

## **CBI response to the government growth review**

***“The path to strong, sustainable and balanced growth”***

**February 2011**

# SECTION I: EXECUTIVE SUMMARY

## 1. Opportunities for the UK

This paper sets out the CBI's response to the government's Growth Review consultation contained in the joint BIS/HMT Paper "The path to strong, sustainable and balanced growth", November 2010. The consultation specifically invited business to take part in an exercise to look at what each part of the government is doing to address the barriers facing industry.

In this response we have focussed on the six specific "horizontal themes" identified in the consultation:

- Planning
- Trade and inward investment
- Competition
- Regulation
- Access to finance
- Corporate governance

and have illustrated some of the obstacles to growth in each of these areas with examples from sectors or industries that have been adversely affected.

The CBI believes that the big opportunities for growth in coming years are in:

- **galvanising our export performance, particularly to the faster-growing areas of the world**
- **releasing pent-up demand for domestic investment needs and the renewal of our infrastructure**
- **improving the prospects for our high growth firms by ensuring that they can develop their early-years' potential**

In each of these areas, more needs to be done to crystallise and articulate a vision for the UK economy and its place in a rapidly changing global context. In this, the government has a central and critical role to play:

- The growth imperative needs to become a central focus of the government's narrative. This needs to be communicated in a way that captures the imagination of the public. This will make businesses and individuals feel more confident about investing and will support the idea that the UK is open for business so that the UK continues to attract and retain multinational firms and talent.
- Where there are overlapping objectives inherent in policy choices, decisions must be made prioritising the economic growth objective over other objectives. Recent examples of policies in which elements run counter to the growth imperative include the immigration laws, the Bribery Act, many aspects of employment regulation and the lack of clarity around energy regulation and aspects of the localism agenda.
- The government needs to be better joined up across competing objectives which pull in different directions. Their growth vision must ensure that priorities are coordinated towards promoting growth above all else.

## 2. Critical actions for the government to stimulate growth

### 2.1 *Government should redouble its efforts to boost exports*

Much of the UK's success in increasing its exports will be dependent on the underlying competitiveness of UK industry. But in crucial areas, the government also has a significant role to play. The Prime Minister's commitment to boosting UK export performance must be extended fully across Whitehall, and the efforts of UKTI fully supported by all major departments. In particular, we welcome the recent announcement that ECGD will be made more accessible to SME exporters. Additional effort is required to ensure that Free Trade Agreements are concluded with as many target export markets as possible, removing constraints to trade such as cumbersome customs procedures, ineffective IP legislation and protectionism in public procurement. UKTI must be organised and managed in a way that expands its specialist support capability and fully exploits the opportunities of new markets. The government must also play a central role in all aspects of export support, providing world class information, contacts and financial/risk backing.

### 2.2 *Exploit pent-up demand for investment in domestic infrastructure projects*

To facilitate investment in projects in such areas as energy, waste and flood management, decisions are needed in the regulatory and policy framework to reduce uncertainty and encourage investment. Reforms of the planning system must be completed quickly, and urgent clarity is needed about measures to encourage private-sector investment.

**The Electricity Market Review** must provide incentives that align policy and investment cycles and ensure that no competitive burden is placed upon intensive energy users.

#### **An effective planning system is a prerequisite for infrastructure investment**

With £200 billion of investment in infrastructure required over the next five years, it is imperative that the planning system gives investors confidence that decisions will be taken quickly and efficiently. The fast-track process for nationally significant infrastructure projects must be retained. A presumption in favour of development and a clear 'strategic need' test in the National Planning Policy Framework are essential to convince business that the UK is open for investment.

#### **Regulatory certainty is necessary to stimulate investment in the UK's low carbon future**

The priority for the government must be to set the right vision, framework and signals to enable investment in low carbon innovation. The labyrinth of overlapping regulations that businesses currently have to negotiate send confusing signals to the market. Businesses need a clear policy roadmap that confirms the direction and timetable of travel; the lack of certainty is a significant risk factor for potential investors. Even with such a clear policy roadmap, intervention via a Green Investment Bank can help to support these investments by assuming the risks that the market cannot hold.

#### **The uniformity of the current business rate system must be retained**

The uniform business rate is valued highly by business for the certainty, predictability and uniformity it brings for forward budgeting and forecasting rates of return on new investments. Changes to the business rate system under the localism agenda must not be a stepping stone to full relocalisation of business rates.

## **2.3 Support vibrant and growing firms**

### **Stimulate more diverse financing options for mid-cap firms**

While large firms can access a wide array of financing options to suit their needs, many mid caps often rely solely on bank funding. The volumes of debt raised in the listed and private placement market by mid cap firms is far smaller in the UK than in the US. There are many reasons for this but the lack of scale of the UK market is itself one of the main reasons that more medium sized businesses do not issue debt. Encouraging the development of the medium sized corporate debt markets would be self perpetuating as the costs of issuing and investing in the instruments fall and market liquidity increased.

### **Improve access to finance for smaller firms**

Among other measures, the government should extend the Enterprise Finance Guarantee, making sure it fits the needs of IP-intensive businesses where banks find it hard to extend loans in the absence of physical collateral. There should also be encouragement of more SME financing options, especially non-bank and equity financing.

### **Growth Zones can spur innovation**

There is a pressing need to stimulate private sector activity in areas of the country that have grown reliant on public funds over recent years. With the reduced scope for fiscal levers ruling out the largely unsuccessful interventions of the 1980s, Growth Zones can instead attract investment and jobs by providing an incubator for creative solutions to public policy problems. By avoiding a single, top-down solution, and by encouraging areas to innovate – through the use of land auctions in one zone for instance, or the de-regulation of green belt land in another – the government can conduct a real time experiment in what actually works as a spur to economic activity.

### **More autonomy for commercial and industrial parks**

Industrial parks should be given more authority to run their own affairs in such a way as to maximise growth. In areas that do not have residential premises – such as industrial parks – local authorities should cede decisions over issues such as planning, energy generation and skills development. This would allow firms to formulate action plans that suit their needs –through quicker decisions on micro-generation, or Group Training Associations for instance – in a more effective and efficient manner.

### **Recent regulations continue to hamper businesses**

Upcoming changes including the agency workers directive, the default retirement age and the bribery act will all cause considerable administrative burden and increase uncertainty in the business environment. Harnessing companies' growth potential relies on removing regulatory barriers from investment and job creation not enacting new ones.

### **Reinstate the energy efficiency incentivises for companies in the CRC**

By removing the revenue recycling element of the CRC Energy Efficiency Scheme, the government has undermined its objective to change behaviour. Instead, business is now unexpectedly faced with a 'stealth tax' on carbon which, instead of providing impetus for energy efficiency savings, will likely be written off as another cost of doing business in the UK. To encourage action on energy efficiency, the government must reinstate revenue recycling in the CRC or, if the money cannot be found to do so, stop the scheme and provide a simplified mechanism to encourage take-up across the business community.

### **Government needs to be challenged to resist regulation**

The government's default option should be to avoid regulation if possible. Measures that would help in this regard should include: proper enforcement of the 'one-in-one-out' rule; a 'Regulatory Ombudsman' to rule on jurisdictional issues; consistency in the metrics required for reporting purposes to improve the flow of information from firms to regulators; and a system of single regulatory managers as 'point of contact' to improve co-ordination of multiple inspection visits.

### **The incentives in employment regulation discourage hiring**

Companies – especially SMEs – must feel more confident in creating jobs. This will require concerted action to protect firms from the massive costs – win or lose – associated with employment claims. Restoring the unfair dismissal qualifying period to two years is important, but the government must also act quickly to tackle perverse incentives in the tribunal system. With no cost to raising a claim, the system encourages legalisation of the employment relationship with weak claims from disgruntled employees, who expect a payout regardless of the strength of their case. Greater use of pre-claim hearings, cost awards and the introduction of a deposit system for claims will help address this. The removal of the default retirement age has also made hiring more difficult, as firms are unable to plan ahead with confidence.

## **2.4 *Ensure fundamental restructuring of public services continues to support growth through fiscal consolidation***

### **Increase competition in public services**

Restoring fiscal health to the nation's finances means that public services must focus on the outcomes they deliver for the public and the value they achieve for the taxpayer. An outdated view of the state as a monolithic default provider must not stand in the way of the innovation, modernisation and investment that is waiting to be unleashed through increased competition and choice.

## SECTION II: DETAILED PROPOSALS

### 1. PLANNING

Securing up-to-date infrastructure is a fundamental platform for sustainable economic growth. It is estimated that the UK needs approximately £200 billion of infrastructure investment over the next five years, much of which will come from the private sector. An effective planning system capable of delivering timely decisions is crucial to attracting this private sector investment.

#### 1.1 Strategic planning at a sub-national and national level

***The fast-track process for nationally significant infrastructure projects (NSIPs) must be retained with ministerial sign-off***

The transition from Infrastructure Planning Commission to the Major Infrastructure Planning Unit is already undermining investor confidence, and we cannot risk eroding this further. Changes to the major infrastructure planning system should therefore be kept to an absolute minimum beyond the reinstatement of ministerial sign off. The sign off itself should remain subject to a rigorous three month time limit.

***The National Planning Policy Framework should provide a presumption in favour of sustainable development***

The inclusion of a presumption in favour of sustainable development in the NPPF will help ensure that development should go ahead where it meets the necessary environmental, economic and social criteria. The NPPF must articulate clearly the reality of our national infrastructure priorities for energy, transport, housing, waste and digital infrastructure, as well as the local benefits that come with permitting such development. A presumption in favour of sustainable development within the NPPF, tied to delivery at the local level by distilling national priorities into local priorities, will aid in the delivery of infrastructure of national importance.

***The statutory duty to cooperate must be strengthened and enforceable***

The proposed 'duty to cooperate' between local authorities in the localism bill is welcome, but it is not yet clear how it will work in practice and be enforced. Strengthening the duty will ensure that there is joined up thinking on crucial issues such as waste management and housing development.

***Land auctioning by local authorities must be strongly considered***

Land auctions would provide a strong incentive to local authorities to promote development. However, care must be taken to ensure that it does not undermine a competitive market for developers.

***Reform of the appeals process must provide more certainty and avoid unnecessary delays***

The remit of the Planning Inspectorate should be narrowed to aspects of an application for which permission was rejected, rather than revisiting the whole application. This would ensure that consultation is carried out at an early stage of the planning process.

#### 1.2 Funding for development

***The uniformity of the current business rate system must be retained***

The uniform business rate is valued highly by business for the certainty, predictability and uniformity it brings for forward budgeting and forecasting rates of return on new investments. Changes to the business rate system under the localism agenda must not be a stepping stone to full relocation of business rates and must not allow local authorities to increase the business tax burden.

***Legislation for tax increment financing must be introduced***

Tax increment financing (TIF), which allows local authorities to borrow against future business rates revenue, could play an important role in attracting private funding for large-scale developments. The government must move swiftly to introduce the legislation necessary for TIF to take place. TIF would provide significant capital for large scale projects in a way that a simple retention of the business rates cannot emulate.

***Growth Zones can be used to test new policies***

The Enterprise Zones (EZ) of the 1980s and 1990s met with some success, but in some cases may have displaced investment and jobs rather than generated new economic activity. However, the government should not take this to mean that the concept is flawed. Instead, it should license at the local level a series of controlled experiments, with local areas proposing freedoms that suit their particular needs and aligned to national strategic needs. This would encourage policy innovation, incubating ideas that can be used on national stage, or that could be rejected if they failed to stimulate the desired activity.

***More autonomy for commercial and industrial parks***

Industrial parks should be given more authority to run their own affairs in such a way as to maximise growth. In areas that do not have residential premises – such as industrial parks – local authorities should cede decisions over issues such as planning, energy generation and skills development. This would allow firms to formulate action plans that suit their needs –through quicker decisions on micro-generation, or Group Training Associations for instance – in a more effective and efficient manner.

***Public funding for infrastructure must be transparent and proportionate***

The notice that the community infrastructure levy (CIL) will be retained is welcome but there are significant concerns that the relationship between section 106 agreements and the CIL will not be adequately clarified, and that many businesses will be double charged for infrastructure. The government must clarify the situation so that such double charging does not occur.

## **The planning system and construction**

The UK construction industry enables the creation of all major infrastructure, essential for long term competitiveness. In addition, due to the sectors' long and diverse supply chain – and low dependence on imports - it directly generates significant additional income. As the sector represents over 8.7% of UK GVA<sup>1</sup>, expansion in construction output also constitutes a major driver of growth and job creation.

However, planning regulations add significant cost to infrastructure delivery and deter investment. Early constraints imposed by the existing planning and consultation process can lead to lost opportunities for innovation on the part of contractors. This increases long term costs and can reduce investment.

Removing planning barriers to development will enable the sector to deliver a greater quantity of assets in reduced time, and at reduced cost. The removal of planning barriers will also encourage increased private sector capital investment.

### **A national house builder**

*This firm has operations in much of England and Scotland. It is one of the top ten house builders by volume and has a substantial amount of experience in the submission of and prosecution of planning applications. In 2010 it constructed almost 2,000 homes.*

*For the firm, the planning system has become more complex and time consuming over the past decade. Applications should be determined in eight to 16 weeks in the company's experience the period is often significantly longer and this in turn leads to delays in implementing developments.*

*For example, in January 2010, the company submitted an outline planning application for the erection of up to 508 homes. Prior to the submission of the application there had been extensive discussions with the Local Planning Authority (LPA) and other statutory consultees such as the Highways Agency (HA) to agree as many matters as possible before submission, in order to speed up the decision making process.*

*The company also held a public exhibition in December 2009. While the application was reported to the LPA in May 2010, the recommendation was for deferral due to a holding objection from the HA. This objection was eventually resolved and the application reported to the LPA in mid October 2010 with a recommendation for approval. The six-month gap between deferral and the recommendation was delayed, taking more than twice as long as it should have done.*

*The reasons for this delay are concerning. The company first consulted the HA in summer 2009 and its consultants prepared a wide range of surveys to demonstrate the application would not adversely impact on the strategic road network around the site. However, when the application was submitted, due to a change in personnel, the HA would not agree with the report's conclusions but sought more and more survey work. During this period it appointed several consultant companies to act on its behalf.*

*The firm's consultants were not allowed to have discussions directly with the HA consultants but had to discuss matters with the HA. Four months after the first committee the HA agreed to remove its holding objection without condition and without the need to undertake any improvements to the highway network – a position first agreed with them in summer 2009. This led to a six month delay in approving the application and thus a six month delay in implementing the development.*

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<sup>1</sup> House of Commons Business and Enterprise Committee "Construction Matters" 2008



## **2. TRADE AND INWARD INVESTMENT**

With demand from domestic consumption constrained, net exports and inward investment are the key sustainable sources of growth available to the UK economy. The UK must develop a strategic approach to developing its export industries, showing itself to be: exciting, dynamic and competitive; and ready to shape the 21<sup>st</sup> century not just watch from the sidelines. In order to do this, the government must: identify its key priorities; support British companies as they increase their presence in existing markets, while at the same time breaking into new ones; encourage the development of innovative products and services that will appeal to global consumers; protect outward foreign investment; and attract inward investment.

### **2.1 The role of direct government support**

#### ***Additional ECGD offering must reach its SME client base***

The CBI welcomes the recently announced additional support to be available through ECGD, but the critical thing now is for the government to work with banks to ensure these facilities are ready for roll-out and to ensure its marketing reaches small firms with the potential to step up their export performance.

#### ***UKTI must continue to expand beyond its core SME customer base***

Many mid-caps do not need the classic UKTI offerings; instead, they need up-to-the-minute and informed economic and political intelligence. To deliver this, UKTI must ensure it is thoroughly integrated into the broader staff capabilities of Britain's Embassies and consulates around the world. Excellent communication between UKTI and 'pure' Foreign Office staff on the ground will deliver a valuable intelligence product for UKTI clients.

#### ***'Success' – and targets used to measure it – should be considered in the broadest possible sense***

An excessive focus on simplistic quantitative targets has led to a disincentive for UKTI staff to pursue more proactive work. When measuring their return on investment, UKTI needs to use more sophisticated metrics than headline 'new entrant to market' numbers. Quantitative targets should be complemented with qualitative targets in terms of information and outcomes in terms of business won. Similarly, UKTI's focus on meeting targets for chargeable services should be qualified by other metrics.

#### ***The Passport to Export Scheme / Gateway to Global Growth should be expanded***

The scheme is much valued by SMEs; it has a very narrow definition of first time exporters. Companies with some export experience but which are looking to break into new markets or sectors must also be considered.

#### ***UKTI should build strong sectoral links***

UKTI should build better relationships with key trade associations in support of its shift to a more sectoral approach. There is also room for an improvement in the relationship between business sector advisory groups and staff covering priority markets, to ensure there is no duplication of effort between regional/national or sectoral/market levels.

#### ***UKTI should focus on winning more inward investment***

UKTI needs to identify and establish in-depth relationships with the highest value FDI prospects, both from within the UK and developed economies and from emerging economies. BRIC countries currently account for less than 6 per cent of all global FDI; their increasing economic power makes it important to establish the UK's credentials as a prime destination for investment.

#### ***UKTI offerings should be carefully managed post-RDAs***

The 'classic' UKTI offerings of basic market information, limited funding support, and consultancy services focused on early stage exporting skills, are of most use to SMEs – and are valued by this group of companies. They must be continued, and in particular UKTI must be careful to ensure that in the shift from RDAs to LEPs, companies do not lose their link to export expertise. There is currently a considerable lack of clarity about how SMEs will access trade support services going forward, and what can be done to ensure services are co-ordinated in overseas marketplaces.

## 2.2 Trade agreements and investment treaties

### ***Free Trade Agreements must play to UK strengths***

The UK must set the direction of EU trade policy not simply follow the crowd in negotiations. The government should play to the UK's strengths by pushing for comprehensive liberalisation across all sectors in trade agreements. In particular, it must fight to ensure that liberalisation of the services sector, which make up over 40% of the UK's exports, is at least as ambitious as goods liberalisation. It should also, in consultation with business, draw up a priority list of fast-growing emerging economies, based on the opportunities and challenges each one presents to UK businesses, particularly in high-growth, high-value sectors, and ensure that FTAs are put in place.

### ***Priority must be given to protecting UK investors as a matter of urgency***

With investment protection now an EU competency it is imperative that the government pushes for a grandfathering provision for the UK's existing Bilateral Trade Treaties (BITs), allowing them to continue until the EU negotiates a new BIT that offers at least the same level of protection. Existing treaties should not be abolished on the basis of incompatibility with political goals or policy areas such as labour and environment.

### **Trade & Investment for healthcare and life sciences**

The Life Sciences sector represents around 6.5% of total UK manufacturing value added and 3.6% of total UK manufacturing employment. Productivity – measured in terms of gross value added per employee – increased by some 77% between 1998 and 2007.<sup>2</sup> The industry is characterised by high levels of innovation, with the pharmaceutical and biotechnology sector accounting for around 25% of the UK's total business R&D expenditure.

The UK is a major exporter of Life Sciences products and technologies. In 2008, UK exports of pharmaceuticals totalled around £18 billion while UK exports of medical technologies amounted to around £5.4 billion. By securing ambitious trade agreements the government can compound the UK's comparative advantage in this sector.

#### **A global pharmaceutical firm**

*We believe that a strong trade policy will be a key to supporting the competitiveness of British industry in a globalised economy. Addressing trends towards protectionism and opening up trade will require a range of actions – harmonisation of regulatory and technical frameworks; effective protection and enforcement of intellectual property rights; opening up of foreign investment climates; removal of tariff barriers; and removing local manufacturing requirements are all important elements in creating a level playing field for the pharmaceutical industry.*

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<sup>2</sup> UKTI Website

### 3. COMPETITION

Competition is an essential driver of growth in a market economy. Competitive pressures focus firms' efforts on meeting consumer demands and encourage companies to bear down on costs and invest in innovation. A robust, efficient and effective competition regime is essential for business restructuring as the recovery takes hold, and to promoting the innovation and dynamic markets that will support long-term growth. The critical issue for business is to ensure that the length of time taken to get decisions from the competition authorities is consistent with business life cycles.

The benefits of competition must in particular be harnessed in the delivery of public services. At present the state is too often a monolithic provider standing in the way of the re-engineering and innovation that is necessary to deliver improved outcomes in light of the fiscal retrenchment. Transforming delivery of public services to focus on achievement of outcomes will ensure spending becomes more proactive and boosts new growth through modernisation and better quality public services.

#### 3.1 Competition and monopoly regulation

##### ***A single competition body should be introduced***

Conducting reviews and investigations in separate bodies is inefficient and impairing confidence in the system. Moving to a single competition body, with clear timetables for decisions, would dramatically speed up the competition regime by eradicating duplication. This would reduce the burden and costs to business and increase business confidence in the system.

##### ***The mergers and acquisitions review process must offer greater certainty***

The present test for reviewing mergers and acquisitions can cause uncertainty to firms as to whether their case will be reviewed or not. The system can result in small mergers being reviewed where the costs of the review itself exceed the turnover of the company being acquired. As merger and acquisition activity picks up the government should look to address this lack of certainty so that companies can easily work out whether their merger could be subject to review. In the meantime the share of supply test should be amended by Statutory Instrument to exempt the acquisition of a company whose turnover is less than £5m. This de-regulatory measure will help small companies to restructure coming out of the downturn.

##### ***Market investigations should be reformed and "super complaints" abolished***

The existing structure is over-engineered and cumbersome and results in costs to businesses which are disproportionate to the gains to competition. A "super complaint", followed by an OFT market study and then a Competition Commission market investigation, can take 10 years.

"Super complaints" should be abolished, as they put certain bodies in the position of privileged complainants and quasi-enforcers, and the competition agency be allowed to set its own agenda and priorities for enforcement, based on intelligence gained from a range of sources. Market investigations place a significant burden on business, and have a negative effect on investment and growth if entered into lightly. They should be limited to clear failures of competition only, and be subject to a strict 18-month statutory timetable.

##### ***The appeals system must be replaced***

In the current 'administrative' regime, competition authorities act as investigators, prosecutors and adjudicators, with judicial review providing the only means of appeal. There are clear advantages in moving to a prosecutorial system, such as those in the US, Canada and Australia. Competition authorities would be required to put their case for remedies against a company to a court, and the company would also have its chance to put its argument, giving business much greater confidence that a well-evidenced case had been put together.

#### 3.2 Competition in public procurement

##### ***The government must ensure that non-state provision is used throughout the public sector***

Despite good examples such as the DWP's Work Programme, the MoJ's Rehabilitation Revolution and the NHS's Any Willing Provider model, the failure to recognise the potential of non-state provision is widespread in the public sector. The government should kick-start an opening of

markets throughout the public sector, by setting minimum proportions for the share of services that must be delivered by independent providers.

***Transparency requirements should apply equally to all providers of public services***

Greater transparency in public service contracts would increase the performance and efficiency of all providers (private and public), engender behavioural change in procurement officers, increase value for money and thus enhance outcomes for service users. The government must extend the principle of transparency to in-house public sector providers, so that the value of their services can be assessed against the same criteria as other providers, and develop a 'right to bid' approach where external providers can challenge existing ones.

***Government must remove public providers' exemption from VAT and pension obligations***

Different VAT and pension obligations currently stand in the way of a level playing field for public, private and social providers. Many public sector bodies are exempt from paying VAT but private and social sector organisations are not. The government must eliminate these unfair advantages.

***Capital depreciation costs need to be applied equally to providers of all sectors***

Private providers are contractually obliged to include depreciation in their cost calculations and are therefore at a competitive disadvantage. The government needs to ensure that the full cost of public sector capital assets, such as school buildings, hospitals and prisons, are accounted for in unit cost comparisons between providers. The Treasury should establish guidelines for providers from all sectors to adhere to, which take into account the full cost of providing public services, including capital depreciation.

## **Competition in public services**

The UK leads the world when it comes to innovative partnerships for investment and improvement in public services. As new providers of public services from the private and social sector have competed with the public sector, citizens have exercised choice to find the services that best meet their needs and on their terms. The taxpayer has subsequently achieved better value for money and performance against outcomes. But there are still too many areas where the public sector holds a near-monopoly and the public face a 'like it or lump it' dilemma.

### **There are good examples**

*Most police forces say they want their police officers to spend more time on the streets instead of in the police station processing arrested people. Some private providers have used new custody detention officer roles to reassign warranted police officers who were previously completing tasks such as delivering food to cells, taking prisoner photographs and fingerprints. In one medium-sized force up to 53 officers (or over 100,000 hours of police officer time) returned to the frontline. But only 7 out of 43 in England and Wales have used competitive processes to reform their custody procedures in this way.*

### **Some capable organisations have to exit public service provision**

*Private sector providers have developed real expertise in delivering value for money support services to the NHS, such as in patient transportation. But public sector staff regulations can force even the most experienced provider to leave a market or decide not to enter it altogether. One provider with a proven track record reached the 'preferred bidder' stage of tender, but when the NHS trust client asked it to take on unlimited pension liability, even though it had been agreed that all existing NHS staff would be redeployed, the company felt obliged to withdraw. The trust could not understand the impact such a decision would have on a non-public provider, even one with which it had a strong relationship. Smaller providers do not usually get that far.*

### **Promising partnerships are still a rarity**

*Providers from the public, private and social sectors often bring their own innovations, ethos, ways of working and approaches to problems, with differing strengths and weaknesses. In many cases, public services will need to draw on all three in order to be integrated, public-centric, efficient and effective. NHS pathology is one leading-edge example, delivering year-on-year savings, significant investment through automation and staff skills, reconfiguration of facilities, improving health outcomes and building a world-class capability.*

### **Competition between providers can enhance focus on tackling stubborn problems**

*The delivery of employment services by independent providers demonstrates the real benefits that come from greater competition and a plurality of providers. Competition in this sector has meant providers have been compelled to innovate, constantly developing new approaches to help people back into work and keep them there (e.g. the use of personal advisers) in a way that traditional, monopoly Job Centre services are unable to do.*

### **The benefits of competition are impaired if there is not a level playing field**

*A leading private sector prisons provider has found it hard to compete against the public sector because it is compelled to factor depreciation costs into its bid, whereas public sector providers do not. Most data therefore shows that the cost of supporting a prisoner in a private prison is typically higher than in the public sector, but this is actually misleading - when a fair comparison is made, private prisons typically cost less.*

## 4. REGULATION

Ill-conceived or badly-drafted regulations inflict significant costs on business, acting as a barrier to innovation, investment and employment. Disproportionate regulatory requirements are the cause of three main problems. These are:

- the direct and indirect monetary costs of compliance;
- the sheer complexity and volume of regulations means that firms dedicate significant amounts of management time to compliance, rather than to the commercial activities in which they should be employed;
- the chance of misinterpreting or misapplying regulations helps to foster an unbalanced perception of risk that deadens innovation and entrepreneurial activities.

These costs present a far greater burden for smaller firms that lack the administrative capacity to deal with them.

### ***Recent regulations continue to hamper businesses***

Upcoming changes including the agency workers directive, the default retirement age and the bribery act will all cause considerable administrative burden and increase uncertainty in the business environment. Harnessing companies' growth potential relies on removing regulatory barriers from investment and job creation not enacting new ones.

#### 4.1 Regulatory architecture

##### ***The regulatory framework needs further reform***

The BRE guide '*Reducing Regulation Made Simple: Less regulation, better regulation and regulation as a last resort*' is a welcome contribution, but the government still needs to do more to deliver real results that boost business confidence:

- The 'one-in-one-out' rule must be implemented more rigorously. There is evidence of gaming the system, with costs and benefits deliberately manipulated in order to show compliance with the principle.
- The Regulatory Policy Committee should be given greater powers to challenge the accuracy and proportionality of regulatory impact assessments. The prompt publication of their advice to the government would help to ensure that Whitehall is responsive to their comments.
- A 'Regulatory Ombudsman' should be appointed to mediate when regulations come in to jurisdictional conflict – such as when English Heritage and DDA requirements clash – to prevent businesses having to go to court simply to comply with the law.
- The metrics that firms are required to provide – such as the particulars of 'profit' – should be simplified to reduce compliance costs.
- The barriers that exist to closer co-operation between enforcement agencies and regulators should be reduced, so that they can better co-ordinate their activities and minimise the time spent by business on enforcement visits. The work practices undertaken by the Fair Employment Enforcement Board in examining the work of HMRC, EASI, the GLA and HSE should be extended across different areas of regulation.

#### 4.2 Employment law

##### ***Restore the two year unfair dismissal qualifying period***

SMEs with limited HR capacity could be protected from costly, weak claims by restoring the unfair dismissal qualifying period to two years. This would give firms more time to assess the quality and potential of a new employee and give them confidence to hire in the knowledge they will not face a claim in tribunal if it does not work out. Discrimination claims are not affected by the qualifying

period, meaning this move could be made easily without putting those who are the subject of workplace discrimination at risk of not being able to bring a claim.

### ***Government must ensure that the tribunals system does not discourage employment***

The current tribunals system imposes little or no cost on disgruntled employees, while layering costs on employers so that they are encouraged to settle to minimise their exposure; this inevitably has a negative effect on hiring decisions. The government should take immediate action to: incentivise pre-claim settlements by removing obstacles to Compromise Agreements; drive out weak and vexatious claims through pre-trial hearings charging and the use of costs; and to discourage the impression of 'City-style pay outs' by capping discrimination awards and publicising the median awards.

### ***Government must fill the void left by the abolition of the Default Retirement Age (DRA)***

To encourage a flexible approach to retirement, employers must have certainty that open dialogue with employees about their future plans will not leave them open to legal challenge. These conversations must be protected in the Age Regulations 2006 – employers should not be penalised for succession planning. The government must also spell out in the age regulations how companies can use the concept of an 'employer justified retirement age' (EJRA) that is established in the guidance recently published by BIS. It is vital that workforce planning and opportunities to promote younger workers are considered legitimate aims of introducing an EJRA, and the EJRA a proportionate means of delivering them. These changes will pave the way for the government's policy aim of increasing employment participation rates for older workers to be achieved.

### ***Skilled migration must be a priority***

From April, an annual cap of 21,700 will be placed on the number on non-EEA (European Economic Area) migrants entering the UK through Tier 1 and Tier 2 of the UK Points-Based System. However, the ability to transfer staff and hire internationally is essential to supporting the decision to invest in the UK. The government has rightly prioritised skilled workers coming to the UK with a job offer – through Tier 2 – in the design on the system. As the government continues to seek to reduce net migration, this number must be protected.

### ***References to 'quality' of work should be removed from new agency regulations***

Regulation 6.3.f of the Agency Workers Regulations 2010 requires that agency workers receive pay that is 'directly attributable to the quantity or quality of the work done by a worker'. While the 'quantity' of work is objectively quantifiable, the 'quality' of work needs a subjective assessment by the end-user that requires costly administration and a level of supervision suggestive of an employment relationship. Judging by quality would significantly reduce the flexibility of the agency workforce, by requiring users to conduct performance assessment. The government should therefore remove the reference to 'quality' from the regulation. This will reduce the costs of administering agency workers, help reduce a significant source of uncertainty for companies and ultimately help more agency workers to find work.

### ***The legal framework for industrial relations must be reformed to strike the right balance***

Workplace disputes are best resolved by discussion between employers and employees. Strikes are regrettable and should always be the last resort. Therefore, where workplace disagreements run a risk of escalating into industrial action, a fair balance between the interests of employees and trade unions on the one hand, and employers, customers and the general public on the other is needed. To that end, the CBI has proposed 11 recommendations that will help minimise the disruption caused by strikes<sup>3</sup> ensure the views of ordinary employees are heard, and curb wildcat strikes through proactive trade union actions.

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<sup>3</sup> 'Keeping the wheels turning: Modernising the legal framework of industrial relations' September 2010

Key proposals include:

- Restore firms' right to hire agency workers to cover for striking employees, and rationalise the situation whereby firms are able to hire directly to cover strikers' posts, but not indirectly. Employees have a right to withdraw their labour if the right procedures are followed, but employers have a responsibility to their supply chains, shareholders, customers and other employees to keep their businesses up and running during a period of strike action.
- When a union seeks recognition, workers should always be balloted on whether they support this. At present, if the union has more than 50% membership, automatic recognition can be awarded.
- Given the disruption caused by strikes, the bar for strike action should be raised. Strikes should only go ahead if they are supported by 40% of those balloted, as well as a simple majority of those voting. These reforms will prevent essential reforms to the public finances and private sector restructuring being hindered by industrial action that goes ahead on the basis of tiny turnouts of the affected members.

### ***TUPE regulations create a two-tier workforce***

Regulations 4 (4) and 4 (5) of the UK TUPE Regulations 2006 prevent an employer from harmonising terms and conditions of a newly acquired business or service team with its existing workforce. While changes can be made to reflect market conditions, it is not possible to have one workforce with the same terms and conditions of employment. Further gold—plating has taken place in the extension of TUPE rules to a change in service provider even when it is not considered to be “an undertaking or part of an undertaking” as defined in EU law; the government must therefore undo this undue gold-plating. The existence of such a two-tier workforce can cause significant employment relations difficulties and constrain efficiency.

### ***Reduce the 90-day consultation period for collective redundancies to 30 days***

Under Regulation 188.1.1A.a of TULRCA 1992 employers must consult with ‘appropriate representatives’ for 90 days when proposing more than 100 redundancies, in contrast to 30 days when proposing between 20 and 99 redundancies. This reduces firms’ ability to react quickly, and subjects employees to a prolonged period of uncertainty. The regulation should be removed so that consultation for redundancies involving over 20 people lasts for 30 days. Staff losing their jobs would continue to receive full notice and statutory redundancy pay.

### ***Changes to pension rules are required***

Governments have a poor record for removing poorly drafted legislation that restricts corporate activity without protecting scheme members. There are two key areas where the government can help. The first is by removing the debt liability on a group making changes within their own scheme where no members or assets leave the company (so-called Section 75 debt). This debt was meant for genuine multi-employer schemes, not corporate groups. The second is by accepting that – with many of these schemes now closed – firms will look to de-risk themselves by buying out liabilities over time. The government should foster an approach that accepts this as fact, and that it is good for growth – allowing firms to return focus to their core businesses. The regulator should see de-risking as something to be managed and properly regulated, not prevented.

## **4.3 Health and Safety**

### ***Local authority inspection should be harmonised and improved***

Many firms – especially those in consumer facing industries and many smaller firms – are not regulated by the HSE but by their local authority. This leads to a wide variety of interpretations: CBI members report that local authorities generally have a different view of comparative risk to the HSE; and firms with sites across different authorities report contradictory advice. While larger firms in this situation can benefit from dealing with one authority through the primary authority schemes, this option is not available to smaller firms. The government must harmonise risk attitudes and inspection standards of local authorities with those practiced by the HSE in the areas they regulate.



### ***Advice to firms – especially SMEs – must be proportionate***

One of the reasons larger firms find health and safety law less costly is that they can use internal expertise to decide what appropriate steps to take. Smaller firms generally use external experts who often “cover all the bases” on risk management, leaving the firm with an unwieldy and not particularly company-specific approach to risk. The government should encourage certification for consultants who sell their services to business through IOSH and other industry bodies, and this must include an injunction to ensure that risk assessments and plans for risk management are practical and relevant to each workplace, removing unnecessary work and cost for smaller business.

## **4.4 Environment, climate change and energy**

### ***Reinstate the energy efficiency incentive for companies in the CRC***

By removing the revenue recycling element of the CRC Energy Efficiency Scheme, the government has undermined its objective to change behaviour. Instead, business is now unexpectedly faced with a ‘stealth tax’ on carbon which, instead of providing impetus for energy efficiency savings, will likely be written off as another cost of doing business in the UK. To encourage action on energy efficiency, the government must reinstate revenue recycling in the CRC or, if the money cannot be found to do so, stop the scheme and provide a simplified mechanism to encourage take-up across the business community.

### ***Eliminate the Emissions Performance Standard***

The government has proposed to introduce an Emissions Performance Standard (EPS) to regulate the carbon produced by new coal-fired power stations. However, this scheme would add no carbon savings beyond those already guaranteed under existing policy, and it would add another layer of complex bureaucracy. An EPS replicates existing planning policy that any new coal stations require a Carbon Capture and Storage (CCS) demonstration, and could deter UK investment in CCS, with a consequent adverse impact on low carbon energy security. Once technically and commercially proven, CCS will effectively become the Best Available Technology for new coal power stations, and an EPS would therefore be an unnecessary additional measure.

### ***Electricity market review must not undermine energy intensive industries***

The UK’s international competitiveness is threatened by climate policies which increase energy prices above those faced by their international competitors. Without action, business may well shift production and investment overseas, resulting in job losses and higher carbon emissions globally. It is crucial that the Electricity Market Review provides the right incentives to align policy signals and investment decisions so that the UK is able to decarbonise its energy infrastructure and secure supply at competitive prices. In doing so the government must avoid placing additional competitive burdens upon energy users, especially intensive energy users. The government should provide protection, such as an exemption from the cumulative cost of all energy and climate policies for the sectors most at risk of carbon leakage.

### ***Give businesses greater certainty on pricing landfill waste***

The landfill tax escalator is the most effective mechanism the government can use to minimise the amount of waste sent to landfill, and complements existing policies on recycling and recovering energy from residual waste. In contrast, landfill bans and restrictions are blunt tools that would undermine these positive initiatives. Therefore, the government must focus on making the existing mechanisms more effective – rather than introducing further regulations – to hit EU landfill diversion targets. Businesses welcome the government’s floor price on landfill tax until 2020 and want to see greater long term certainty in pricing.

### ***Government must lead negotiations in Europe on future environmental policy development***

With almost 80% of environmental regulation under DEFRA set at European level, it is crucial that the government takes the lead in shaping the right outcomes for the UK at EU level. This means not only ensuring appropriate transposition of directives but influencing the policy debate from the beginning. In addition there should be pressure placed on other member states to implement existing directives before introducing new ones. Shaping the early thinking on a successor to the 6<sup>th</sup> Environmental Action Plan would give the government an opportunity to set the direction of EU environmental policy for the next decade.

***Given significant and existing tax pressure on the aviation sector, further hikes in APD must not take place***

The government plans to further increase the tax burden on aviation are a cause of serious concern and would have a severe impact on the competitiveness of the UK as a place to invest for airlines carrying both passengers and freight. The tax take from the APD alone has risen from £0.9 billion in 2005-06 to £1.9 billion in 2009-10, and it is projected to rise to £3.6 billion by 2015-16 on current policy. From next year, aviation will be included in the EU-Emissions Trading Scheme, highlighting the need for the cumulative costs of environmental taxation to be considered, to avoid potential distortions to competition. The proposal to introduce a per-plane tax – a policy considered and rejected by the previous government - should also be abandoned.

#### **4.5 Bribery**

***Concerns over the foreign public officials' clause***

The legislation omits the notion of corruption, dishonesty or impropriety. This means legitimate business promotional expenditure and proportionate use of corporate hospitality could fall foul of the law. Under the current primary legislation, a pharmaceutical company offering bona fide hospitality to a doctor in China – technically a state employee – while tendering for contracts there could lead to a prosecution under the Bribery Act, even if there is no corrupt intent. This section has potential consequences for sponsors of major sporting events such as the Olympic Games, and must be resolved as soon as possible. We believe the law – and at the very least the guidance – should state that there must be evidence of corrupt intent behind hospitality and promotional expenditure.

***Government must ensure that businesses located in the UK are not disadvantaged***

Firms need to be able to rely on the guidance to ensure they are compliant with the law. Greater clarity is needed in guidance in defining the 'adequate procedures' companies must go through in order to show compliance, either in the Ministry of Justice or prosecutorial guidance. In particular, businesses need a greater understanding of what actions will be deemed proportionate and reasonable, particularly around hospitality and promotional expenses, gifts, political and charitable donations and whistle-blowing procedures and employee protections.

***Certainty is needed for supply chains***

Employers are also concerned that they will be liable for the offences of firms in their supply chains – not just in their own workforce. The guidance is not clear about which entities firms' anti-bribery procedures should apply to. This is an important issue for business – and one that must be put right before implementation.

***Government must fulfil its commitment to address business concerns***

The potential for offences under the Act to lead to mandatory debarment under the EU Procurement Directive is causing firms significant concerns. This would hinder the competitiveness of UK companies. The government should issue a clear statement in guidance that if an offence relates to management procedures in a company it should not automatically lead to such debarments.

## **Regulation in the retail sector**

The retail sector plays a vital role in the UK economy. The 286,000 retail outlets – accounting for 9% of all VAT-registered businesses in the UK – took in £285billion in sales revenue in 2009. The sector accounts for 8% of total UK GDP, and employs 2.9million people (11% of the total workforce). However, with earnings trailing inflation and the recent VAT rise compounding sluggish consumer confidence, the sector would benefit from a concerted effort to remove unwarranted barriers to growth.

Regulation is a particular challenge for a sector with such diversity. Large national retailers are affected by regulation from multiple government departments and regulators, reflecting the wide span of their businesses, while the many small, independent retailers battle with the disproportionate manner in which regulations fall on their businesses.

### **A small regional retailer**

*Employment regulations make it very difficult for us to resource the business efficiently. Last summer a dispute with an employee went to a tribunal. Although our lawyer advised us that we were likely to win the case, it turned out to be cheaper to settle rather than fight the case and win. The employee faced no risk from pursuing the case, whereas it was going to cost us thousands of pounds to win – how is this a balanced system?*

### **An SME focussed on business-to-business activities**

*The disproportionate costs associated with managing and administering most aspects of employment law / H&S means there is less to invest in the business for growth. Ours is a medium size company and our contract with employment law and health and safety costs £25K per annum plus many hours of 3 employees' time.*

### **A national retailer that uses a franchise model**

*Many of our local franchises find H&S regulations particularly difficult. We look to help them from the centre as far as possible, but the lack of consistency amongst Local Authorities is astounding: what one council considers acceptable, another expressly forbids. This means that managers of these entrepreneurial businesses have to spend far too much time thinking about mitigating infinitesimal risks rather than meeting customer demand.*

### **A large national retailer**

*The landfill tax and the foresight of the escalating costs each year to 2014 have been effective in ensuring our in-store policy is always to avoid sending waste to landfill. At this stage, the introduction of bans on certain substances to landfill would undermine the efforts we are making to find greener waste treatment solutions, that at the same time can be tailored to our stores across the UK*

### **A high street chain**

*We have been working for some time on converting our business to a carbon-neutral model. The recent changes to the CRC have sadly changed the scheme from a strong incentive to us to finish the job into simply an additional financial and administrative burden.*

## 5. ACCESS TO FINANCE

Ensuring a supply of affordable and readily available finance is critical to securing a private sector recovery, enabling firms to invest, trade and create jobs. Much of the emphasis in the wake of the financial crisis was on emergency measures to provide working capital as credit flows dried up for many firms. To help support future growth, a broader emphasis is required including:

- ensuring lending is normalised, including for those parts of the economy where accessing credit is still difficult;
- ensuring that capital is available for long-term investment, including for investment in critical national infrastructure;
- undertaking reforms to make the banking system more stable, whilst ensuring the banks are in a position to support the economy through lending.

### 5.1 Improving access to finance for SMEs and mid-caps

#### ***Improving the attractiveness of the corporate bond market for issuers***

SMEs and mid caps often find the process of issuing debt more expensive and complicated than bank loans and, for private placements, covenants are often more rigid and restrictive than would be typical for bilateral bank loans. Obtaining a rating for the issued instrument adds further costs. These costs are relatively fixed and so proportionately higher for smaller issues. The process of issuing debt could be made more attractive by:

- Reducing the cost of corporate finance and placing fees. As mid cap private placements or market issues would generally not be underwritten, bank or corporate finance houses' exposures would typically be limited and government led incentives could be developed to encourage firms to reduce the costs of issuing debt. This could include allowing debt placed with third parties which meets certain criteria to be included in the calculation of industry lending targets.
- Simplifying the process of issuing debt will reduce costs. The government should engage with trade bodies and market participants to establish private placement and mid cap bond documentation standards. These standards should discourage restrictive covenants, ensuring that risk is factored into pricing and levels of due diligence rather than reducing flexibility.
- Using risk-sharing and guarantees to support banks which provide suitable products. There are often costs relating to issuing debt which are not transparent in bank lending, for example the costs of interest rate or currency hedging. The government could reduce these costs for banks which provide risk management products that are directly linked to bond issuance, reducing the regulatory capital cost to banks and investment firms of providing these products.
- Educating firms about the possibilities of bond issuance. A significant barrier to issuing debt for many companies may be one of experience. The government should support industry-led educational efforts targeted at mid caps, including advice provided by banks.

#### ***Improve the attractiveness of corporate bonds for investors***

Investors are often reluctant to invest in SME or mid cap debt because the lack of an existing developed market means that important market facilities are not in place for example brokers willing to commit capital or develop research. Investors themselves do not have resources in place to undertake the levels of due diligence needed to make investment in the larger number of small issues worthwhile. They are often unwilling to accept the additional risks associated with the limited liquidity in the market. SME and mid cap bonds could be made more attractive for investors by:

- Reducing the risk of investing in mid cap debt. The government could provide guarantees or credit enhancements to portfolios of securitised debt. This could be provided through the 'Big Society Bank'.

- Encouraging investment vehicles for mid cap corporate bonds, by including collective investment schemes and securitisations which will diversify the portfolio. Although corporate bond funds are already popular with investors, few specifically target mid cap firms. Investors of this kind are important to the growth of the market and they could be supported with short term tax incentives, similar to the approach used for VCTs.
- Government support for investors who wish to invest in small or mid cap firm debt by making coupons on private placements and corporate bonds that meet certain criteria tax deductible or exempt.
- Broadening the base of investors by supporting market led solutions to drive the growth of retail investment in corporate bonds, for example through support of the London Stock Exchange's Order book for Retail Bonds ("ORB") and the development of mid cap bond indices.

### ***The Enterprise Finance Guarantee should be further developed***

Some smaller companies continue to find borrowing more difficult or costly, partly as a result of proportionately higher transaction costs for lenders or greater perceived credit risks and because of greater requirements for security. Providing long-term certainty for small businesses by committing to maintain and develop the enterprise finance guarantee (EFG), as well as continuing with the 'time to pay' scheme to allow viable businesses flexibility with working capital will support financing for this important section of the economy.

### ***The EFG should be available to more IP-intensive businesses***

Companies whose assets are predominantly in intellectual property, and which do not have traditional physical assets on the balance sheet to secure lending against, have found the lending environment particularly constrained. However, many medium-sized IP-intensive businesses are not eligible for the EFG. The government should therefore develop and widen access to the EFG. In particular, the current EFG upper lending limit of £1m is not flexible enough. Evidence suggests that there would be demand and take up by a relatively small, but still significant, number of companies were the EFG to be extended to £2m and the turnover threshold raised £25m to £50m.

### ***The EIS and VCTs can be improved to catalyse new investment***

Larger SMEs face a long-standing gap in the availability of long-term equity growth capital for firms requiring between £2m and £10m. The government can help to address this by improving the Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCTs) to catalyse new investment by entrepreneurs, and by following through on the Rowlands Review. In addition the cost of raising equity should be made tax-deductible.

## **5.2 Capital for long-term investment**

### ***The Green Investment Bank must be effective in reallocating risk***

The scale of investment needed to replace our aging energy infrastructure and implement energy efficiency measures is too great to be accommodated on the balance sheets of the utilities, and capital is not flowing from the investment community due to the perceived risks associated with low-carbon investments. The Green Investment Bank (GIB), while not a silver bullet, will play a vital role in reallocating some of those risks, thus unlocking private capital – particularly from institutional investors, who hold substantial capital reserves and have an appetite for alternative, long-term investments - and lower the overall cost of financing our low-carbon infrastructure. But in order to be effective, the GIB must be set up under statute, with the powers to leverage up its capital through the issuance of government guaranteed bonds.

## **Access to finance and creative industries**

The creative industries are a key pillar of the UK's economy. In 2007, the industries contributed 6.2% of GVA, £57bn to GDP and employed over two million people. Exports were £16.6bn in 2007, representing 4.5% of total exports of goods and services.

The UK has the largest creative sector in Europe, one of the world's largest music industries and one of its most advanced digital TV and radio markets. A potential growth rate of 4% a year in real terms from 2008-2013 has been predicted, given the right business conditions. This would take the GDP contribution to £85bn by 2013, compared with £57bn in 2007. It is also estimated that a further 150,000 jobs could be created by 2013, either directly in creative industries or indirectly in related industries. However, to achieve this level of growth, access to finance is essential.

Businesses in the creative sector face both cyclical and structural challenges to accessing finance. Structural challenges relate to the fact that creative firms are often SMEs and have unpredictable sources of revenue and intangible, intellectual property-based assets. The result is that potential investors tend to view the industry as high-risk. If the UK is to remain a significant global player in the creative industries this is a challenge that we need to and can overcome.

The government can help by making sure that there is a level playing field for creative firms in accessing support via the existing interventions that are available. Creative firms often have difficulty plugging into the Enterprise Finance Guarantee, Enterprise Investment Scheme and Venture Capital Trusts. The government, creative firms and investors can all help make sure that the way those schemes are run does not inadvertently disadvantage creative sectors. The government could also help by ensuring that creative firms can access the R&D tax credit, without any hidden obstacles; for example restrictions on minimum R&D spend.

The government and industry should also work together to explore the scope for the use of public funding to de-risk investments in the sector, where several good examples (e.g. Creative Capital Fund and North East Creative Content Fund) have already proved the concept. Accessing finance is one of the main obstacles to growth in this sector but through strategic reforms, and an improved dialogue between creative firms on the demand side and investors on the finance side, we should be able to unlock significant potential for growth.

## 6. CORPORATE GOVERNANCE

The objective for corporate governance should be to ensure that the framework for investors and companies is consistent with promoting UK competitiveness and long-term economic growth. The big picture backdrop is a need for significant capital investment to drive forward private sector growth and employment. So it is important that the corporate governance in the UK is attractive to all forms of investment, both domestic and international.

Company ownership has a significant influence over issues such as the location of research & development, management of brands and intellectual property. It also has significant network effects, with business and professional services activity likely to cluster around the decision-making centre, and a substantial influence over where companies pay their corporate taxes. All of these issues have a direct bearing on the UK's future economic prospects. It is important to note however, that the UK's corporate governance is already well-regarded internationally, and there is a danger of giving up this advantage if the wrong reforms are made. There are therefore a number of significant health warnings to consider in assessing any reforms to corporate governance and company ownership:

- first, the critical test for ownership must remain an economic rather than a political issue;
- second, it is the underlying business environment that ultimately makes a difference to the ownership and investment location decisions of global businesses;
- third, the UK should remain fiercely committed to open markets and be careful not to indulge in protectionism.

### 6.1 Reforming corporate governance

#### ***Regulatory and tax changes should promote and reward long-term equity ownership***

The best way of promoting a long-term approach to company ownership, and preventing takeovers being driven by investors with only short-term time horizons, is to promote and reward long-term equity ownership. The government should explore various regulatory and tax changes that would provide more of an incentive, or at least remove some current disincentives, for long-term equity ownership. The review should cover revision to accounting and solvency rules that currently discourage equity ownership at points in the economic cycle. In its forthcoming 'Corporate Tax Roadmap' the government should look at how to ensure a level playing field for equity ownership and reward long-term ownership of shares.

#### ***Take steps to develop relationships between boards and investors***

Strong and high quality engagement between boards and shareholders is an important part of the equation in promoting a long-term approach to company ownership. The "Investor Stewardship Code" is designed to promote better shareholder engagement with firms, and should be an important tool in delivering this objective. The government must ensure that the new Code will reach out to foreign investors and encourage them to be active and engaged investors.

#### ***There should be transparency and certainty around takeover rules***

Greater transparency and certainty around takeovers and bid situations would be welcome, but changes to the takeover rules must be approached cautiously if M&A activity is not to be discouraged. Measures here include: tightening the 'put up or shut up' regime to reduce the period of uncertainty for firms in a potential bid situation; ensuring that advisory fees are structured so that they do not bias the outcome of bids; and introducing greater 'truth in takeovers' to ensure sufficient disclosure and accountability around future intentions for the acquired business.

#### ***Greater clarity over the national security test would provide certainty***

Takeover and merger situations should be judged on economic factors in competition tests. There has been much talk of broadening the 'public interest' so that a broader range of factors other than competition can be considered by regulators when takeovers are proposed. This and any other politicisation of ownership decisions must be strongly resisted. However, greater clarity over where the *existing* national security test might be applied could be useful, for example, in energy, communications and other critical infrastructure.