

Ai GROUP

Submission to the Victorian Government on the

2022-23 Budget

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GROUP

About Australian Industry Group

The Australian Industry Group (Ai Group®) is a peak national employer organisation representing traditional, innovative and emerging industry sectors. We have been acting on behalf of businesses across Australia for nearly 150 years.

Together with partner organisations we represent the interests of more than 60,000 businesses employing more than 1 million staff. Our members are small and large businesses in sectors including manufacturing, construction, engineering, transport & logistics, labour hire, mining services, the defence industry, civil airlines and ICT.

Our vision is for *thriving industries and a prosperous community*. We offer our membership high quality services, strong advocacy and an effective voice at all levels of government underpinned by our respected position of policy leadership and political non-partisanship.

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Executive summary

The Victorian economy has begun to recover from the delta outbreak and associated restrictions. This is, however, only a beginning and the tasks of locking in the recovery of activity and employment and catching up on ground that has been lost over the past two years will still require considerable attention in the 2022-23 Budget. Alongside this priority, the Government should also take measures that will set the state up for advances in living standards over the medium to longer term.

A confident and engaged business sector is critical to meeting these challenges and Ai Group's proposals for the 2022-23 Budget are aimed at encouraging a rapid recovery of business investment and private sector employment both in support of recovery and repair and to secure the advances in productivity needed to underpin future improvements in living standards.

The most serious constraints on business in Victoria are in two areas that the Government can have significant impact: workers – both skilled and unskilled – and costs on business. The Government can pursue a vigorous policy to upskill, re-skill and attract skilled workers to the state together with those we need in the low skilled area such as hospitality and retail. Similarly the Government is encouraged to pursue a policy which does not impose new costs on businesses, especially with the significant concerns emanating from COVID 19.

The development of the skills of Victorians remains fundamental both to future improvements in productivity and real incomes and to the broader availability of opportunity across the community. With labour and skills shortages increasingly reported by employers, there is strong scope for government and employers to work to lift engagement of individuals in employment-based training to help address both the immediate labour shortages and future needs for a more highly skilled workforce.

Ai Group also sees strong potential for a greater focus by the State Government on assisting to lift the capabilities of Victorian businesses – particularly small and medium sized businesses. Our proposals for the 2022-23 Budget cover greater emphasis on assisting businesses to lift their use of digital technologies and digitally enhanced processes - including in relation to cyber security; assisting business efforts to deepen international engagement by providing connections, greater understanding of regulations in other countries and political risk insights, and by encouraging export success; and assisting in the development of more resilient and effective management of supply chains and supply chain risks.

One way that governments can seek to meet its industry, and other policy objectives is through its power as a purchaser of a range of goods and services. We put forward for consideration a set of principles that should inform the use of government procurement as a means of achieving such policy objectives.

Our submission includes specific suggestions in relation to achieving the Government's emission reduction targets. Our proposals relate to budgetary provisions for effective implementation of the Gas Substitution Roadmap; support for addressing transmission development challenges; and encouragement for broader decarbonisation initiatives - including by giving consideration to whether, and under what circumstances, government procurement is a cost-effective way of encouraging emissions reduction and

by exploring the scope for the use of industrial contracts for difference to encourage the development and adoption of innovative approaches to emissions reduction.

Our submission also includes several recommendations in relation to making progress towards the Government's objectives of reducing waste and promoting the circular economy and building the depth of business engagement in these agendas.

We believe the 2022-23 budget needs to be stimulatory and certainly should avoid a counter-productive increase in tax burdens while the economy is still recovering from the downturn in activity and employment and the damage to confidence that we have seen over the past two years.

There certainly should be no increase in taxes and charges in the 2022-23 Budget. Further, we urge the removal of the payroll tax surcharge introduced in last year's budget.

That said, we also recognise the significance of the large increase in public sector debt and the deterioration of budget positions across the federation. We also recognise the importance of reestablishing sustainable budgets and debt levels and rebuilding fiscal buffers so that future generations can have the capacity that Australia's governments had in 2020 and 2021 to deploy fiscal ammunition in supporting households and businesses during the COVID-19 crisis.

This will require an increase in scrutiny over the efficiency of existing and new areas of government spending and a serious rethink of our approach to taxation and intergovernmental financial relations.

In this context we urge the Victorian Government to use the Budget to adopt a leadership position about the importance of developing a national approach to improving Australia's taxation and intergovernmental finances.

1. Skills

Recommendations

- Support existing worker upskilling and reskilling and remove barriers to micro-credentials provision by education and training providers.
- Establish a statewide workforce plan for digital literacy, fluency and mastery.
- Fund pilots that develop higher level skills through an enhanced apprenticeship model.
- Explore legislative change which allows declaration of apprenticeships for higher level qualifications.
- Trial a wide range of work-based and work integrated learning models across post-secondary education that include incentives for employers to take on students.
- Introduce hubs that incentivise partnerships between industry and education and training providers.
- Support for employers to develop a multicultural workforce.

Policy approach

The skills urgency constraining Victoria's dynamic and digitally transforming economy demands action that alleviates skill pressures in the short term and addresses longer term structural change in the education and training system. Beyond immediate relief afforded by skilled migration, measures that assist employers to source, train and employ workers with the necessary skills, and to re-skill their existing employees must be coupled with the structural reforms already commenced by the Government.

Ai Group has welcomed the new Victorian Skills Authority which promises to match Victoria's employment demands with training and ensure Victorian employers and communities can find workers with the skills they need, when and where they need them. Also welcomed is the release of specific new grants and funding to support industry through education and training: they promise to address emerging needs through innovative thinking and approaches.

While these reforms and funding commitments provide a good focus on industry's skill pressures, Victorian employers need both continued and new skill-based initiatives and measures to improve outcomes for industry development and sustained economic growth.

In the short-term, training support for companies to transition existing workers into roles needed by employers being impacted by the need to adopt new technology and practices will also provide relief. The nature of work is increasingly changing from the performance of relatively routine tasks to more complex capabilities. In addition to specific technical skills, training needs to include digital skills at varying levels and human capabilities that allow workers to function effectively in changing work environments.

Companies need ready access to a broad range of micro-credentials that align with the increasingly regular re-skilling needs of industry. The Government should work to remove barriers to the provision of micro-credentials by providers to ensure that education and training offerings are nimble.

The current and future Victorian workforce must be better equipped for the digitally transforming economy. Improvement is needed at all levels - digital literacy, digital fluency and digital mastery- so that basic digital skill levels are assured, and numbers of digital professionals are sufficient. Current projections show large shortages of tech-based professionals.¹ A digital skills workforce plan for Victoria will allow mapping and alignment of education and training. Additional attention is required in relation to the skills to support the decarbonisation of industry.

Ai Group is encouraged by the creation of Apprenticeships Victoria as an initiative that will help increase the profile of the apprenticeship model with both employers and prospective apprentices and trainees. As digital transformation continues impacting every industry, it is vital that higher level skills programs are introduced across industry areas to meet the need for creeping skill levels. There is great opportunity to address these higher-level skill needs through an enhanced apprenticeship model that reaches into AQF levels beyond the usual Certificate III and IV programs. Pilots have commenced in some sectors, some assisted by the Victorian Government, but there is scope to explore more opportunities.

One systemic challenge that higher level apprenticeships raise is in recognising higher education qualifications as apprenticeships and traineeships. Currently in Victoria, only VET-level qualifications can be legally approved as an apprenticeship or traineeship. This formal recognition is important for both employers and apprentices. It provides the structure of training contracts and VRQA regulation that offers confidence in the legitimacy of employment and training arrangements to both parties. Legislative changes that allow the relevant Minister to 'declare' apprenticeships for higher level qualifications would be a simple matter that would have a significant impact on broadening the scope of apprenticeships.

Work-based and work-integrated learning models suit today's workplace, allowing students to be immersed in fast changing, digitalised work environments and develop work readiness. An Ai Group survey late in 2020 found 80 per cent of employers would take on either university or TAFE students². New pilots that trial more work-based learning opportunities at all qualification levels should include support for employers in recognition of the time commitment and resources devoted to student placements and projects. A successful example is the Victorian DMTC and Defence Science Institute Scholarships Program managed by Ai Group.

The decreasing shelf life of skills means new paradigms must be created for partnerships between industry and VET and higher education providers. It is of mutual benefit to collaborate on new models, learning content, delivery, placements, research and incubation and to co-locate. Collaborative metropolitan and regional hubs, learning from the Centres of Vocational Excellence model in Europe, would develop strategies to meet local skill needs and assist large and small companies to create innovative solutions to skill challenges. The hubs would develop tripartite industry-student-provider engagement models that foster and increase relationships, and result in industry-tuned workforce entrants.

¹ For example, Roadmap to Deliver One Million Tech Jobs, Technology Council of Australia, October 2021

² Skills Urgency: Transforming Australia's Workplaces, Ai Group, 2021

Victorian employers must embrace a multicultural workforce but their ability to do so is hampered by a misunderstanding as to what is required to embrace and attract young multicultural workers. The Government should consider how best to enable youth groups which engage with young people to better work with industry. There is currently a huge mis-match that needs to be dealt with that would benefit society generally and the economy specifically by having more young people being given employment opportunities.

2. Industry Policy

The last two years have been challenging for Victorian businesses, with COVID-19 disruptions, the complexity of dealing with changing restrictions on activity and supply chain and demand pressures affecting profitability and growth ambitions. Investments to support businesses' recovery and its ability to assist drive the next phase of Victoria's economic development should be given priority in the 2022-23 Budget.

Recommendations for Capacity Improvement Programs

- Companies should be supported to become more globally competitive by taking fuller advantage of Industry 4.0, digitalization, and the Clean Economy.
- Drive the general uplift of the cyber-security skills of businesses and their employees.
- Continue the support to companies which undertake international expansion, including advice on local regulations, introductions to local officials and political risk insights.
- Build the capabilities of Victorian businesses and exporters to adjust to post-pandemic exporting.
- Drive the adoption of end-to-end integrated supply chain management systems that provide industry-wide and business-level efficiencies.
- Provide certainty to Victorian companies regarding local procurement and recognize the supply chain benefits of local manufacture.
- The Government should continue to support the 'Cremorne Hub' to enable skill development and 'start up' activity in the Cremorne area. Its international recognition as an IT area of significance needs to be enhanced Government involvement especially in ensuring it attracts personnel to the area both locally and from overseas.

Policy approach

The Government has a long and successful history of capacity improvement programs for domestic and internationally focused businesses, often in partnership with Industry Associations. Ai Group proposals are to orientate attention to ensuring that Victorian businesses are equipped for a digitally connected world; to lift their participation in international business; and to ensure they are better equipped to manage changing, and increasingly challenging, supply chains and supply chain risks.

Global Victoria is a vital support for Victorian exporting businesses. The on site assistance provides easier access to markets and the expertise of the Victorian commissioners makes exporting far simpler than would otherwise be possible. The Government has continued to invest in exporting and we encourage you to maintain ha approach. We also recommend the digital focus that's been adopted by Global Victoria during the

pandemic. Its allowed increased exposure to potential export markets at much lower costs and enabling better utilisation of time.

The business approach to digitisation has become more focused over the past 21 months as businesses have been able to continue operating whilst in lockdown. Given the positive impact of technology and digitisation, now would be an excellent time to pursue a policy with smaller businesses to encourage digital appreciation and develop greater efficiencies. Victorian business and labour inefficiencies have been masked by the high net immigration rates of recent years. We now have little choice but to become more efficient, inventive and positive in the approach and encourage technical leaps in production processes.

Recommendations in relation to Government Procurement

- Procurement processes should be nationally aligned to the greatest extent possible, transparent, and subject to ongoing improvement to reduce the costs of tendering and access for domestic suppliers, particularly SMEs.
- Government should consider exploring a 'principles-based' approach to some elements of procurement to better facilitate innovation and manage competing interests (local content, recycled content etc.).
- Procurement projects should be designed to enable businesses to leverage the relationships they build, or the products/processes they develop, to find more opportunities in local and global supply chains.
- Governments should be flexible on the definition of local content, and 'local' should apply to Australia broadly, not single states.

Policy approach to Government Procurement

There are opportunities for well-designed procurement rules for governments to create positive market impacts in line with broader goals such as stimulation of domestic manufacturing capability, management of waste, the circular economy transition, and environmental sustainability more broadly. To better support domestic businesses to participate, grow and gain access to more local and global opportunities, in designing the use of procurement arrangements for these ends, strong consideration needs to be given to the barriers to access in Government projects, such as specifications and complexity, emphasis on upfront costs and a lack of harmonization.

3. Climate Policy and Energy

Recommendations

- Ensure budgetary space for the outcomes of the Gas Substitution Roadmap when finalized.
- Offer public support to address transmission development challenges, applying surplus Easement Land Tax revenues to defray the costs.
- Support industry decarbonisation including by assessing the efficiency and effectiveness of using public procurement and industrial contracts for difference as policy instruments to support decarbonisation.

Policy approach

Successful transition to net zero emissions and a new energy advantage is critical for businesses in Victoria and nationwide. While the State already has significant activities across multiple workstreams there are further steps that should be taken or provided for in the coming Budget. These relate to natural gas transition, electricity infrastructure, and signalling credible demand for clean products.

Natural gas transition

The Victorian Government is currently developing a Gas Substitution Roadmap that considers options for delivering the energy services and industrial feedstocks currently provided by natural gas. The issues involved are very complex, involving diverse user contexts; some technological uncertainty about the best solutions in different contexts; current significant cost premiums for what may eventually be the most attractive options; disagreements over the relative costs of supporting infrastructure needed for electrification versus renewable gas pathways; appliance makers' need for clear frameworks and timeframes; and potentially the need to manage declines in utilisation and value of existing infrastructure without inequitable impacts on remaining users.

The outcomes of the Roadmap are not yet clear and we do not wish to prejudge them. But Ai Group strongly urges the Government to thoroughly resource them in the forthcoming Budget. Transition in gas is not a light lift, but it has wide ranging implications.

Some may be addressed through public funding, some through existing mechanisms such as Victorian Energy Upgrades, some through potential new mechanisms that may be considered. For any transition pathway to work it is essential that sound and well-consulted policy design be supported by adequate resources. Otherwise, gas users will continue to face existing affordability problems and the State's 2030 emissions target will prove harder to achieve.

Electricity infrastructure and funding options

There is no electricity transition without electricity transmission. Multiple major transmission and interregional connection projects are needed to support the emerging high-renewables electricity system. However, these projects face significant barriers. These include the concerns that major developments cause to local communities and landholders, which could stall existing developments or (if ignored) poison sentiment towards the many further projects that will be needed; and the existing cost allocation approach to interconnections, which can't take account of benefits beyond the borders of the two regions being connected.

Energy users are already apprehensive at the cumulative cost of the transmission projects that are likely to be required, though these fears will ease if the projects are well chosen, well delivered and demonstrate strong systemic value. Public funding may be an important part of solutions to the barriers mentioned above. Support and benefits for impacted communities can address development concerns. Cash or finance injections outside the regulated asset base cost recovery process can sidestep the limits of hard-to-change cost allocation methods and other roadblocks.

One possible source of funding could draw from the State's Easement Land Tax (ELT) targeting transmission easements. The ELT effectively taxes electricity consumption in Victoria. Originally introduced to fund past commitments to the aluminium sector, ELT revenue has grown strongly with land values and is now well above the cost of the State's

aluminium arrangement. Consideration should be given to applying surplus revenue to defray costs to energy users, or support developments that will benefit energy users.

Demand signals for clean industry

Reaching the State's widely shared (including by Ai Group) goal of net zero emissions by 2050 will require transformations in the production of many materials and goods, including aluminium, cement, chemicals, glass, steel and much more. While some improvements will be incremental, zero- or near-zero-emissions products will ultimately require new or substantially upgraded facilities using different or heavily modified processes. The significant investments required will be made when investors are confident in demand for clean products.

There are many potential policy pathways to support that demand. We offer two for consideration in the coming Budget.

Procurement and infrastructure.

Public procurement is a substantial source of demand, particularly for currently emissions-intensive construction materials. Government should consider whether it is efficient and effective to leverage procurement to establish forward signals of its intention to increase over time the share of cleaner materials and products in its procurement and in publicly supported major projects.

Many cleaner processes currently have a significant cost premium over conventional alternatives. Thus, a decision to commit to, for example, at least 5% low-emissions cement and concrete would have significant budget implications. However, demand for and deployment of these low- and zero-emissions technologies is essential to lower their cost over time. The Government should therefore evaluate how effective it would be to provide long-term indications of its preparedness to pay for a growing percentage of clean products in relevant procurement streams, especially infrastructure and public buildings. A part of this would be to define what counts as 'clean' by using outcome or performance metrics rather than specifying technology inputs.

Industrial Contracts for Difference (CfD).

The Government has already used a form of CfD through the Victorian Renewable Energy Target, providing investors with increased revenue certainty that eases development and lowers finance costs. CfDs are also potentially relevant to industrial decarbonisation, where industry faces various forms of uncertainty and often significant, but declining, cost premiums for clean inputs or processes. Very substantial investments in clean production could be greatly de-risked by CfDs for industrial inputs (such as the cost of green hydrogen versus natural gas) or outputs (such as the cost of zero emissions aluminium versus prevailing market prices). Germany is consulting extensively on industrial CfDs as a plank in its transition strategy. Victoria should explore this concept further with industry and other stakeholders.

4. Waste and the Circular Economy

Recommendations

- Funding decisions for circular economy and waste should consider, complement, and capitalise on federal funding opportunities to maximise outcomes for businesses and the community.
- Funding for company level product stewardship and circular projects could help drive innovation and action in Victoria, beyond scheme or regulatory activity.
- State purchasing decisions should drive circular economy transition and procurement processes should be flexible enough to manage competing policy interests, while delivering value to the Victorian community.
- Increased reinvestment of landfill levy funds should be used to expand sorting and processing infrastructure, and support demand for recycled content.

Policy Approach

Ai Group supports the Government's objectives of decreasing waste and promoting the development of the circular economy.

State funding in support of these objectives should consider, complement, and capitalise on federal funding opportunities (such as the National Product Stewardship Investment Fund (NPSIF) and the Modern Manufacturing Strategy and Initiative) to maximise outcomes for businesses and the community.

Funding for product stewardship and circular projects at a company level should be used to support Victorian businesses to work towards state policy objectives as well as contribute to national efforts in this area. Industry-led stewardship can help to stimulate innovation and maximise the benefits of public funding through co-investment.

The government should evaluate the relative efficiency of supporting markets for circular products and services through its procurement practices. Where circular principles are concerned, sustainable procurement by government should go beyond blanket recycled input specifications (which are inflexible and vulnerable to supply issues) and foster genuinely improved outcomes and innovations.

Public and private procurement is becoming increasingly complex due to our understanding of value evolving beyond cost to include social and environmental considerations. Our broadening view of value creates a need to manage complex and competing policy objectives, such as buying local or using recycled inputs, which may be at odds with each other. Investment in skilling procurement experts to manage these tensions can potentially unlock greater value for the state.

Victoria should also consider whether an efficient and effective way to increase sorting and processing infrastructure and supporting demand for recycled content is to reinvest a greater percentage of landfill levy funding for these purposes.

5. Taxation and Charges

Budget proposals

- Do not introduce any new taxes or business charges.
- Remove the payroll tax surcharge on larger businesses introduced in last year's Budget.
- Reconsideration of the Government's Superload Charging Policy.
- Adopt a leadership role in initiating and sustaining a national conversation on the adoption of a structure of taxation and intergovernmental transfers that will equip the country for the considerable emerging fiscal challenges.

Policy approach

Taxation imposts are currently holding back investment and job creation at a time when we need to ensure the economy recovers and rebuilds. Business is especially nervous about new taxes, levies and imposts. The additional costs impact on business competitiveness and confidence and may cause a re-think on their investment. We can point to individual businesses that are considering their investment decisions in Victoria based on their concerns that Government impositions on them will continue to increase.

This situation should not be allowed to get any worse and, at a minimum, Ai Group urges the Government not to introduce any new taxes or charges in the 2022-23 Budget. Beyond this we also advocate for the removal of the payroll tax surcharge announced in the Government's 2021-22 Budget. This is a discriminatory and distorting tax impost; it has contributed to the erosion of confidence in the Victoria Government, and it has seen businesses reconsidering plans for new investment in the state and looking more closely at alternative locations beyond the state's borders for their existing operations. Its removal would not only send a sharply positive signal to the business community: it would improve the disincentive for them to add more jobs and allow them to contribute more decisively to the recovery of employment in the state.

Worksafe liabilities continue to be a concern for the Government and businesses which are required to pay premiums. Ai Group's concern is that the scheme is being asked to manage liabilities and claims that it was never established to do. This is particularly in relation to mental health injuries which continue to increase and are increasingly supported. Many of these claims are not caused by the workplace, yet employers are being asked to support people on the basis that they are a workplace injury.

Ai Group recommends that Worksafe premiums not be increased and that a better model be considered to support those who are claiming mental health injuries. Increased premiums would become an active disincentive to employers to increase its labour force.

The increasing costs of OHS and the allied response to COVID 19 should, we suggest, also be at the forefront of the Government's mind. Businesses have accepted the increasing cost of doing business as a result of the pandemic but it also means the ability to have other costs imposed is extremely limited.

The Government should reconsider its Superload Charging Policy. The policy is imposed on local manufacturers and significantly erodes their margins. It is particularly difficult for manufacturers using super loads and attempting to be competitive in other states. The government could consider the best process too support local manufacturers which need

to use Victoria's road system. Perhaps companies paying payroll tax in the state should be exempted from the current Tupelo judging policy post up consideration needs to be given to ensure manufacturers remain competitive with overseas operators.

We recognise that, under existing taxation arrangements in Australia, the states have limited options for raising revenue in an efficient way. Our national current tax arrangements are simply not in any shape to meet the tasks of putting our public finances on a sustainable footing and rebuilding our fiscal buffers. They certainly provide little leeway to finance new areas of public sector activity however meritorious.

As a critical step to longer term reforms to the adequacy, efficiency, fairness and sustainability of taxation arrangements, there is a need for mature and principled discussion. Ai Group urges the Victorian government to take a leadership position in progressing this critical agenda.



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