs

These other period incremental cost impacts should be identified only if they are unusual compared to the current period due to larger dollar values or less frequent expenditure patterns.

3. The incremental cost impacts to be measured are the incremental savings or costs of those new actions that result to ensure compliance with a proposed new regulation or a proposed change in an existing regulation and that would not have resulted in the absence of the new requirements.

This can include the initial deployment of resources as well as the redeployment of resources from other activities.

4. Incremental Costs of compliance are to exclude those costs that would have been incurred even in the absence of the proposed changes.

5. Incremental Cost reductions are to be shown separately from incremental cost increases. Reductions do not include benefits obtained from improved trade barriers or income tax benefits.

6. Recognition of incremental costs is to follow an accrual basis of accounting approach.

7. The incremental cost data can be determined by informed judgment and, where appropriate, supported by the accounting and financial records.

8. Incremental cost changes are to be measured starting at the point in time where compliance with the new regulation or the regulation changes is required.
9. The incremental impact on compliance costs is to include changes in the following:
 - a) Internal Costs: the decrease or increase in on-going expenses of compliance
 - b) Transition Costs: one-time savings or expenses in the mechanisms to comply
 - c) Opportunity Costs: if measurable, obvious and not ambiguous
10. Where practical, incremental compliance cost changes are to be identified with a specific regulation or group of regulations.
11. Four types of costs are to be excluded from the calculation of incremental cost changes:
 - a) costs not directly attributable to compliance actions;
 - b) payments to the various governments for income, capital and excise taxes, foreign trade tariffs and import duties;
 - c) opportunity costs that have not had a measurable impact on the company or are not capable of quantification;
 - d) costs of over-compliance where a company decided to meet a more stringent criterion than that actually required by regulation.
12. Immaterial changes in compliance costs do not need to be collected.

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

DATA COLLECTION METHODOLOGY

1. Government and the industry sector jointly determine:
 - . which period(s) to review;
 - . the list of proposed regulation changes that have the greatest relevance;
 - . companies to be involved.
2. Government meets with the potential companies to solicit their voluntary participation in the study.
3. One company executive should be designated as the contact person for the consultant to identify the correct individuals for the interviews and act as a coordinator with the consultant.
4. Company personnel involved in the interviews should be chosen for their knowledge of the company's operating and reporting structures as well as for their professional training and ability to make informed judgments that would be in accord with the objectives and methodology of the review.
5. A government consultant should perform the following:
 - . explain the methodology to the participants in advance of the interviews;
 - . make field visits to each company, for on-site interviews and data gathering;
 - . complete cost calculations subsequent to the interviews.
6. Each participating company should be responsible for the following:
 - . assigning and instructing its personnel for the interviews;
 - . assessing what data may be necessary during the interview based on the consultants description, taking into account the company's structure, location of accounting records and other factors; and
 - . attending the interview and describing the impacts.

7. The collection of incremental cost data by the consultant at each company will require three steps:
 - . identifying those activities that may be affected by the proposed regulatory change;
 - . identifying the extent to which the compliance actions would have been performed in the absence of the new regulations;
 - . determining the incremental cost impact of each new compliance action identified and categorized as Personnel Costs, Capital Costs or Other Costs.

8. The consultant should retain the Schedules and Working Papers and other confidential information and calculations.

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

THE REGULATORY REQUIREMENTS TO BE CONSIDERED

Examples of Areas of Regulatory Activities

1. Corporate Governance
 - . Corporation Legislation
 - . Competition Act
 - . Disclosure Requirements

2. Taxation
 - . Income Tax
 - . Real Estate Tax
 - . Customs Duties
 - . Excise Tax
 - . Business and Property Tax
 - . Goods and Services Tax
 - . Provincial Sales Tax
 - . Commodity Taxes

3. Environmental
 - . General Emission Requirements
 - . Handling and Disposal Requirements
 - . Environmental Assessments
 - . Government User Fees

4. Goods and Services
 - . Market Entry Controls
 - . Price Controls
 - . Product Controls
 - . Production Controls
 - . Information Disclosure

5. Human Resources and Labour Management
 - . Employee Health and Safety
 - . Labour Legislation
 - . Pensions
 - . Remuneration
 - . Entry Requirements
 - . Pay Equity

- . Payroll Deductions
- 6. Transportation
 - . Safety and Distribution Specifications
 - . Rates and Fees
 - . Interprovincial Movement
- 7. Communication Controls
 - . Advertising/Marketing
 - . Broadcasting
 - . Telecommunications
- 8. Consumer
 - . Protection Legislation
 - . Labelling Requirements
 - . Substance Restrictions
- 9. Financial Transactions
 - . Loans and Guarantees
 - . Monetary Regulation
 - . Currency Regulation
- 10. General Reporting
 - . Statistical Reports
- 11. Infrastructure
 - . Land Use and Zoning
 - . Government Supplied Services
- 12. Intellectual Property
 - . Patents and Copyrights
 - . Trademarks
 - . Licences
- 13. Government Programs in Support of Business
 - . Loans and Loan Guarantees
 - . Grants
- 14. Government Procurement Policies
 - . Price Stabilization Objectives
 - . Employment Equity Requirements
- 15. Transfer of Government Technology and Intellectual Property
 - . Licences for Government Patents

**ACCOUNTING PROTOCOL
SCHEDULES AND WORKING PAPERS**

ANALYSIS OF COMPANY ACTIVITIES THAT MAY BE AFFECTED

Schedule Three Completion Procedures

The business Activity Areas and Examples columns are illustrative only and are grouped as they are generally understood by government. Clear separation of these functions may not occur in a specific company.

Make any changes necessary to reflect the individual organization being studied.

For each new regulation or change to an existing regulation, develop an Entity Compliance Model of the systems and procedures currently in place. The Model should cover all aspects of compliance including monitoring of new developments, internal administration and accounting, periodic reports as well as audits and dispute resolution.

The Model should be documented and can be based upon discussions with appropriate company personnel.

Schedule Three questions seek to identify where new compliance activities may occur in the company that can be directly attributed to the proposed regulatory changes.

Against each overall Activity Area, the first question should be answered in either the negative (No) or in the positive (Yes or Not Known).

The second question should be completed where a positive answer has been given to the first question. Refer to the regulatory changes under Columns 1&2.

Where an Activity Area received a positive answer to the first question, categorize where the expected new incremental cost impact will be recognized under the third question as Personnel, Capital or Other costs.

For each Activity Area given a positive answer, proceed to Schedule 4, 5 or 6 as appropriate.

Schedule 3

THE COST OF REGULATORY COMPLIANCE
ANALYSIS OF COMPANY ACTIVITIES THAT HAVE BEEN AFFECTED

ACTIVITY AREAS	EXAMPLES	Will Your Activities in These Areas Be Affected By The Regulatory Changes?	Where Possible Identify the Specific Regulations?	Where Might the Incremental Effect Occur: Personnel, Capital or Other Costs
1. General Administration	<ul style="list-style-type: none"> . Strategic Management\ Shareholder Relations . Information Systems . Regulatory\Legal Affairs . Contracting\Leasing 			
2. Budgeting/Control	<ul style="list-style-type: none"> . Accounting\Auditing . Payments . Cash Flow Management\ Budgeting . Inventory Management 			
3. Financing\Investment\ Taxation	<ul style="list-style-type: none"> . Banking\Financing . Investment . Acquisition\Divestment of Assets . Taxation 			
4. Human Resources Management	<ul style="list-style-type: none"> . Wages\Benefits\Pensions . Recruitment\Training and Skills Development . Personnel Management\ Labour Relations . Employment\Labour Conditions 			
5. Delivery\Distribution\Sales	<ul style="list-style-type: none"> . Product\Service Delivery . Product\Service Distribution . Sales . Pricing 			

Schedule 3

THE COST OF REGULATORY COMPLIANCE
ANALYSIS OF COMPANY ACTIVITIES THAT HAVE BEEN AFFECTED

ACTIVITY AREA	EXAMPLES	Will Your Activities in These Areas Be Affected By the Regulatory Changes?	Where Possible Identify the Specific Regulations	Where Might the Incremental Effect Occur: Personnel, Capital or Other Costs
6. Development of Products\Services	<ul style="list-style-type: none"> . Research\Design\Engineering . Produce\Process\Service Development . Acquisition of Intellectual Property . Development of Facilities 			
7. Supply Management	<ul style="list-style-type: none"> . Sourcing . Purchasing . Relations with Suppliers . Accessing Infrastructure 			
8. Marketing	<ul style="list-style-type: none"> . Market Research\Analysis . Marketing . Advertising . Other Promotional Activities 			
9. Production	<ul style="list-style-type: none"> . Production\Provision of Goods\Services . Quality Control . Packaging\Labelling . Health\Safety\Environmental Control 			
10. Customer\Client Services	<ul style="list-style-type: none"> . Customer\Client Relations . After-Sales Service . Customer\Client Support . Warrantee\Guarantees 			

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

INCREMENTAL IMPACT ON PERSONNEL COSTS

Schedule Four Completion Procedures

- . For each Activity Area identified with an incremental Personnel Cost impact on Schedule 3, complete one schedule for each government, legislation and regulation number that is involved.
- . Personnel with direct responsibility will be those who are expected to comply with the regulation requirements on a recurring annual basis, including the filing of reports or information requests.
- . Indirect involvement should cover other personnel throughout the company who will supply information or services to those that will be directly responsible. These could be people involved in operations, information systems and other areas.
- . Individuals should be categorized within three levels: Management, Administration and Operations. Management would include the senior executives and strategic decision-makers. Administration would cover managers and staff that support the activities of Management and Operations. Development, production and sales staff would be included under Operations.
- . It is intended that activities affected by the proposed changes be identified and a brief description entered under the first column.
- . The number of people is calculated as the sum of whole or part individuals, at each level, that may be wholly or partially affected by compliance activities.
- . Compensation, in the case of company personnel, means average salary or wage plus related benefits on an annual basis for each level involved.
- . Overhead represents an estimate of the company's incremental cost to provide workplace facilities and services for the personnel levels affected by the new compliance activities. The amount should be expressed on an annual basis as an increment to the compensation values. Factors to be considered would include equipment costs, computer systems and rent, determined on a reasonable basis such as square footage.
- . The total annual incremental costs multiplied by the number of people, by level, should be entered in the last column for the section on company personnel.
- . Total amounts should be transferred to Schedule 7 for summary under the appropriate Activity Area and the Area of Regulation.
- . It is important to gather data for the functions affected on a time basis as well as dollars. This

will provide a first assessment on Schedule 8 as the significance of the impact on compliance costs.

Eg. The impact on compliance time as a percentage of the total time available

The impact on incremental compliance cost as a percentage of total compensation

Costs for external personnel means the incremental annual fees expected to be paid to outside professionals for services related to the new regulatory compliance, including disbursements.

The number of people and annual costs for external personnel are not required.

Enter the incremental compliance portion of external personnel costs in the last column.

Schedule 4

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

WORKING PAPER FOR THE INCREMENTAL IMPACT ON PERSONNEL COSTS

Activity Area: _____

Area of Regulation: _____

Level of Government: _____

Legislation: _____

Regulation Number: _____

Activity Description	Number of People	Annual Incremental Costs			Total Incurred In the Current Period
		Compensation	Overhead	Total	
1. Company Personnel					
Direct Responsibility: Management Administration Operations					
Total Direct Incremental Costs				\$	\$
Indirect Involvement: Management Administration Operations					
Total Indirect Incremental Costs				\$	\$
Total Company Costs				\$	\$
2. External Personnel					
Contract Services Consultants					
Total External Incremental Costs				\$	\$
Total Incremental Impact on Personnel				\$	\$

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

INCREMENTAL IMPACT ON CAPITAL COSTS

Schedule Five Completion Procedures

- . For each Activity Area identified with an incremental Capital Cost impact on Schedule 3, complete one schedule for each government, legislation and proposed regulation change.
- . The examples are illustrative only and more company specific descriptions can be substituted.
- . Incremental savings or costs in the two columns are to be those changes that are expected to result while ensuring that the company will be in compliance with the proposed regulation changes.
- . Incremental cost impacts can include intangible assets as well as leases capitalized in accordance with generally accepted accounting principles.
- . Applicable planning and incremental design costs, special tooling and other equipment costs that are normally not capitalized for financial statements purposes are to be included.
- . Depreciation is not to be included.
- . The "Other Periods" column is for those changes that are subsequent to the current period but that may be directly related to the regulatory changes. They should be unusual compared to the current period due to larger dollar values or less frequent expenditure patterns.
- . Other incremental Period impacts could include changes in estimated start-up or decommission costs as well as recurring but non-annual regulatory modification costs.
- . The subsequent period should be noted on the Schedule and the amounts should be expressed in dollar values of that period, not in current period dollars.
- . Totals from both Other Periods and Current Periods should be transferred to Schedule 7 for Activity Area and Area of Regulation.

Schedule 5

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

WORKING PAPER FOR THE INCREMENTAL IMPACT ON CAPITAL COSTS

Activity Area: _____
 Area of Regulation: _____
 Level of Government: _____
 Legislation: _____
 Regulation Number: _____

Examples

	Incurred in Other Periods		Incurred In the Current Period
	Period	Total	Total
1. Incremental costs of Acquisition or modifications to buildings, plants and/or equipment			
2. Capitalized value of assets under financial lease arrangements			
3. Incremental costs related to start-up or decommission of facilities			
4. Computer software acquired or developed for compliance use			
Total Incremental Impact on Capital Costs		\$	\$

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

INCREMENTAL IMPACT ON OTHER COSTS

Schedule Six Completion Procedures

For each Activity Area identified with an Other Cost impact on Schedule 3, complete one Schedule for each government, legislation and proposed regulation change.

The examples are illustrative only and more company specific descriptions can be substituted.

The "Other Periods" column should be used for those incremental changes that are expected to occur in periods subsequent to the current one and will be directly related to new compliance requirements. In addition, these incremental impacts should be unusual compared to the current period due to their large dollar amounts or their timing.

The subsequent period should be noted on the Schedule and the amounts should be expressed in dollar values of that period, not in current period dollars.

Totals from both columns should be transferred to Schedule 7 for each Activity Area and Area of Regulation.

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

WORKING PAPER FOR THE INCREMENTAL IMPACT ON OTHER COSTS

Activity Area: _____
 Area of Regulation: _____
 Level of Government: _____
 Legislation: _____
 Regulation Number: _____

Examples	Incurred In Other Periods		Incurred In The Current Period
	Period	Total	Total
1. Operating Incremental Costs			
Marketing and Market Research		\$	\$
Research and Development of New or Modified Products			
Computer communication and transmission of compliance compliance information			
Total		\$	\$
2. Extraordinary Incremental Costs			
Employee training courses		\$	\$
Environmental protection or clean-up costs			
Pension, health or other liabilities incurred			
Other measurable incremental opportunity costs			
Total		\$	\$
Total Incremental Impact on Capital Costs		\$	\$

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

SUMMARY OF THE INCREMENTAL IMPACT BY GOVERNMENT

Schedule Seven Completion Procedures

- . There should be one Schedule for each Activity Area with a positive response on Schedule 3.
- . Incremental savings or costs, preferably by government and the proposed new regulation or changed regulation, should be transferred from the respective Schedules 4, 5 and 6 for each Area of Regulation.
- . Where Other incremental Period amounts are brought forward, the subsequent periods should be added to Schedule 7 by footnote or in parenthesis.
- . The amounts in the Total columns should be transferred to Schedule 8.

Schedule 7

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

SUMMARY OF THE INCREMENTAL IMPACT BY GOVERNMENT

ACTIVITY AREA: _____

AREA OF REGULATION: _____

Level of Government and Regulation Number(s)	Incurred in Other Periods*			Incurred in the Current Period				Other and Current Period Totals
	Incremental Capital Costs	Other Incremental Costs	Total	Incremental Personnel Cost	Incremental Capital Costs	Other Incremental Costs	Total	
Federal								
Total Federal								
Provincial								
Total Provincial								
Municipal								
Total Municipal								
Total Incremental Impact on Compliance Costs								

* Please Note the affected Periods

**THE INCREMENTAL IMPACT ON
THE COSTS OF COMPLIANCE**

SUMMARY OF THE INCREMENTAL IMPACT BY COMPANY ACTIVITY

Schedule Eight Completion Procedures

There should only be one completed Schedule per regulation.

Savings or costs will be available from a related Schedule 7 for each Activity Area that had a positive response on Schedule 3.

Where Other Period amounts are brought forward, the subsequent periods should be added to the Schedule by footnote or in parenthesis.

The columns "Is The Impact Significant..." can only be completed with the company as their qualitative comments on the relevance of the impact of the changes on their Entity Compliance Model of the organization.

The objective is to record whether the expected impact might be greater than the estimated dollar amounts calculated. This should consider at least the following:

- the incremental impact on Personnel compliance costs (per Schedule 4) expressed as a percentage, based on annual totals of either time available or compensation
- a loss of productive talent or capital
- the postponing or losing of business opportunities

Answers to the Dollar Value column should be Yes or No, strictly on the basis of the calculated incremental cost impact to the company.

Answers in the last column should indicate the percentage impact and an assessment as to why impact is, or is not, important. These answers can be the opposite of the Dollar Value column. Eg. a higher percentage of a persons' time may have to be devoted to compliance activities.

Schedule 8

THE INCREMENTAL IMPACT ON THE COSTS OF COMPLIANCE

SUMMARY OF THE INCREMENTAL IMPACT BY COMPANY ACTIVITY

ACTIVITY AREA	TOTAL INCREMENTAL COST IMPACT			IS THE COMPLIANCE IMPACT SIGNIFICANT DUE TO:	
	Other* Periods	Current Period	Total	Dollar Value?	Changes in Productive Talent, Capital or Opportunities?
1. General Administration					
2. Budgeting\Control					
3. Financing\Investment\Taxation					
4. Human Resources Management					
5. Delivery\Distribution\Sales					
6. Development of Products\Services					
7. Supply Management					
8. Marketing					
9. Production					
10. Customer\Client Services					
Total Incremental Impact on Costs			\$		

*Please Note the Affected Period

TAB C

ENTITY COMPLIANCE MODEL (ECM) FOR THE MANAGEMENT OF WHMIS

Corporate Hygienist Staff Activities

1. Approve all products for use in the plant before any purchase can be made.
 - use a standardized form to request information from suppliers
 - suppliers must provide complete details on product composition and proof of compliance with WHMIS regulations
 - suppliers must provide their own MSDS form and labels for approval
 - hygienists enter the data to the company's centralized computer which can be accessed by each plant to produce an internal MSDS form and labels
2. Maintain the central computer data base by performing a three year review and update of all supplier product information.
3. Perform internal audits or reviews of the various plants to ensure that the correct documentation is being retained to confirm that appropriate training is being given to the workers.
4. Prepare and plan the training programs to be given to new employees and the annual refresher courses for overall content that can be tailored to each plant's unique requirements.

Plant Hazardous Materials Staff Activities

1. Manger has sole responsibility to order all hazardous materials for the plant.
 - confirm in advance that the specific product has been approved for use in the plant by the corporate hygienist by accessing the central database
2. Ensure the correct handling procedures are in place and followed for each product, including management of the inventory and storage facilities.
 - prepare the onsite MSDS forms and labels to have ready when the products arrive
 - receive, label and move the products to their correct locations

Plant Safety Staff Activities

1. Manager has sole responsibility to decide when the products can actually be used in the plant
 - confirms that the correct MSDS forms and labels are onsite
 - verifies that training has been given to the employees and that the training

2. Prepares the content for the training sessions for new employees and the annual refresher courses for all employees.

TAB D

CASE STUDY

**INFORMATION TECHNOLOGY FIRMS:
THE BUSINESS IMPACT TEST AND
CUSTOMS AND EXCISE REGULATIONS**

Report of Industry Canada's BIT consultations
with IT Sector Firms

BACKGROUND

In 1994, as part of the federal government's effort to improve the effectiveness and efficiency of Canada's regulatory framework, 14 Information Technology (IT) sector firms participated in a pilot Business Impact Test (BIT) and BICAP Case Study. The 14 IT firms, concentrated in the Toronto and Ottawa regions, were selected in consultation with the "Strategic Microelectronics Consortium" and CATA. Eleven of the firms were small businesses, while three were large. Overall, the 14 participants reflect a diversity of companies in the IT sector.

METHODOLOGY

In order to test and refine the BIT and BICAP Processes, Industry Canada initiated a pilot project with firms from the Information Technology (IT) sector. The studies concentrated, mainly, on two geographical areas in order to limit cost. Ottawa and Toronto were selected as the two primary regions for the IT study because they possessed a representative range of firms in the industry that could be fully studied, compared, and analysed.

Through consultations with members representing large and small IT sector firms, nineteen firms were invited to participate in the pilot BIT project. Sixteen firms volunteered to undertake the challenge, with fourteen firms finishing the process. Senior Officials within these IT firms were responsible for the BIT Process. The participating firms reflect the diversity of interests that exist within the IT sector:

- (1) Firms were involved in both the manufacturing of software and hardware.
- (2) Out of the 14 firms, eleven of these firms were small businesses, while three were large businesses.
- (3) Except for one participant from Montreal, the companies were from Ottawa and Toronto.
- (4) Firms differed in their levels of export and import activities.

The first step in the consultations was for senior officials in the firms to identify the most burdensome regulatory areas. To facilitate this process, participants were provided with a detailed list of regulations and their sub-sections grouped into 15 major areas (See Tab D, Appendix 2). The participants then filled out a "Pre-BIT" questionnaire to determine which of the 15 regulatory areas caused problems for their firms and which ones they would like to examine through the BIT software (See Tab D, Appendix 3). Up to five specific "fixable" areas were to be chosen that they believed could be refined in a way to be significantly beneficial to their firm. The objective of this consultation was not to identify regulations to be eliminated, but

to determine, in systematic fashion, the possibilities for improvement.³

The BIT software was then used to determine causes of the problems, and to outline preliminary solutions; "fixes". Once the nature of the problem was determined through the BIT software, estimates of the scope and extent of savings that could be achieved with the "fixes" were determined through interviewers using the BICAP as a framework. Officials of 8 of the smaller 14 firms were interviewed with the BICAP framework for "Existing Regulations".⁴ (*See Tab A - "Guide and Manual for Determining the Impacts....." BICAP framework for Existing Regulations*).

The BICAP results help reveal the importance of the compliance costs that firms face when dealing with current Customs and Excise regulations. It therefore provides a perspective for suggestions of fixes based on potential areas for savings. In this work, the eight firms were asked to examine potential savings due to a specific set of fixes for improving Customs and Excise regulations; Specifically, it was assumed that:

- Current tariff rates and structure remains in place; but that
- Regulations for tariffs and clearance are changed to a self-assessment approach similar to income or sales tax, and that associated audits be conducted as part of normal federal tax audits; that
- Brokers are no longer necessary to clear and move products across the border; and that
- Consultants are no longer necessary to complete application for tariff rebates.

³It should be noted that due to the success of this pilot project in the IT Sector, the BIT and BICAP processes for analysing regulatory impacts are now being utilized in the automotive and forestry sectors.

⁴It should be noted that the eight firms who applied the BICAP are not the same "eight who ranked Customs and Excise in the Bit process as a major problem.

OBSERVATIONS ON THE SOURCE OF REGULATORY BURDENS IN THE IT SECTOR

Nine regulatory areas were identified as having the most burden on operations. The overall ranking of potential cost reductions and of regulatory burdens are:

- | | |
|---|----------------------------|
| 1. Taxation | 5. Transportation |
| 2. Environmental and Health | 6. Communications Controls |
| 3. Goods and Services | 7. Consumer |
| 4. Human Resources
and Labour Management | 8. Financial Transactions |
| | 9. Reporting |

The remaining areas included: Infrastructure, Intellectual Property, Corporate Governance, Government Programs in Support of Business, Government Procurement Policies, Transfer of Government Technology.

The problems with "Taxation" has two distinct components; those related to commodity taxes, specifically GST/PST, and those related to the Customs and Excise system. Out of the 14 firms who participated, eight had major concerns with the impediments associated with Customs and Excise taxes and virtually all small firms felt that Customs and Excise regulations were a major burden to their business. Only one out of the three large IT firms expressed major concerns over Customs and Excise regulations

*Note: A 15th firm completed the Pre-Bit Survey, but was unable to return the BIT software survey because of technical problems.

OBSERVATIONS ON THE IMPACTS OF CUSTOMS & EXCISE REGULATIONS

In general, IT firms had difficulties with both the regulatory framework and the administrative procedures. The individual responses detail relatively unique sets of problems with Customs and Excise Regulation which relate to each firm's practices. However, there were some common areas. Specifically, the firms often identified three major sources of regulatory burden. The most often reported problems were:

1) PROBLEMS ARISING IN THE SHIPMENT OF GOODS THAT ARE TO BE RETURNED

Core Concern - There are a number of goods that are exported and then re-imported (or vice-versa) in fairly quick succession. Specifically, these are goods neither exported for sale nor subsequently "imported" in the traditional sense of buying components. Consequently no money is exchanged based upon the value of the goods involved, yet the full customs treatment (eg. paperwork) is reportedly applied at the border, creating what appear to be unnecessary costs and delays. This is particularly aggravating with products that a company feels free to import and export under NAFTA.

-The following examples highlight the difficulties faced by some small Canadian firms:

---- **Warranty** - A good made in Kanata, sold in the United States, is in need of repair. The firm only offers repair services in Ottawa, necessitating shipment across the border for warranty service. Consequently, the good has to be imported back into Canada, repaired, and then exported back to the customer. Participants in the survey feel that products being shipped back and forth receive harsher treatment and encounter longer delays than those encountered during their original shipment. The need for brokers to move warranty goods through the border is considered inappropriate and expensive when the intent of NAFTA is for North American computer products to move freely in the first place. Furthermore, potential customers are very sensitive about tying up some key products at the border that unexpectedly require repair.

----**Products Shipped Across the Border for Demonstration Purposes** - When an American company wants to test a Canadian product to see if they want to eventually buy it, no sale is associated with such shipments, yet it can be tied up at customs for long periods of time. Such hassles may encourage American firms to look elsewhere and it can affect a firm's ability to market the product, if it is the only demonstration model available. Sometimes small firms may even have to send their working prototype, and delays at the border can significantly slow their product's development.

----**Shipment to Foreign Trade Shows** - In order to send equipment to a trade show in the U.S., firms find it necessary to schedule shipping two to three weeks in advance just to clear customs. One of the many customs complications potentially faced at the border is the treatment of intellectual property provisions and the inherent delays in sorting out problems.

For some firms, they may be sending the only unit of a machine that they own and whose use is essential to production or R&D. Therefore, a firm ends up being deprived of a machine's productive use while it sits waiting to clear customs. It was suggested that a simple transit permit for demonstration goods (goods not to be sold) could facilitate quicker and more efficient turnaround times.

----**Shipments for Product Testing** - Products are sometimes sent to the United States because a U.S. company (or branch office) may be the only one capable of conducting a particular test. Any delays at the border can impact on R&D efforts of a business.

----**Overall Consequences** - There are a number of situations where goods require export and re-import in quick succession. The delays and tie ups at the border impose a variety of what are considered to be unnecessary burdens on the firms. Areas such as productive capacity, R&D, customer relations and market access are impacted in a negative fashion.

2) PROBLEMS IN EXPORTING PRODUCTS

Core Concerns - Major concerns reside in the affects of "timing" of movement of goods across the border. Firms are not arguing with paying customs fees. It is the problem encountered in moving exports in a timely predictable fashion that is costly to their businesses. Under NAFTA, there is suppose to be free movement of computers and software across the border. Uncertainty due to customs treatment at the border can in effect serve as a non-tariff barrier. Uncertainty about the interpretation of shipments and the timing of exports reportedly restrict the access of small IT firms to the U.S. market. They believe that Customs and Excise enforcement needs to be consistent with the spirit and intent of NAFTA.

It was also reported that brokers were, at times, ineffective in getting some shipments through due to complexities in customs regulations. They suggest that the regulatory framework should seek to reduce dependence on brokerage houses by the smaller firms of the IT sector. They also believe that shipment of their product should be unencumbered at the border due to NAFTA. They argue that the framework benefits brokerage firms and other outside consultants the most, at the expense of IT firms. Some companies report paying more money to brokerage firms than that paid in duties and tariffs to the government. They report finding that the overall Customs and Excise framework is so confusing that the expertise of brokerage firms and their prohibitive expenses are mandatory.

-The following examples highlight some of the difficulties faced by some firms in exporting their products to the U.S. market.:

----**Economics of Scale and Access to Markets** - It was reported by some firms that only volume contracts with U.S. firms can be considered since smaller shipments are often made uneconomical by customs cost. Specifically, pursuing small contracts can be economically unattractive; due to costs and delays related to customs, and the necessity to use brokers in moving goods across the border. This encourages some U.S. firms to use U.S. suppliers.

----**Country of Origin Provisions and NAFTA** - It is reported that the major source of costs and delay at the border is the paperwork associated with Country of Origin requirements. The use of Brokerage firms is considered essential for ensuring full and accurate compliance in the documentation of Country of Origin requirements. The impact on firms was felt two ways:

- (1) Exports to the United States - For small firms required to establish "Country of Origin" it is an administrative nightmare to track and monitor the required information, particularly if multiple country components are involved. Even if foreign components are not involved, it is reportedly still difficult to prove at the border, thereby causing delays.
- (2) Re-Exports from outside North America - Once a Canadian product is exported to a non North American country, it is reported to lose its exemption on export back to North America. The potential NAFTA paperwork burden for these transactions makes small Canadian firm products less competitive.

----**Overall Consequences** - Foreign distributors are often reportedly uneasy about dealing with small Canadian suppliers because of the insecurities generated over timeliness and dependability at the border. NAFTA and/or its application has not sufficiently eased these difficulties as originally envisioned. A few firms report considering opening up U.S. branch plants in order to avoid these hassles.

3) PROBLEMS ASSOCIATED WITH IMPORTING COMPONENTS

-The following examples highlight the difficulties of importing components etc. faced by small Canadian firms:

Core Concerns - There are many similarities to the difficulties experienced in exporting goods; Country of Origin, costs of brokers, discriminatory shipping rates, NAFTA, etc. Concerns arise due to the difficulties of "timing" imports for small IT firms. An excessive amount of time, personnel, and paperwork is required to facilitate the shipment of goods from foreign customers and suppliers. With small volume shipments, firms cannot afford delays and hassles involved with understanding, acquiring, and dealing with paperwork.

----**Country of Origin** - Components from foreign countries are subject to duties and tariffs. The availability of needed materials can be limited when secondary sources originate in non-North American countries. Costs are increased because of the delays in the availability of materials.

Many IT firms design and engineer products; specifications are then sent overseas for manufacturing; and finally the components or end product is imported back to Canada. Documenting the cost of foreign inputs in end product can be very difficult where the value of intellectual property is a consideration.

----**Duty Drawback Tax** - The Duty Drawback Tax is an irritant because the cost of retrieving previously paid import taxes can be substantial. Some firms do not even bother to claim back some of the duty paid out on components subsequently exported because of the hassle and costs associated with the required documentation. Of particular concern is the time lag involved in receiving money owed by Revenue Canada.

----**Technological Lags** - Policies on Customs duties are considered, at times, out of date, particularly as they apply to software and new software development that may be used as components. These so called "grey areas" in Customs and Excise legislation results in time consuming and inconsistent customs interpretation.

PROBLEMS WITH PROCEDURES, SPECIFIC REGULATORY PROBLEMS AND THEIR IMPACTS:

A major source of problems is associated with the processing of paperwork and brokerage fees. Although the Reporting and Monitoring requirements for Customs and Excise are being better understood, participants in this study find that the design of the forms and requirements are still complex, confusing and cumbersome. The main difficulty is in the cumulative impact of various requirements. There are a multitude of different customs import/export forms to be processed in all relevant areas. A significant amount of personnel and training requirements is mandatory. The following provides details of some specific problems highlighted by the participants

"Country of Origin" (Content Regulations) - Components from foreign countries (Outside of NAFTA originating countries) can be subject to duties and tariffs. NAFTA paperwork is therefore a problem for customers outside North America who want to re-export a Canadian IT firm's basic product, plus their own value added input, back to North America, because the exemption can be lost having left North America. This can create costly administrative difficulties, particularly for small firms, if inputs from foreign markets are utilized in end products. When a product is re-exported out of the country, tracking and monitoring all the components from different countries for duty and tariff purposes can create significant costs and delays. The effect of these complex provisions is that the sources of needed inputs is in effect

restricted when these sources are located outside North America.

The result is that some small IT firms are often unable to source the cheapest possible inputs. Some companies find that even if foreign components are not involved, it can still be difficult to prove that fact at the border, thereby causing delays. When products are returned from a U.S. purchaser for credit, the accounts must be balanced on an item by item basis.

"Software and Hardware Regulations" - Some firms are critical of the fact that duty applies to imported and exported software, but it does not apply to mass produced application software. They find that it is difficult to determine exempt software. Regulations are written for large hard goods, not software, thereby creating a large "grey zone" at the border for interpreting the treatment (duty and customs charges) vis a vis new software that has no definitions or tariff classifications. One IT firm argued that outdated duties are on the book, such as "duties shall be charged based on the number of inches of recording surface".

"Customs Officials and Enforcement Procedures" - Overall, there can be inconsistent application of Customs and Excise rules due to their complex nature. Uncertainty is created in cases where interpretation is required. Furthermore, small IT firms feel that they are often at the mercy of the mood of customs officials on a given shipment or their various levels of competence. Customs has affected the delivery of some software packages and components when Canadian customs representatives were not available. Similarly, availability of customs officials is all too often limited.

POTENTIAL SAVINGS WITH REFINED CUSTOMS AND EXCISE MEASURES

The savings that could be achieved with reforms to Customs and Excise regulations were examined in interviews with officers of eight of the small IT firms. The detailed results from these company profiles are summarized in Tab D, Appendix 1. To obtain this data, each of the officers examined how their activities would change and what would be saved if;

- Current tariff rates and structure remains in place; but that
- Regulations for tariffs and clearance are changed to a self-assessment approach similar to income or sales tax, and that associated audits be conducted as part of the normal federal tax audits; that
- Brokers are no longer necessary to clear and move products across the border; and that
- Consultants are no longer necessary to complete application for tariff rebates or credits.

In addition, two of the firms estimated the savings that could be achieved by simply taking on the activities of brokerage rather than out sourcing. A summary overview of the results are outlined

in Tab D, Appendix 4.

Potential savings were generally associated with what were considered "Delivery and Distribution" (inputs), "Supply" (outputs) and "Budgeting and Control" activities. The savings are associated with reduced paper work, need for tracking, follow-up, etc. Savings also included the release of resources of those responsible for these activities for more beneficial ends. In this respect, it is important to emphasize that much concern arises due to the hassles and delays outlined in the previous section, not just costs.

The total estimated savings that the firms believe they could achieve with the "fix" outlined above range from a low of \$5000 to \$115000. The results reflect the differences in the size of firms, markets and their import/export practices. To put these observations in perspective, savings in this range could be viewed as equivalent to:

- An increase in export sales revenue of, generally, 1% - 5% or more; or
- up to a reduction of 1% - 10% in the cost of labour; or
- at least a \$13 reduction in the cost incurred per customs transaction.

REDUCED COSTS OF LABOUR, CONSULTANTS, AND BROKERAGE FEES

Labour or Personnel costs generally constitute the bulk of the internal savings. Such savings constitute about 8% to 10% of the total potential savings. In various combinations, the firms use their accountants, auditors, shippers, traffic coordinators, administrators, export managers, and senior management to deal with these regulations. The small firms interviewed in this work, report that anywhere from one to five people, were involved for anywhere from 5 to 96 days per year in Customs and Excise related activities.

Who undertakes these customs functions and what they could be doing is just as important as how many are involved and the cost. Presidents, Vice-Presidents, and shippers all may be involved who have other key functions. Considerable disruption occurs when these individuals must spend time away from their normal responsibilities.

When the complexities and/or scope of export/import become too burdensome, most of the small firms interviewed, resort to brokers. The savings on brokerage fees often represent the bulk of the potential savings. Savings that could be obtained by eliminating their involvement constitutes about 15% to 100 % of the total potential savings identified in this work. If the system could be simplified sufficiently to permit the work of the brokers to be handled internally, two firms estimated that they would save 50% and 90% of their present brokerage costs, respectively.

Examples from various firms:

-In one firm, 59 out of 260 employees are presently involved in various aspects of preparing and expediting customs paperwork requiring an estimated 12 days per year at a cost of \$9100. This firm exports 55% of its products yet only requires the payment of \$2500 for external consultants fees.

In another firm, with only 26 employees who export 80% of their product, a full time traffic coordinator facilitates imports and exports at a cost of \$70000 including overhead, and external brokers are still required at a cost of \$42000 along with consultants at a cost of \$3000.

Processing brokerage bills, customs slips, and the traffic classifications of each import and export is estimated to take 96 days per year at another firm at a cost of \$14900. There are 140 employees in the firm. Brokerage fees on these transactions are estimated at \$50000. The company averages 4 imports and 15 exports per day (4940 transactions per year), leading to an estimated average potential savings of \$13 per customs transaction.

COMMENTS OF PARTICIPANTS

IMPROVED REGULATIONS AND PROCESSES:

- The firms interviewed in this work suggested that the requirements and paperwork be streamlined. It was suggested that the use of electronic rather than paper forms would be an important step forward. Furthermore, they would like one form instead of the multitude currently involved.
- They argue that reforms should reflect the vital importance of eliminating delays and uncertainties associated with imports and exports. Simplified and clearer regulations, definitions and processes would greatly assist these small firms. Duty Payment, clearance and duty/tariff remission processes based on self assessment models would assist these firms.
- A mechanism to quickly explain the treatment of emerging technologies which fall outside the scope of existing policy was identified as important in this sector to avoid uncertainty at the Border.

IMPROVEMENTS TO SPECIFIC PROVISIONS:

- Provide a simple Customs and Excise system systems for goods that require quick turnaround between initial export and import (eg. those used for trade shows or returned for repair or warranty). Exemptions were suggested for these goods.
- They argue that the treatment of goods and "Country of Origin" provisions should be consistent with the spirit of NAFTA, i.e there should be free unencumbered flow of Computer and software across the Canadian/U.S. border .
- They would like to see the duty draw-back system refined to avoid the delays in refunds and expenses now encountered in obtaining refunds.

AUTHOR'S OBSERVATIONS:

It is unclear exactly how much of the problem is related to Canadian customs activities and which issues need to be dealt within the context of trade issues. However, these firms are monitored by Revenue Canada at the border for compliance with Customs and Excise regulations and in-house for GST and income taxes. It would appear that an appropriately tailored in-house self assessment style of Customs and Excise rules could relieve many of the burdens currently faced by firms. Such flexibility is being provided to large exporters. Combined "real-time" audits of all three assessments should generally benefit these businesses. Such an initiative would seem important to avoid the *de facto* trade barriers created by an unnecessary complex Customs and Excise system.

Russ Roberts
Peter Sharp

SUMMARY REPORT - CUSTOMS AND EXCISE REGULATIONS / POTENTIAL SAVINGS CREATED BY IMPROVED CUSTOMS PROCESSES

COST CENTRES

COMPANY DESCRIPTION	POTENTIAL TOTAL SAVINGS - CUSTOMS & EXCISE	DELIVERY/ DISTRIBUTION SALES.	BUDGETING AND CONTROL	PRODUCTION	SUPPLY	COMMENTS AND EXPLANATIONS
<p>Integrated Circuit Consulting (Start-Up Stage of Growth)</p> <p>1996 - Annual Sales (\$2 - \$10 million) --- 0% exports ---100% imports (\$200000)</p> <p>1996 -President -7 full time employees -3 part-time</p> <p>1995 Employed 4 full-time ---two contract staff ---no administration. and accounting staff</p>	\$12000				<p>\$12000 (100% of Total Customs and Excise potential savings)</p> <p>-Operating (input) costs of purchasing</p> <p>-Excise Tax Act impacts on importing</p>	<p>-Total of Customs and Excise potential savings is \$12000 annually. The \$12000 in additional cost of purchases occurs due to the following: ----Delays at the border and the cost increases associated with such delays prevents the company from importing specific cheaper cost U.S. inputs. ----Cheaper U.S. supplier cannot be used at a potential saving of \$500 dollars per component on an annual order of 24, equalling the \$12000 total. Company forced to use more expensive Canadian supplier.</p> <p>-Opportunity Costs of border delay problems in general cannot be calculated. Due to the problems of Customs and Excise, there is a loss of opportunity to be the most efficient and effective with the company's overall purchases of supplies and its cost of inputs.</p>
<p>Communications - Voice and Telephone Processing Computers (Low Growth Stage)</p> <p>Annual Sales (\$2 - \$10 million) (\$4.2 million in 1993) ---Exports 20% and growing. ---Imports 5% of components - mainly uses Canadian distributors</p> <p>Employs 18 people ---The manager, finance and administration provides accounting and information services in support of fulfilling Customs and Excise requirements</p>	<p>\$5000</p> <p>(\$10000 See Comments Section)</p>		<p>\$5000 Personnel related costs (100% of total Customs and Excise potential savings. ----If changes in regulation were made, it would cost the company \$5000 dollars to set up an equivalent internal function to replace broker and their \$10000 price tag.</p>			<p>-Company averages 30 exports and 200 imports per year. ----Brokerage costs are significant ----Paperwork, personnel and Customs Act etc. sources of problems, with an emphasis on their impact on purchasing. ----standardization and simplification of import/export documentation desired, therefore non use of brokers could save as much as \$10000</p> <p>**Purchasing requirement to prepare paperwork internally, rather than have broker do it is: ----100hrs. X 50 (\$5000) would be the cost for the company to take over the functions of what the broker does (at a cost of \$10000), if regulatory changes enacted.</p>

COMPANY DESCRIPTION	POTENTIAL TOTAL SAVINGS - CUSTOMS & EXCISE	DELIVERY/ DISTRIBUTION SALES.	BUDGETING AND CONTROL	PRODUCTION	SUPPLY	COMMENTS AND EXPLANATIONS
<p>Communications - Computer and Communications Security Networks</p> <p>(Start-Up Stage of Growth)</p> <p>Annual sales of 4 million ---Exports 80% of all goods ---80% - 90% of annual sales will be export sales to the U.S. (\$2.6 - 2.9 million)</p> <p>---Imports 50% - 60% of components --- 80% of imported components comes from U.S.</p> <p>Employs 45 people (1996) ---26 employed (1995)</p>	\$115000	<p>\$77000 Personnel related costs (67% of total Customs and Excise potential savings)</p> <p>SUBTOTALS:</p> <p>-\$(\$21000) Internal Company Costs - 60% of one traffic coordinator on procurement coordination. (18% of total). -\$(\$21000) Internal Company Costs - overhead for one traffic coordinator. (18% of total). -\$(\$32000) External Costs - broker fees. (28% of total). -\$(\$3000) External Costs-training by outside consultants. (3% of total)</p>			<p>\$38000 Personnel related costs (33% of total Customs and Excise potential savings).</p> <p>SUBTOTALS:</p> <p>-\$(\$14000) Internal Company Costs - 40% of one traffic coordinator on purchasing. (12% of total). -\$(\$14000) Internal Company Costs, traffic coordinator overhead. (12% of total) -\$(\$10000) External Costs - brokers fees. (9% of total).</p>	<p>-Personnel and Broker's fees overall are main costs or areas consuming the time of the traffic coordinator. --Procurement (purchasing) needs requires 40% of traffic coordinator's time. --Personnel and brokerage fees - 60% of traffic coordinator's time.</p> <p>-With an expected 80% export rate savings in export processing costs would amount to savings of \$115000 - if import/export rules were simplified.</p>
<p>Manufacturer of Lamps, Lamp Sockets, Switches, Computer Aftermarket</p> <p>(Low Growth)</p> <p>Annual Sales (\$2 - \$10 million) ---25% - 50% export oriented</p> <p>Employs 51-100</p>	\$21000	<p>\$21000 Personnel related costs (100% of total Customs and Excise potential savings)</p> <p>SUBTOTALS:</p> <p>-\$(\$3000) Company costs. (1.5% of total) Shipping is still required but costs of doing forms are reduced by (100 hrs. X 3 labour) leading to the savings of \$3000. -\$(\$18000) - Broker Fees (86% of total) -Overall, the Customs Act is a major source of difficulty.</p>				<p>-Importing and Exporting broker fees can be saved with simplification of Customs and Excise rules</p> <p>-Personnel and Computer Services are the areas most impacted in terms of cost.</p> <p>-Broker fees could be reduced by the \$18000 figure noted in the Delivery/Distribution column if export/import forms were simplified.</p>

COMPANY DESCRIPTION	POTENTIAL TOTAL SAVINGS - CUSTOMS & EXCISE	DELIVERY/ DISTRIBUTION/ SALES.	BUDGETING AND CONTROL	PRODUCTION	SUPPLY	COMMENTS AND EXPLANATIONS
<p>LAN Equipment</p> <p>Employs 140</p>	\$64900		<p>\$6500 Personnel Related Costs (10% of total Customs and Excise potential savings)</p> <p>SUBTOTALS:</p> <p>-Processing Brokerage bills and custom slips (4 days per month) leads to this cost of \$6500</p>	<p>\$58400 personnel related costs-- Production - traffic area costs personnel related (90% total Customs and Excise potential savings)</p> <p>SUBTOTALS:</p> <p>-\$8400 (13% of total) Internal Company Costs - personnel -Traffic classifications processing each import and export (37.5 hrs/month) leads to this cost of \$8400</p> <p>-\$50000) Broker costs (77% of total) -----(\$34000 fees -----(\$21000) info. retrieval ...*** (- \$5000) savings - see comments section</p>		<p>-Company averages 4 imports and 15 exports per day. --Great savings if broker fees were less, largest portion of Customs and Excise regulatory costs and burdens. -Costs of personnel are the highest, focus of costs. --Save on paperwork and personnel costs (accounting and auditing) in processing brokerage bills</p> <p>-Outline of brokerage cost breakdown is \$34000 (fees) and \$21000 (information retrieval). --Company mentions that \$21000 of fees is passed onto purchasers. --***If company were to assume the work of brokerage house, they estimate that internal cost (mostly personnel) would be \$5000, hence the overall net cost savings if brokers gone is \$50000</p>
<p>Design and Manufacture Radio Communication and Central Systems</p> <p>(Mature Stage of Growth)</p> <p>Annual Sales (\$2.5 million) ---10% - 15% export based (\$250000 - \$375000)</p> <p>---Total cost of components \$1 million of which 10% - 15% are imported (\$100000 - \$150000)</p> <p>Employs 19</p>	\$8621	<p>\$8621 Personnel related costs (100% of Total Customs and Excise potential savings) --Personnel most required are shipping and export managers.</p> <p>SUBTOTALS:</p> <p>-\$1621 (19% of total) Internal Company Costs - paper preparation and broker communication ----5 people at 40 hrs or 5 days/yr. leads to this cost of \$1621</p> <p>-\$7000) Broker Fees (81% of total)</p>				<p>-Breakdown of \$7000 in brokers fees for 100 imports and 50 exports per year ----Import fees (\$50 each) to Broker ----Export Fees (\$40 each) to Broker --A simplified Customs and Excise system (export and import paperwork) would save time and reduce broker fees --no additional staff is required to administer and report.</p> <p>-Administrative Staff is the President and one staff accountant (administrator)</p>

COMPANY DESCRIPTION	POTENTIAL TOTAL SAVINGS - CUSTOMS & EXCISE	DELIVERY/ DISTRIBUTION SALES.	BUDGETING AND CONTROL	PRODUCTION	SUPPLY	COMMENTS AND EXPLANATIONS
<p>Manufacturer - Microchips (Start-Up Stage of Growth)</p> <p>Annual Sales (2\$ - \$10 million) ---Exports 95% - 100% of product. (90% of this total to the U.S.) ---Imports 100% of components</p> <p>Employs 40</p>	\$30000	<p>\$30000 Personnel related costs (100% of total Customs and Excise potential savings)</p> <p>SUBTOTALS:</p> <p>-(18000) Internal Company (60% of total) Costs - time spent preparing documents for broker (one person for 2 days/month), equals \$1500 per month = \$18000 annually</p> <p>-(12000) brokers (40% of total) -- Broker fees on transactions cost \$1000 per month = \$12000 annually.</p>				<p>-Concern about lost dollars, related to personnel costs and preparing export documents for the broker and payment of general broker fees.</p> <p>-Seeking simplification of export and import documents in order to reduce broker expenses</p> <p>-Concern about time lost by V.P. Distribution</p> <p>-Activity is related to paperwork preparation for border inspection</p>
<p>Manufacturer - Protection Relays (High Growth Stage)</p> <p>Annual Sales (\$10-\$100 million) ---55% of product exported and dropping. ---Negligible imports.</p> <p>Employs 133 (1996) Employed 260 (1995)</p>	\$16600	<p>\$13300 (80% of total Customs and Excise potential savings)</p> <p>SUBTOTALS:</p> <p>-(8300) Personnel related costs (50%) total Customs and Excise potential savings - 54 of the 260 employees, at a cost of \$8300, are required for documentation time for Int'l and U.S. exports. --Int'l exports (2 days/yr) -- U.S. exports (7 days/yr)</p> <p>-(5000) Capital (30% total) Customs and Excise potential savings. ---Acquisition of computer hardware for U.S. Traffic Manager (\$5000)</p>	<p>\$3300 Personnel related costs 20% of total Customs and Excise potential savings</p> <p>SUBTOTALS:</p> <p>-(800) (5% of total) Internal Company Costs -- 5 of the 260 employees are required for duty drawback claim, the accounting time for documenting re-imports and duty drawback (\$800) - total is estimated at 30 hrs./yr.</p> <p>-(2500) (15% of total) external consultants --fees paid to prepare drawback claims.</p>			<p>-Cost Accounting Protocol results are not incremental costs, but total cost savings possible if customs and excise reform occurs..</p> <p>-Compliance with Documentation requirements to export and import (personnel requirements are highest aspect of Customs and Excise regulation in finding and filling out paperwork. --Capital costs are second most burdensome. --Except for savings on brokers fees and other external consultants fees, benefits of other changes on personnel would be small.</p> <p>-In general, company made conscious decision to minimize exposure to high compliance areas; use of software or consultants instead of hiring staff and systems analyst approach to ensure compliance. -Clarification and simplification of export and import documentation for products would be key to reducing personnel costs</p> <p>-Specific regulation to reform are the Export Act and the International Sale of Goods Act.</p>

**COST OF REGULATORY COMPLIANCE PROJECT CLASSIFICATION
OF REGULATION**

- | | | |
|-----|--|---|
| (1) | CORPORATE GOVERNANCE | Corporation Legislation
Competition Act
Disclosure Requirements |
| (2) | TAXATION | Income Tax
Real Estate Tax
Customs Duties
Excise Tax
Business and Property Tax
Goods and Services Tax
Commodity Taxes |
| (3) | ENVIRONMENTAL | General Emission Requirements
Handling and Disposal Requirements
Environmental Assessment
Government User Fees |
| (4) | GOODS AND SERVICES | Market Entry controls
Price Controls
Production Controls
Information Disclosure |
| (5) | HUMAN RESOURCES AND LABOUR MANAGEMENT | Employee Health and Safety
Labour Legislation
Pensions
Remuneration
Entry Requirements
Pay Equity
Payroll Deductions |
| (6) | TRANSPORTATION | Safety and Distribution Specifications
Rates and Fees |
| (7) | COMMUNICATIONS CONTROLS | Advertising/Marketing
Broadcasting
Telecommunications |

PRE-BIT QUESTIONNAIRE

Appendix 3

1. Please indicate, Yes or No, which of the following activities of your firm are impacted by government imposed regulation. RANK them in descending order to indicate the most troublesome regulation to the least troublesome regulation. (ie. 1st, 2nd, 3rd, etc.)

ACTIVITY	ARE ACTIVITIES IMPAIRED?	EXAMPLES	RANK	SOURCE OF IMPACT
General Administration	Yes No	Strategic Management/Shareholders Relations Information Systems Regulatory and Legal Affairs Contracting/Leasing		Eg. WHIMS, Employment Equity, Customs, etc.
Budgeting/ Control	Yes No	Accounting/Auditing Payments Cash Flow Management/Budgeting Inventory Management		
Financing/ Investment/ Taxation	Yes No	Banking/Financing Investment Acquisition/Divestment of Assets Taxation		
Human Resources Management	Yes No	Wages/Benefits/Pensions Recruitment/Training and Skills Development Personnel Management/Labour Relations Employment/Labour Conditions		
Delivery/ Distribution/ Sales	Yes No	Product/Service Delivery Product/Service Distribution Sales Pricing		
Development of Products/ Services	Yes No	Research/Design/Engineering Product/Process/Service Development Acquisition of Intellectual Property Development of Facilities		
Supply Management	Yes No	Sourcing Purchasing Relations with Suppliers Accessing Infrastructure		
Marketing	Yes No	Market Research/Analysis Marketing Advertising Other Promotional Activities		
Production	Yes No	Production/Provision of Goods/Services Quality Control Packaging/Labelling Health/Safety/Environmental Control		
Customer/ Client Services	Yes No	Customer/Client Relations After-Sales Service Customer/Client Support Warranty/Guarantees		

2. Which five AREAS of regulation cause the greatest problems for your firm? Please rank them in descending order, i.e. 1st, 2nd, 3rd, etc., and identify the responsible legislation and jurisdiction.

RANKING	AREA OF REGULATION	RESPONSIBLE JURISDICTION	LEGISLATION
1st			
2nd			
3rd			
4th			
5th			

3. Please identify your firm and yourself:

Firm: _____
 Respondent: _____

4. Please describe the nature of the product and services you provide, e.g. accounting software, communications devices etc.

POTENTIAL CUSTOMS AND EXCISE SAVINGS ⁵

Total Potential Savings/ Total Sales Per Firm ^A	Potential Savings on Total Sales (%) ^B	Potential Savings on Export Sales (%) ^C	Potential Savings on Import Costs (%) ^D
\$12000 (\$5000000 - est.)	.24%	Not Applicable	6%
\$10000 (4200000)	.24%	1.2%	Not Available
\$115000 (\$4000000)	2.88%	3.59%	Not Available
\$21000 (\$5000000 - est.)	.42%	1.2%	Not Available
\$64900 \$69900	Not Available	Not Available	Not Available
\$8621 (\$2500000)	.34%	2.88%	6.8%
\$30000 (\$5000000 - est.)	.6%	.6% (Exports all products)	Not Available
\$16600 (\$50000000 - est.)	.03%	.07%	Not Available

A) Total Potential Savings and Sales - Total Potential Savings are estimated as determined from the BIT survey and BICAP results. Total Sales for each company are provided in brackets.

B) Potential Savings on Total Sales (Percentage) - Total Potential Savings are estimated as a percentage of Total Sales for each company.

C) Potential Savings on Export Sales (Percentage) - Total Potential Savings are estimated as a percentage of Export Sales for each company.

D) Potential Savings on Import Costs (Percentage) - Total Potential Savings are estimated as a percentage of the costs of imports for each company.

⁵ This chart provides an overview and possible interpretations of the BIT/BICAP based estimates provided by senior officials from the eight IT sector participants. These estimates were provided based upon potential savings if specific reforms to customs and excise regulations were to be enacted. To provide perspective on the data, this chart compares and analyzes potential savings as percentages of total sales, export sales and/or import costs respectively. All the data is derived from appendix 1. If estimates were required in the calculations, the mid-point(s) were chosen to provide consistency in the data. Firms should not generalize from these results any particular comparisons to their own particular situation.

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