



AUSTRALIAN INDUSTRY
GROUP

The NSW 2007-08 Budget

**Establishing NSW as a Base for
Global Success**

**Australian Industry Group
June 2007**

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Establishing NSW as a Base for Global Success

The 2007-08 Budget presents a critical opportunity to build the economic prosperity of the State as it recovers from recent disappointing levels and reassert the role of NSW as a key driver in the national economy.

Across Australia, business and the economy is undergoing significant structural shifts in the face of emerging global challenges and opportunities.

The intensification of globalisation as China, India, Brazil, and Eastern Europe continue to emerge as competitive commercial centres presents new challenges to a wide cross-section of Australian industry. The associated boom in commodity prices, while a blessing in many respects, is simultaneously constraining the expansion of other industries through the shortages of skilled labour and the exposure to the higher value of the domestic currency.

These pressures are joined by the exposure to a long period of underinvestment in infrastructure and by a phase of readjustment in the housing sector.

The Main Priorities

Ai Group believes the way forward in the face of these challenges is clear. The Government should:

- Commit to reasserting the place of NSW as a genuinely competitive place to do business;
- Play a positive role in the renewal of the State's physical infrastructure;
- Partner with business in developing capabilities, innovativeness and the skills of its people; and
- Ensure that NSW takes a positive role in building sustained improvements in Australia's Intergovernmental relations.

To achieve these objectives, we urge the Government to commit to the following priorities:

- Maintain sound fiscal management;
- Reduce the complexity and costs of the State's Occupational Health and Safety arrangements;
- Elevate NSW to the position of national leader in reducing the regulatory burden on business;
- Make the NSW taxation system more competitive;

- Be active in attracting business to NSW and in improving opportunities for local businesses;
- Improve the planning and co-ordination of, and facilitate adequate levels of ongoing investment in, the State's infrastructure;
- Make NSW a leading innovator in building and upgrading the skills of the existing and emerging workforce;
- Facilitating the development of the business capabilities and innovativeness of the State's businesses; and
- Put NSW at the forefront of efforts to improve cooperation between the Federal, State and Local Governments.

Sound Fiscal Management

Maintaining a firm hand on the State's Budget must be a priority for the Government.

For most of the past decade NSW has demonstrated a strong record in managing the overall strength of the budget.

In more recent years however this strength was undermined. This was due to the adverse impacts on revenues of the slowdown in the State's economy generally, and the property market in particular, and on the acceleration of expenditures with strong public sector payroll growth without commensurate improvements in efficiency.

Improvements in efficiency must be pursued. This is particularly the case if sustainable improvements are to be made to the competitiveness of the State's tax system; the level of investment in the State's infrastructure, and the facilitation of the development of skills, capabilities and innovativeness.

Undue attention is often placed on the cash position of the Budget. As a business organisation we recognise the importance of cash flow management but we also know the importance of investing for the future. There is a case for Governments to borrow to invest in infrastructure that adds to the State's wealth and economic capacity. Such borrowing must be rigorously monitored, should not be deployed to fund recurrent expenditures and should generate returns in excess of the cost of capital.

To the extent to which there are opportunities for the Government to contribute to improved economic performance by divesting state-owned assets to the private sector, these strategies should be pursued. Funds realised through such sales should not be used to cover recurrent expenditure but should be used to strengthen the State's balance sheet through sound investments or debt retirement.

Occupational Health and Safety and Workers Compensation

The principal business regulation concern is the Occupational Health and Safety Act. It is a major constraint to the competitiveness of NSW and undermines business confidence.

The Government should support the passing of the Occupational Health and Safety Amendment Bill 2006, and conduct a review of OHS regulations.

The State's Workers Compensation scheme has achieved a dramatic improvement in its financial performance over the past four years. This has been delivered principally through reform of the dispute resolution process, making the scheme far less legalistic and reserving a greater proportion of scheme funds for injured workers rather than legal and other service providers.

The Government must continue to pass on cost savings in the form of premium reductions to further close the gap in average premiums between NSW and Victoria/Queensland. Above all, access to costly and poorly focused common law remedies should not be expanded.

Reducing the regulatory burden on business

NSW should strive to be the nation's leader in reducing unnecessary regulatory burdens on the business community.

Regulatory burdens need to be subject to better measurement and accountability, to enable continued identification of concrete improvements to regulation, particularly recognising the impact on small business.

New regulations must be subject to more rigorous, open and accountable regulatory impact assessment processes.

Make the NSW taxation system more competitive

The NSW taxation system is well short of best practice. Ai Group proposes that the Government commit to having a demonstrably more competitive tax system. Improvements should include a lower rate of payroll tax and fewer transaction taxes.

The abolition of the ill-conceived Vendor Duty and the phased program of removal of some of the States transaction taxes as agreed between the Commonwealth and the NSW Government are welcome developments. Nevertheless they leave considerable scope for further improvement if the State's taxation system is to first meet and then exceed the competitiveness of other States' tax systems.

Ai Group urges the Government to adopt a two-pronged approach to achieving this objective.

- The structure of taxes levied by the State Government should be reshaped so it is the best it can be, taking into account the need to raise revenue; the objective of minimising administrative and compliance costs and keeping the adverse impacts on the State's economic performance as low as possible.
- NSW should take a lead role in the national debate on overhauling Australia's pattern of intergovernmental financial relations. The debate should consider the continued need for cross-subsidies between the States; whether the current approach to managing intergovernmental financial relations inhibits the States from improving the pattern of their own tax systems; and the most effective way of addressing the current imbalances between the spending responsibilities of the States and their own-source revenues.

Both elements of this two-pronged approach should be pursued and even if progress on the second element is slow, NSW should pursue the overhaul of its own tax system. The benefits of improving the structure of taxation in NSW include:

- More competitive rates of payroll and land tax;
- Fewer and less distorting taxes on transactions including on property transfers and on payment of insurance premiums.

Attracting business to NSW and improving opportunities for local businesses

If NSW can lower the cost of regulation and improve its taxation arrangements it will have gone a long way in attracting investment.

There is also scope for the Government to be more proactive in “selling the message” and pursuing strategically important investments with targeted inducements that do not disadvantage existing businesses.

Extending the role of the Industry Capability Network will create opportunities for local businesses by opening opportunities for them to supply Government and other businesses in NSW and offshore.

Infrastructure

For the State’s transport, energy and water infrastructure, in particular, a greater commitment is required to set the foundations for sustained and sustainable growth. Business concerns over the adequacy of investment the longer-term security of energy and water supply are growing.

While recent increases in nominal expenditure on infrastructure and a longer-term planning framework are welcome developments, they need to be reinforced with the following measures:

- The Government should, as a matter of urgency, act to repair the damaging perception that government is an unreliable partner in infrastructure partnerships with the private sector;
- The Government should improve on the current approach to Public Private Partnerships and contracting in general by giving less weight to the removal of political and taxpayer risk and more weight to achieving the most efficient and effective outcome for the citizens and economy of NSW;
- The current patterns of ownership, management and regulation of the State’s energy and water infrastructure should be subject to a genuinely independent review to ensure that business and the broader community can be assured of appropriate levels of investment and ongoing security of supply of these vital services. In this context in particular Ai Group welcomes the Government’s recent announcement of the Owen Inquiry into Electricity Supply in NSW;
- The NSW Government should act in driving all levels of government to establish a coherent approach to national co-ordination and planning of infrastructure development;

- Ai Group does not oppose public sector borrowing for investment in public infrastructure. As a complement to private sector involvement, public sector borrowing to build wealth and income-enhancing assets is a sensible strategy as long as it is matched by rigorous selection of projects, clear accountabilities for the return on assets and a close eye on cash flow management.

A World Leader in Skills Development

Ai Group has advocated for the urgent need to re-orient both the training system and funding mechanisms to meet the needs of business and industry to up-skill and re-skill existing workers. There is an on-going imperative to significantly lift the skill and educational attainment levels of the Australian population. Indeed, OECD data suggests that for every one year increase in the average level of education, a nation's GDP will increase by between 3 and 6 per cent. Yet, Australia is ranked 18th out of thirty developed countries when comparing the proportion of GDP spent on education (5.8%). This is deterioration from a previous ranking of 8th.

A major challenge facing NSW is to increase, in tandem, employment participation and education attainment levels. A significant increase in both the national and state education and training effort will be required. Furthermore, this increased effort will need to become available to individuals throughout their working life.

Data to support the call for the need to increase expenditure in education and training includes:

- Access Economics projects that by 2025, the cost of the VET necessary to achieve the target scenario of no decline in overall employment participation will amount to \$9.8bn in today's prices. This amounts to an extra \$2.5bn over the projected cost of continuing past policies that can be expected to lead to a decline in employment participation;
- Access Economics projects that GDP in real terms would be 2% higher by 2010 and 12% higher by 2025, if employment and GDP rose as projected as a result of additional training. This in turn means that the overall cost of VET would then only rise slightly from 0.5% of GDP today to 0.6% of GDP in 2025;
- The Centre for the Economics of Education & Training (CEET), Monash University, has predicted a shortfall of 240,000 qualified people over the next decade if supply remains at its current level;
- CEET estimate that the resource base for VET will need to expand by 5 per cent per annum over the next decade to avoid the predicted shortfall in qualified people.

With these considerable challenges facing the economy it is imperative that the training system be strengthened. This will require an expansion of the resource base of the VET system in line with the estimates provided by CEET. Importantly, this resource expansion should simultaneously be used to increase the competitiveness of the training market using both private and public training providers.

The State Government should commit new resources over the next 5 years that will:

- Increase the revenue base in the VET sector to reach the estimates provided by CEET – 5% per annum;
- The recommended 5% increase per annum should be comprised of both State and Commonwealth contributions;
- The recommended increase must be coupled with initiatives to increase the competitiveness and flexibility of the training market.

Developing Business Capabilities

Following Ai Group's proposal for a national Business Capability Initiative, the Commonwealth Government has recently announced the creation of Productivity Centres. While the details of this program are currently under consideration, Ai Group proposes that NSW take an active stance in assessing and putting in place complementary measures that help small and medium-sized businesses build capabilities and expertise in:

- Identifying opportunities for growth;
- Exploiting relevant new technologies;
- Encouraging collaboration with potential supply chain partners; and
- Developing the appropriate business capabilities and strategic management skills.

NSW to take the Lead in Improving Cooperation between the Federal, State and Local Governments

Australia's federation is sagging. Across a wide cross-section of policy areas, there is confusion of responsibilities, overlapping bureaucracies and a clouding of responsibilities. Waste and perverse incentives abound.

The appearance of Australia's intergovernmental relations is not one of Governments working hand in hand; rather it is one of blame shifting.

Ai Group proposes that the NSW Government should take the lead in forging a reassessment and overhaul of Australia's intergovernmental relations.

An independent assessment should be made of the current allocation of responsibilities; current revenue raising capabilities; the forms of intergovernmental co-operation and the pattern of intergovernmental financial transactions. This should inform a dispassionate assessment of improvements that should and can be made and the establishment of a clear program of reforms.

A process modelled along the lines of the former National Competition Policy could see a progressive implementation of concrete and sustained improvements of the Australian federation.