

THE ROLE OF MODERN GOVERNMENT

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ABOUT THIS PAPER

When Labour re-enters government it will be faced with the challenge of providing real growth to an economy facing serious external pressures and internal (and long running) structural issues. We will not be able to sustain the everyday, foundational economy we need or rebuild the public services we require, unless we do so.

The consequences of the pandemic, and the still uncertain duration and depth of issues caused by the war in Ukraine make this challenge doubly difficult. It is likely that the the mid 2020's will be a tight fiscal environment whichever government is in power.

In this context Labour must invest but it also must innovate. It must strain every muscle available to a government in a developed economy to go for growth and do the best by the people of Britain. Having been out of power for so long, the danger is some of these muscles have atrophied, and this paper sets out to remedy that.

Inside the author draws on his experience at the highest levels of finance and the ESG world, as well as the insights of othe business and political leaders to set out what these areas are. Where Labour can have a major impact on business and society in either a fiscally neutral or low cost way. It is intended to stimulate thinking among Labour politicians, policymakers & supporters with time to develop policy ahead of the next election.

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Andrew Dyson has recently retired from a career in investment management and investment consulting in the UK and US. His last executive role was Chairman and Chief Executive Officer of PGIM Quant Solutions, a \$120bn asset manager, from 2017 until earlier this year, and chaired the inaugural PGIM ESG Council.

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FOREWORD

GOVERNMENT MUST BE A CHANGE MAKER

After 12 years of Conservative rule we seem to have come full circle. A Government born with a message of austerity has ended up back where they started. In between we have had 12 years of low economic growth and stagnating incomes. The recent Tory mini budget showed the perils of a cut and run dash for growth discarding any notion of fiscal responsibility. The result was higher borrowing costs for the country and families, a warning from the IMF, an emergency intervention from the Bank of England to prop up pension schemes and serious damage to the UK's international reputation.

No Government gets to choose the circumstances in which it comes to office. If Labour wins next time, it looks likely that it will be down to us to restore the UK's financial stability as well as make the changes we all want to see. As Keir Starmer has said, that might mean that some things we want to do – good Labour things – take longer than we would have hoped.

However our commitment to financial stability should never be interpreted as lack of ambition or hunger for change. What it does mean is that we have to look to more than public spending as a mechanism for achieving change. Resources matter. They always do. But so too do new ways of working, innovation in how things are done and making the most of technological change.

This paper sets out some ideas of how change might be brought about with either no or minimal increased spending. There is of course a formal Labour policy making structure and none of the ideas here should be considered as policy we have adopted. They are however a very useful contribution to a debate that we need to have.

No one joins the Labour Party because we want to keep the world as it is. We are the change makers. We have rescued our public services before and we will do it again. And we will do it in a way that combines investment with change to ensure we get the best value for money and the best outcomes possible.

Pat Mcfadden MP,
Shadow Chief Secretary to the Treasury

THE ROLE OF MODERN GOVERNMENT

INTRODUCTION

Since its foundation, the Labour Party has always believed that government can make the lives of people better. Nothing has exemplified that more than the foundation of the NHS which has and continues to lift and support the wellbeing of the British people. Unfortunately, because of chronic mismanagement of our economy for the last dozen years by the Conservatives, an incoming Labour government will be severely constrained in its ability to spend more money, and what limited funds exist will inevitably need to be primarily focused on health and other services that have been so systematically run down by the Tories.

However, that does not mean that we should abandon our belief in or ambition for the power of government to make a difference. In this paper, we provide a systematic high-level framework to spell out how good government can make a huge difference to the British economy and British people without needing to spend significant money, as well as examples of individual ideas that flow from this framework. We hope this will allow us to follow up by fleshing out specific areas of interest in more detail based on dialogue around these concepts.

As the Labour Party leadership has made clear, accelerating economic growth is central to everything they want to achieve and a necessary precursor for achieving their ambitions in government. The relationship between government and business is at the heart of this mission. Building and facilitating good, successful, strong British businesses – big or small – will be central to helping achieve this vision for the UK. Businesses create and sustain jobs – both directly and through the indirect services they need; they should support rising wages that allow their workers to share in the growth they create; the tax they should pay helps provide the services on which they and the whole country depend; and they can create new industries and areas of competitive advantage that help the UK succeed internationally.

Equally, having a strong pro-business agenda within government does not mean a blank cheque that ignores bad practices. As we will lay out, there are also individual businesses that fall short of this standard. They may try and make profits at the expense of their employees, or indeed at the expense of the British taxpayer and British society by artificially avoiding taxes, or by ignoring the standards that society has set as acceptable conduct e.g. in terms of the environment. Labour's pro-business agenda does not mean overlooking these issues but rather tackling them in a way that supports the majority of businesses that don't behave this way.

Finally, we should freely acknowledge that although the market economy is incredibly powerful at creating overall economic growth and individual opportunity, no system is perfect, and there are many areas where a market system on its own will fail. Government can and should step into these gaps and look to address these failures.

Government policy backed up by committed government action can address all of these without needing to spend significant sums of money and can allow good businesses to thrive while eroding or preventing the bad practices that a minority follow.

We hope this document provides a road map for impactful policies that will once again reinforce belief in the power of government to make a difference to people's lives, to create and cement the growth that we so badly need, and yet to do so in a manner consistent with the economic mess that a Labour government will be inheriting.

OVERALL FRAMEWORK

In what is likely to be a tight fiscal environment, a future Labour government will need to leverage everything it can to make a difference. There are many levers that should be available to a government to achieve its policy goals without having to commit substantial incremental funds, and these often are given much less consideration than they should be.

The goal of this work is to shine a light on the power of government to make a difference and to layout a systematic framework to categorize and explore specific opportunities. We explore the ability of government to make a difference under the following headings:

1. Regulation / legislation
2. The role of regulators
3. Competition policy
4. Industrial policy, including acceleration of new markets
5. Trade policy
6. Enforcement of existing and new laws and rules
7. Procurement
8. To use other areas of policy to enhance tax collection
9. Incentivisation and activation of private capital
10. As a “groundbreaker” where a small amount of government support can be leverage into much greater multiples of private capital

Although it's clearly a major area of government activity, we are not including any direct work on taxation principles or the taxation base. However, we do recognize and address a range of ways government activity can provide incentives for companies or individuals to refrain from avoiding tax.

THE MANY ROLES OF MODERN GOVERNMENT

In this section, we examine the underlying principles behind each of the above, and reference specific examples of policies that might flow from applying these principles:

1. REGULATION / LEGISLATION

If we want to change society for the better and support those who are being left behind, it is important not to underestimate the power of regulation.

In particular, any regulation around the behavior of employers / companies can favorably impact their workers and customers. For example, ensuring that 'platform' companies give identical rights to their staff as traditional businesses, or ensuring that restaurants pay all tips and service charges over to their workers are zero cost ways of making a real difference.

Legislating against the ability of big companies to delay paying their suppliers – as opposed to the current voluntary code - would make an enormous difference to the ability of small companies to survive and thrive.

Another interesting area to explore is the potential of broad anti-avoidance legislation; narrowly drawn legislation often creates a sub-industry of advisors around how to circumvent the intent of the legislation. It would be valuable to explore if and how broad legislation could prevent this because it does not require government to think through all the unintended loopholes in advance.

This principle is applied in other legal and regulatory areas, e.g. Similar strategies have seemingly proved effective in the tax field but can this be extended into other domains such as anti-profiteering?

Possible policy examples:

- Ensuring equivalent employment rights for flexible and part time workers.
- Compelling restaurants to pay all service charges to their staff.
- Compelling prompt payment of small suppliers.
- Use of broad anti-avoidance legislation to prevent deliberate circumvention.

2. THE ROLE OF REGULATORS

There is much frustration around the behaviour of quasi-monopolistic or oligopolistic industries which creates a demand for nationalisation. But this latter path may be the only acceptable course of action in some cases, but must never be undertaken lightly. In every case it will be expensive, disruptive and legally and politically fraught.

In most cases, effective regulatory frameworks could achieve the desired goals / behaviours. General regulatory frameworks always involve setting a balance between the interests of the company / shareholders vs the customers, workers and wider society.

How that balance is set can be supportive of or detrimental to our political goals. Achieving a stronger commitment to infrastructure spending across the economy, greater emphasis on green technologies, firmer commitments to better service for citizens at scale will require Labour to address this balance of power via regulation.

One area to consider is the regulators themselves: it is essential to understand why existing regulation fails to achieve its desired ends and how we can avoid regulatory “capture”. Consideration should be given to the structure, skills and oversight of the disparate regulators. We would include the Financial Conduct Authority (FCA) in scope here since it has a critical role to play in ensuring a fair and effective financial and savings system.

Possible policy examples:

- Review of individual regulatory frameworks and associated powers and penalties.
- Review the structure of regulators, including potential benefits of an overall regulatory oversight department.
- Review of regulation as a positive, achievement oriented activity – as well as a protection against bad practice.

3. ENFORCEMENT OF EXISTING AND NEW LAWS AND REGULATIONS

Corporates are economically rational entities and will generally be making balancing decisions between the practical costs of non-compliance with the commercial impact. A commitment to vigorous enforcement can therefore change their behaviours much more quickly and effectively than new laws and does not need any spending. Many regulations are sufficient on paper but have been lackadaisically enforced by Conservative governments.

For example, making non-payment of the minimum wage easier to report accompanied by strong penalties for non-compliance would quickly deter employers from such behaviour. Likewise, much stronger penalties for antisocial behaviour, such as waste or sewage dumping, coupled with vigorous enforcement would ensure companies, management and boards made different choices in this arena.

A further extension would be to ensure that sign-up and adherence to non-mandatory codes of good practice such as the Prompt Payment Code is strongly encouraged.

Possible policy examples:

- Review of existing rules and laws to identify areas which are not being effectively enforced or where the penalties are insufficient to promote compliance.
- Consideration of how to promote wider adoption of codes of good practice.

4. COMPETITION POLICY

Competition policy can have significant impact on the economy at both a macro and micro level. At a macro-economic level, there is considerable academic evidence that declining competition within industries is weakening the position of both customers and workers. Labour should investigate routes to restore a balance that works for all stakeholders.

The digital industries present a very specific case, because left unchecked the economics of platforms can facilitate a higher level of concentration, so this means that particular scrutiny is needed of takeover and anti-competitive activity in this area.

At a micro-economic level, particular thought is needed around the preservation of key companies and industries within the UK economy, and we should consider what the parameters of those might be, as well as how this can be best achieved.

Possible policy examples:

- Strengthening of government powers to maintain competition and prevent over-concentration in specific industries.
- Development of a specific framework for the technology industry given the unique challenges that it presents.
- Creation of a framework for protecting key national companies and industries.
- A strategy for dealing, in a balanced manner, with anti-competitive practice from overseas business.

5. INDUSTRIAL POLICY, INCLUDING ACCELERATION OF NEW MARKETS

Many governments around the world have successfully prioritized development and global success in particular industries. Typically, this has been because they represent areas of national competitive advantage which can help accelerate growth, or because they meet a specific domestic policy need and priority.

For example, an incoming Labour government is likely to want the UK to be a leader in our ability to support the transition to Net Zero globally. Government has several levers available to support a desired industrial policy such as either creating tax allowances and incentives for investment which can be tied to particular industries or encouraging geographic clustering of expertise through looser planning rules (or place-based taxation variations).

A comprehensive approach to “place” will also address subsidiary barriers as well such as lack of housing or lack of cross-provider transport ticketing. A less often recognized strategy is around shortening the time for new technologies to scale by stimulating and accelerating adoption e.g. by subsidizing the cost to consumers for a period. The logic is that a new technology such as solar panel use or electric vehicles may find some initial early adopters but can take a long time for demand to increase. This inhibits the benefits of scale that come from broader adoption and help reduce costs and make the technology competitive. Government action can accelerate that adoption process.

Possible policy examples:

- Development of incentive structures for the encouragement of national industrial priorities.
- Consideration and removal of specific barriers to achieving these priorities e.g. in housing or transportation.
- Identification of areas of national advantage or priority that are sub-scale today, and strategies for accelerating their take up.

6. TRADE POLICY

Any honest conversation with business today will reveal the difficulties and loss of opportunities that the casual attitude of the Conservative government to Brexit has created. Their approach has directly impacted our growth and financial prosperity at a national level as well as harming the individual businesses of all sizes.

Labour must pursue trade policies that serve the interest of British business and British consumers. Making Brexit work by adopting an intelligent trade policy with our biggest export market – rather than today’s casual and dogmatic approach - should be an immediate goal for an incoming Labour government before any further economic damage is done.

Possible policy examples:

- A detailed consultation with business about its needs from central government’s trade policy.
- Development of broad social and economic objectives for Britain’s trade policy as an independent nation.
- A plan for the centralized institutions of trade policy specifically the DfIT.
- Development, negotiation and implementation of an effective post-Brexit trade strategy.

7. LEADING BY EXAMPLE, INCLUDING THE USE OF PROCUREMENT

One advantage of Brexit is that it does offer government greater freedom to define its procurement policies to take account of broader societal impact of those purchases.

An often quoted example would be a greater ability to “buy British”, and we should establish a robust framework for direct procurement activity including consideration of whether any legal clarifications are needed in the new operating environment.

However, we should explore other areas where there are broader benefits e.g. insisting on a minimum level of corporate tax payment in the UK as a condition for being a candidate supplier would produce both direct incentives not to evade UK taxation but also strong PR incentives to be on the eligible list.

This can usefully be extended more broadly to consider how government can lead by example, or use its position to advocate for good behaviors from corporates as well as put pressure on and highlight behaviors that are antithetical to the broad societal goals that we seek to achieve.

Possible policy examples:

- Review of procurement policies to see how they can be used to accelerate / achieve other policy goals
- Consideration of the power of Government PR and endorsement, and how this can be utilized to promote good corporate behaviors and deter bad ones.

8. TO USE OTHER AREAS OF POLICY TO ENHANCE TAX COLLECTION

The example in section seven of insisting on a minimum level of corporate taxation as a condition of being a candidate for procurement highlights a broader principle. Without changing the basis of taxation in any way, government can increase tax revenue overall by adopting policies that discourage avoidance strategies.

Another example in the individual field would be to follow the example of the US and insist that a condition of retaining a British passport even while abroad is to file UK tax returns; it is completely reasonable to take the view that citizenship has both rights and responsibilities.

Possible policy example:

- Consideration of areas where rights of citizenship should be balanced by disincentives to avoid tax e.g. in maintaining a British passport if non-resident.

9. INCENTIVISATION AND ACTIVATION OF PRIVATE CAPITAL

Globally there is substantial institutional and corporate capital looking for effective investment opportunities. Another mechanism to achieve policy goals is to explore structures to encourage the allocation of that capital without needing to spend government money directly e.g. through targeted taxation incentives or allowances.

This can be married with localisation policy goals (such as in a “leveling up” type agenda) e.g. by creating differential incentives to establish new employment in some regions over others. Different incentives are likely to produce meaningful outcomes since the corporate policy decision will be a relative one (as exemplified for example by US location decisions albeit there are many flaws in that local system that a more centralized version could avoid).

Another facet of enabling private capital is to ensure that there are no artificial legal or regulatory barriers to allowing institutional investors to invest in desirable areas where they are otherwise keen to do so e.g. in long-term environmental or social projects.

Possible policy examples:

- Targeted incentives for private sector investment in key priority areas.
- Favorable local investment regimes to bring capital into areas of historic underinvestment
- Removal or amendment of any legal or regulatory hurdles that are otherwise deterring needed investment.

IO. AS A 'GROUNDBREAKER' WHERE A SMALL AMOUNT OF GOVERNMENT SUPPORT CAN BE LEVERAGED INTO MUCH GREATER MULTIPLES OF PRIVATE CAPITAL

While these areas potentially involve some commitment either of funds or backstop, so are not truly cost-free, the goal would be to explore structures where a small amount of government commitment would produce a much larger quantity of private sector investment.

This could take several forms e.g. there are tranching funding structures where the total capital raised is multiples higher than the “equity-like” capital in the last tier, and the ability to find those equity investors acts as a limit on the total fund raising.

The willingness of government to be that equity investor could then unlock the whole structure. Likewise, if government is willing to act as an insurer of last resort that may take away a very small sliver of risk that was otherwise preventing a desirable project or investment from getting going e.g. the Dutch National Mortgage Guarantee scheme. Consideration should be given to the effectiveness of the British Business Bank in this area, and whether it can be enhanced in any way.

Possible policy examples:

- Creation of joint investment structures with the private sector which significantly multiply the capital committed
- Creation of Government-backed national mortgage standards and structures which allow broader mortgage availability.
- Review of the operation and effectiveness of the British Business Bank.

CONCLUSION

As we said in our introduction, one of the key defining lines of the Labour Party throughout history has been the belief that government can make people's lives better and be a force for good across the economy as a whole.

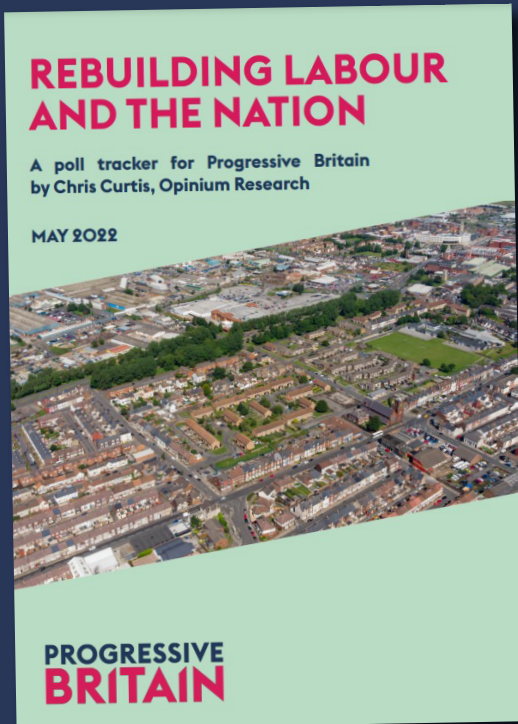
Throughout much of that history, that good has come through direct government spending, e.g. with the creation of the NHS, but because of the economic mismanagement after what will likely be 14 years of Conservative government added to the burden of the COVID pandemic, the scope for additional government spending will be at best very limited.

However, this does not mean that we should abandon our aspirations for government to improve the lives of the British people. As this paper has described, there are in fact a huge array of tools that an incoming Labour government can use to be a force for good without the need for meaningful incremental spending, if any. Moreover, many of the impacts of resultant policies will be felt more quickly. There is no need to either abandon aspirations or fall into the political traps of opponents. By embracing these opportunities instead, the Labour Party can develop a highly positive and impactful program for government.

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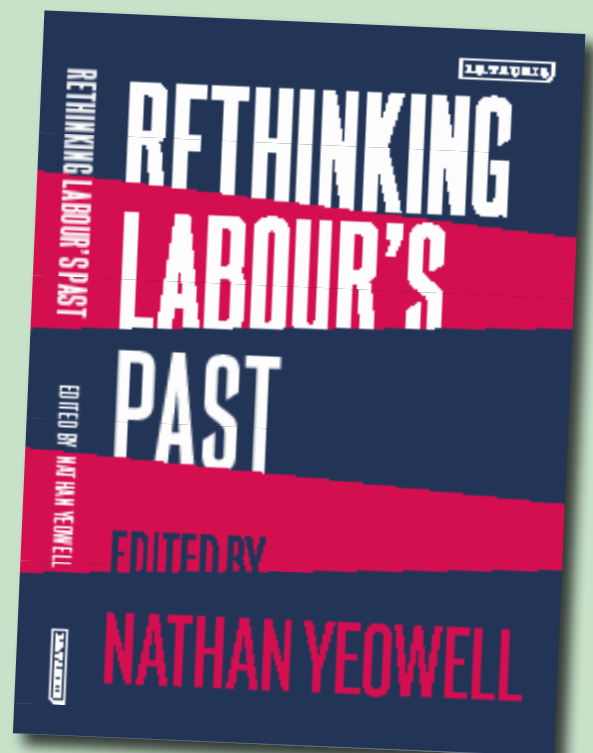
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