
**Indigenous Expenditure Report
Project Update May 2010
'Cost differentials'**

Information Bulletin number 3 provided an overview of the method used to determine expenditure related to services related to Indigenous people. An important part of this method is to use 'measures of service use' as a basis for prorating expenditure between Indigenous and non-Indigenous people. This Bulletin provides an overview of the cost differential factor adjustment to the service use measure that is used to split expenditure on mainstream services between Indigenous and non-Indigenous Australians.

What is a 'cost differential'

An Indigenous cost differential factor is defined as 'a measure of the relative cost of providing mainstream services to an Indigenous person as compared to the cost of providing the same services to a non-Indigenous person'.

The provision of services to Indigenous people might be generally more costly if Indigenous people are disproportionately located in remote areas, or if Indigenous service users have additional service needs (such as language difficulties), regardless of their location.

For most mainstream services, it is currently very difficult to identify the magnitude of any differences in the cost of providing services to Indigenous and non-Indigenous people. One of the main issues is separating which service costs are specifically related to the Indigenous status of service users, and which costs are a result of other factors such as geographical location — and therefore not directly related to Indigenous status.

For example, the more remote an area is, the higher the cost of service delivery is likely to be, regardless of the Indigenous status of service users. However, as a larger proportion of Indigenous people than non-Indigenous people live in remote communities, the extent to which remoteness (or other generic high cost factors) should be considered in cost differentials will depend on the extent to which Indigenous people are represented in a population.

Cost differential sources and methods

Little research has been undertaken on the differences in cost of providing mainstream services to Indigenous and non-Indigenous people. The Steering Committee acknowledges that given the range of influences that could potentially affect cost differentials, targeted research projects may be required in specific service areas.

Detailed studies may take time and be costly, and may only be practical in areas of particular policy importance. Even in these areas, the information will take time to accumulate. As a consequence, the Steering Committee has agreed a range of methods that jurisdictions can use to identify cost differential data, including:

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- *administrative data that links costs to Indigenous/non-Indigenous users* — government administrative systems may record the amount of expenditure made for each recipient of a government service, by Indigenous status
- *government resourcing and/or policy settings* — government funding mechanisms may explicitly provide extra funding to government service providers, which provide services to Indigenous people (a ‘weighting’). For example, an aged care provider may receive 1.25 times the standard government subsidy for each Indigenous client
- *studies/analysis of service delivery cost drivers* — such analysis looks at the different cost drivers (such as location, time, level/type of service) and the Indigenous representation associated with each cost driver (for example, the number of Indigenous people receiving low cost services)
- *proxies using cost differential information from similar exercises* — prior Commonwealth Grants Commission research on cost ‘impediments’ can provide a starting point for IER calculations
- *proxies using cost differential information from similar services* — for example, the cost differential for providing primary school services *could* be used as a proxy for the cost differential for providing special education services
- *seeking out expert opinion* — reliability may be affected if the local experts have an incentive (or believe that there may be an incentive) to over or under estimate the true cost differential ratio — for example, to obtain a more favourable budget allocation in future years.

If you have any questions, would like to contribute views to the Indigenous Expenditure Report project, or want to receive Indigenous Expenditure Report updates, please contact the Secretariat (gsp.ier@pc.gov.au).

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