

STANDPOINT.

David and George, Make Up Your Minds

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David Cameron and George Osborne are the real division in the coalition (Bloomberg/ Getty Images)

Coherence, according to one definition in the OED, is a "harmonious connexion of the several parts, so that the whole 'hangs together'". It is a concept that seems alien to the Government. And not because it is a coalition. Sure, any coalition government will cope with differences of opinion. And this one is no exception, as the recent rather ugly campaign to change the voting system in Britain clearly demonstrated. It is no surprise that the Prime Minister and his Deputy disagree over the extent to which Britain should surrender further sovereignty to the EU, or at least that is the case if the Prime Minister means what he says about preventing further transfers from Westminster to Brussels. Nor is it any surprise that the coalition partners disagree about policy towards immigration, or the NHS.

Not for me to say whether those differences are worth bearing, and in some cases ignoring, in order to be in government. The fact is that a coalition has been cobbled together and is functioning, providing an answer to the question put by Tevye in *Fiddler on the Roof* when confronted with his daughter's decision to

marry a non-Jew. "A bird may love a fish, but where would they build a home together?" The answer seems to be, "In the House of Commons." Indeed, it is arguable that the surprisingly strong performance of the Conservatives in the May 5 elections proves that he has developed a formula that works, one that enabled him to win the referendum on alternative voting, and to make some gains while his coalition partner was destroyed and Labour suffered a huge defeat in Scotland.

Why tinker with a winning formula? Answer, because a formula for winning a series of local elections is no more certain a formula for successfully governing and sweeping the field in a general election, than a formula that results in losses in local elections is a formula for a defeat in a general election. In the end, a government must govern, and given the circumstances in which Britain now finds itself it must govern effectively — produce results that move the country out of the economic intensive care unit at least into the rehab section.

Because differences between the coalition partners attract so much media attention, there is a danger that the results of the May 5 election will continue to obscure the far more important fact that the government is groaning under the burden of its incoherence, not created by differences between the parties of the coalition, not even by differences between the wings of the Tory Party, but between the team of Prime Minister and Chancellor of the Exchequer, on the one side, and...well, the team of Prime Minister and Chancellor of the Exchequer on the other. The result is an incoherence, what Karl Marx might have called internal contradictions, serious enough that neither the Prime Minister's vaunted presentational skills, nor the Chancellor's ostentatious display of confidence and his insistence that he has no Plan B, can conceal the fact that the government so often faces in opposite directions at the same time that it cannot move towards a solution to Britain's ills.

No good to say that Labour doesn't know what it stands for. It can always hide behind the claim that the duty of the loyal opposition is to oppose, or that, after Gordon Brown, it needs time to think through the proper role of a left-wing party. The government is supposed to govern, to take the country in an understandable and visible direction towards a goal it is prepared to defend. This one can't seem to do that, although the road it is travelling is paved with the best of intentions.

One of the best of those intentions is to devolve power from Westminster to local councils. There is, after all, an entire chapter in the Conservative canon about pushing power down to the unit of government closest to the people, and further to "local councils, communities and neighbourhoods and individuals", to cite David Cameron's statement when launching the agenda to implement perhaps his noblest vision, the Big Society. But this government is not engaged in a theoretical exercise: it is dealing with decades in which local governments have become increasingly infected with left-leaning, expansive and intrusive attitudes about the proper role of government; in which councils have become dominated by apparatchiks rather than by citizen-politicians modelling themselves after Cincinnatus; in which multiculturalism and relativism have become the received

wisdom. In short, the government is not engaged in the rather standard and oft-practised process of moving the line that separates the powers of central from local governments a few millimetres to the right or the left, a periodic feature of democratic government. It is engaged in a revolution, an attempt to reverse powerful habits of mind and peel away institutional barnacles in which the existing local ruling class has a major stake. Revolutionaries do not succeed by delegating power to those whom it wishes to weaken or destroy. They succeed by recognising that the facts on the ground are nothing like those theoreticians imagined when they called for devolving power to the smallest unit of government. There are times — such as these — when powerful leadership from a democratically — elected centre is necessary to get the nation's business done, being careful always not to cross the line that separates such as Franklin Roosevelt and Margaret Thatcher from Vladimir Lenin and Adolf Hitler.

One of those annoying facts on the ground is that Britain is entering an age of austerity, one in which fiscal necessity demands that there be "cuts" in government spending, to use the now famous expression for what in some instances are merely nominal reductions in the rate at which spending is increased. The needed austerity is, of course, convenient for those who want to redraw the line between government and individual responsibility, shrinking the former and expanding the latter, to revive civil society. They would push for such a change even if the Treasury were wrestling with the delicious problem of how to distribute a surplus. The Prime Minister is one such, and before finances collapsed and hard times hit, he had been hoping to share the fruits of economic growth between expansion of the State (why remains a bit of a mystery, but it is unkind to demand theoretical clarity of working politicians), and the tax cuts that would increase individuals' ability to choose for themselves just how they want to live.

It was not to be, and he now finds himself in the business of distributing pain, relegated to the role of Scrooge rather than Lady Bountiful. Unfortunately, the Prime Minister has outsourced a good part of the pain distribution to members of a class that do not share his vision of a future nation in which a revived civil society has essentially replaced them. So it is no surprise that Local Government Secretary Eric Pickles is at war with councils that find charitable organisations among the first lambs to shear, his spluttering notwithstanding. After all, the unpaid army of local philanthropists needed to man civil society threatens the jobs and, on a more elevated level, the very philosophy of government that has guided the councillors to whom responsibility for allocating "the cuts" is being devolved. And, because secular Britain does not have the network of churches that perform so many social functions in America, it is unlikely that civil society will spring full-blown from Cameron's head, especially with the local powers-that-be stomping on any signs of voluntarism replacing government direction and compulsion.

This is one policy area in which the government is being crushed under the weight of its incoherence. It wants to devolve power from the centre, and it wants to direct newly scarce resources to purposes uncongenial to those to whom it is

devolving power. If withdrawing some vital service prevents a cut in executive salaries; or funds construction of fancy, very green offices for councillors; or permits the hiring of a "head of strategic commissioning" at £79,000-£87,000 per annum, surely no one can doubt the wisdom of such a move. And if a civic group appears and volunteers to run a community centre on a self-funding basis, why permit such an intrusion on the government's sphere? Better to close it than to allow creeping privatisation.

You can't have decentralisation of power to a bureaucracy that quite naturally believes its pay cheques are top priority if you also want to keep libraries open; you can't hand the power to distribute pain to politicians who value easing the social problems of transgender citizens over well-lit streets; and you can't rely on the emergence of a disinterested band of politicians to challenge the entrenched bunch after so many years when the public has had no experience of a better way of running a town, and sees only short-run loss from transferring power to Burke's little platoons, if any such have survived the past decades of local misgovernance.

Despite such examples, the government sees no inconsistency in pursuing both the goal of decentralisation and the goal of resurrecting civil society. But, as in the words of the popular song, "It's gotta be this or that."

So, too, with the government's policies towards the financial sector. The government recognises, as all but the economically illiterate must, that Britain has a huge competitive advantage in the provision of financial services — banking, insurance, lawyering. It also recognises, although this is less certain, that the health of that sector depends on the infrastructure in what is called the City, and on the ability of its inhabitants to interface with comparative ease, grumbling about public transport and traffic notwithstanding. Finally, it recognises, or says it does, that the health of the financial sector depends on its ability to attract wealthy investors, many of them non-subjects of the Crown.

So far, so good. Enter incoherence. More than one government official has preached to me the importance of geographic and economic diversification, which on inquiry often turns out to reflect an anti-City bias: City denizens earn too much, they don't make things, their lifestyles are offensively ostentatious. Scarce resources must be spent, they say, to attract businesses away from the City and into sectors other than finance. The political motive is clear: there are votes to be had, maybe, up North, from a bit of City-bashing. But the economic logic is unclear: the City is a wealth-creating, export-leading jewel in the economy's dented crown. To build economic policy around an animus to it, or some mistaken notion that to grow the rest of the country it is important to neglect the City, borders on the bizarre.

As does the approach towards an expansion of Heathrow. Again, there is one policy that proclaims Britain to be open for business, and another that makes it difficult to get here. The Prime Minister's scuttling of a third runway is forcing BA to plan a hub at the new, modern, under-utilised Madrid airport, so that high-

flying businessmen can meet there without suffering the delays and hassles of gathering in London from locations around the world.

There is more, and worse. Merlin the magician may have dwelt in Camelot, but Project Merlin, the deal the government cut with the bankers, is less likely to create so jovial an environment. Again, incoherence rears its ugly head, or in this case, heads. The first problem is the effect the limitation of bankers' compensation might have on London's appeal to these high-flyers, who are high-flyers both in an income sense, and in the sense of their ability to fly to whatever tax locale they find attractive. I am no fan of the procedure by which bankers' pay packages are determined; corporate governance is so badly flawed that excesses are inevitable. But neither do I believe that risk-averse government civil servants, or born-to-wealth ministers can, without a loss of efficiency and dilution of incentives, substitute their views on pay for what a properly functioning corporate governance system, one that aligned private and public incentives, could produce. You might want to make London attractive for international financiers, but you can't do it by attacking the economic propriety and moral basis of their incomes. The disease is poor corporate governance, which can't be cured by political posturing.

Nor can it be cured by taxing earnings in excess of £150,000 at a 50 per cent rate. The government defends this policy, which clearly contradicts its desire to expand the City, on two grounds. First, the high rate is needed to prove to the middle and poorer classes, whose benefits are about to be reduced, that "we are all in this together." Secondly, the 50 per cent rate is temporary. Or so says the Chancellor, who fills the dual-and, at times, duelling-roles of chief political strategist for the Tory Party and keeper of the national finances, the man who proved that politics trumps economics by proposing a special "fee" for non-doms (I am one such) that Eamonn Butler, director of the Adam Smith Institute, estimates brought £162 million into the Treasury at a cost of £800 million lost through the departure of thousands of non-doms. The fee, rather than a more sensible tax graduated according to income, was proposed as a substitute for some inheritance taxes in what proved to be a successful effort to frighten Gordon Brown into calling off the election he seemed at the time almost certain to win.

Like the non-dom fee, the 50 per cent tax, by the Chancellor's own reckoning, is unlikely to raise much revenue-unless a study he has ordered shows that it does, in which case "temporary" might take on the meaning of many "temporary" government measures over the ages. Besides, Mr Osborne has not directly repudiated the Deputy Prime Minister's suggestion that any reduction in the 50 per cent rate be accompanied by a new tax on wealth, or the Business Minister's call for a "mansion tax" — a less incentive-destroying tax than a high marginal tax on incomes, as readers of Henry George will be aware, but not one to encourage wealthy investors to come to or remain in Britain.

What the government fails to recognise is that it is effectively telling high-earners that they must pay more tax. This is because the government must bow to the

so-called popular demand that more of the wealth producers' income be sent to the Treasury rather than spent on their own (lavish) lifestyles. Rather than adopt a Churchillian "never give in", the government has announced that, under pressure, it will limit bonuses, raise taxes and fees, and make life uncomfortable for high earners — the very people it is counting on to come through the door now that "Britain is open for business," rather than hop on a plane to Switzerland.

It is important, of course, not to panic and distort policy in response to threats from high earners to pull up stakes. For many, fresh mountain air is no substitute for the cultural attractions of London, and a more benign tax environment no cure for raging boredom.

But it is equally important not to ignore the many signs that the combination of quasi-official hostility to high earners — not unusual among the classes that benefit from inherited wealth — and a draconian tax regime just might trigger more of an exodus, or discourage newcomers, to an extent that conflicts with policies aimed at producing a speedy and robust economic recovery. And there are many such signs:

- the Adam Smith Institute says its studies show that 500 top managers of some 80 hedge funds have left the country
- the Swiss Funds Association reports that 20 to 25 hedge funds have left the UK for Switzerland in the past year
- a Lloyds TSB poll of almost 1,000 people with savings or investments in excess of £250,000 found that 36 per cent say they want to emigrate, and 14 per cent are likely to leave within two years

Sooner rather than later the government will have to decide whether it wants high earners to enter its open door, keeping in mind that the richest 1 per cent of Britons account for about 25 per cent of all taxes paid into the Treasury. It seems that it does, given the Prime Minister's desire to allow the immigration of relatively well-heeled entrepreneurs. But then again, it seems that it doesn't, because it threatens to tax away what many in the coalition seem to regard as ill-gotten gains.

That policy incoherence is reflected in still other parts of the Project Merlin deal. The government is eager for the banks to shore up their capital base so that another financial downturn does not become a meltdown. It is also eager to show that it is tough on the banks. So it increased the bank levy this year to £2.5 billion in a display of capital-draining toughness. It is also eager for the banks to abandon risky lending, but wants banks to lend more than they ordinarily would to business, especially small businesses.

So, in the hope of ending bank-bashing, the banks overlooked these contradictions and agreed to lend an additional £190 billion to all businesses, including £76 billion to small businesses which have found it difficult to get funding since the financial crisis brought wildly risky lending to an end. How such

mandated lending to businesses the banks do not deem attractive risks is consistent with prudent banking remains unexplained.

In the event that direct taxes on the banks are not contribution enough to the Treasury's coffers, they were required to pledge £200 million of capital to the Prime Minister's Big Society Bank, to be used to finance community projects, mainly outside London and the South East. Clearly, the government recognises that small and medium-size businesses (SMEs in bureaucratese) are important job creators. So one goal of government policy is to encourage their establishment and growth. Never mind that

- higher tax rates act as a disincentive to risk-taking
- increased VAT drains purchasing power that might have been directed to small businesses
- the Treasury's promise to send a horde of tax collectors to teach SMEs how to organise their data might not add to the lure of entrepreneurship
- entrepreneurs are at risk of *ex post* seizure of their profits by a Treasury that refuses to draw a sharp and visible line between illegal tax evasion and perfectly legal taxavoidance

Those are the sorts of things that try the souls of the very entrepreneurs the government wants to see set up and prosper. They are also easy to fix. Another indicator of incoherence is the manner in which enterprise zones are being created. The selection process is so laden with difficulties, the selectors so unfamiliar with the needs of small businesses, that many potential entrepreneurs will find the game not worth the candle.

Then there are the regional growth funds, surely intended to be made available to small businesses. Well, not really. For one thing, the funds are aimed at regions other than the South-East (set up a small business, but not in the City where professional support and a zesty stimulating atmosphere are available). For another, to ease the burden of processing the many applications for limited funds, direct applicants must request a minimum of £1 million, which Lord Heseltine takes credit for reducing from the £5 million level originally contemplated. No surprise that the bulk of the £450 million first tranche (of a total fund of £1.4 billion) went to such fledgling enterprises as General Motors and Proctor & Gamble, with high-tech sectors "relatively under-represented among first-round winners", according to the *Financial Times*.

Resources are limited, as the Chancellor repeatedly reminds us, and it does seem odd for a government that professes dedication to free markets to channel such funds as are available to firms with ready access to capital markets. If reports that the plan is being revised to eliminate its big-business bias are correct, that is good news. Better news would be that the government has decided to use the money to reduce taxes, perhaps the surest way to create permanent jobs. But that would require a coherent rather than a programme-by-programme approach to economic growth.

In short, the government is currently promoting an incoherent mix of policies designed to

- shore up the banks while draining them of capital
- reduce risky lending while forcing banks to lend to businesses at rates some analysts say do not reflect the risks involved
- encourage financial firms to set up shop in Britain while taxing their staffs more and limiting compensation
- foster small businesses while effectively precluding them from participating in the programmes aimed at helping them
- failing to exempt them fully from excessive regulation and Treasury harassment

There is more of course: making war while cutting military spending; trying to become more competitive in world markets while driving up the cost of energy in pursuit of unattainable green objectives; trying to assert the primacy of Parliament while remaining a member of a European Union now dominated by 17 eurozone countries eager to dip into Her Majesty's Treasury, while the Chancellor cries poverty and the Prime Minister promises never to go along with increases in the eurocracy budget (apart from when they ask). You get the idea.

The good news is that it is early days: the *Economist* tells us that the "coalition has not stopped thinking." With the distractions of the May 5 elections behind them, and unless they take the undeniably encouraging results as an endorsement of incoherence, ministers might use their extended summer break to consider their route in the remaining life of this Parliament. In which of the several opposite directions that they are currently travelling do they really wish to go? By the time Parliament reconvenes, the government will no longer be able to count on the incompetence of the opposition, or on voters' willingness to give the inexperienced new boys a chance. Nor will it be able to blame its incoherence on the fact of coalition or disagreements within the Tory Party. It will just have to do what politicians least like to do — decide.