



Unelected Oligarchy: First Update

David Beetham, November 2011

Much has happened since the paper *Unelected Oligarchy: Corporate and Financial Dominance in Britain's Democracy* was written in June 2011.¹ This update will provide a summary of developments since then, organised under the themes of the paper. As always, it is important to set the context, and three issues that have become paramount in this latest period are worth examining briefly here by way of introduction:

- The sovereign debt crisis in Europe
- The erosion of governmental legitimacy
- The rise of a global protest movement

The sovereign debt crisis

Much is made of the past 'profligacy' of governments across Europe, especially, but not only, in the south. Yet sovereign debts that were sustainable in normal times have become critical due to the cost of the taxpayers' bailout of the banks in 2007-8 and the recession brought on by the financial crisis. At the same time the interest rates on government borrowing and the austerity programmes demanded by the financial markets have combined to make it virtually impossible for some governments to meet their debt repayments. The consequent spectre of sovereign default is once more requiring European taxpayers to shore up their banks, whose loans are now in jeopardy. If one asks why the default of a small country like Greece, representing only two per cent of the EU's GDP, constitutes such a threat, the answer lies not only with the banks which have purchased its bonds, or the fear of contagion to larger countries such as Italy. There is an inverted pyramid of international speculation and derivatives trading riding on a formal Greek default, and, as with the collapse of Lehman's in 2008, no one knows where or how wide the fallout would extend.

The erosion of governmental legitimacy

Since 2007-8 the financial sector has been living with a collapse of its legitimacy, as the public justifications for its structures, activities and rewards have been proved worthless.

¹ D. Beetham (2011) [*Unelected Oligarchy: Corporate and Financial Dominance in Britain's Democracy*](#), Liverpool: Democratic Audit.

Far from being self-regulating, the free market has shown itself prone to system-wide failure. Far from banking activities serving an essential public interest, many of them have proved to be not merely 'socially useless',² but economically damaging. And the claim of bankers to possess an esoteric knowledge and unique skills justifying their huge rewards has been punctured by the revelation that even they did not fully understand many of the complex instruments in which they were trading. Yet this collapse of legitimacy has not been accompanied by any significant loss of economic and political power, diminution of rewards or change in the regulatory framework. Instead we have seen the costs of the banking crisis successfully transferred onto governments, including the opprobrium of driving through unprecedented austerity programmes without popular endorsement.

Whereas bankers and financial traders can hide behind the impersonality of 'the market', governments cannot evade public responsibility or accountability for their actions, even if these are dictated from elsewhere. Many have simply crumbled under the pressure, whether through outright collapse, as in Iceland, electoral wipe-out, as in Ireland, or public humiliation and enforced national coalition or technocratic rule, as in Greece and now Italy. What began as a financial crisis has now become a crisis of democratic governance and popular representation, more acute in some countries than others, and only temporarily alleviated by change in party and personnel at the top.

The rise of a global protest movement

What began as country-specific protests against government cuts, collapsing living standards and lack of jobs has now developed into an international movement of protest against a whole system of political economy, which generates huge inequalities and renders governments more responsive to corporate and financial interests than to their own electorates. How the tent camp movement will develop and what effect it will have on wider public opinion is too early to say. As regards the UK, it is significant that the institution to come under the most intense pressure from the occupation of public space has been St. Paul's Cathedral and the wider Anglican church, not the financiers or the City of London Corporation. As this update shows, business for the latter continues very much as usual, albeit with some limited prospect of reform on the very distant horizon.

² As the chairman of the Financial Services Authority, Jonathan Adair Turner, conceded in an interview with Prospect magazine in August 2009. See J. Adair Turner (2009) '[How to tame global finance](#)', *Prospect magazine*, 27 August.

Updates

1. Finance

The final report of the Independent Commission on Banking (or Vickers report), published on 12 September, recommended that British banks should separate their retail and investment operations by ring-fencing the former. A higher level of equity capital would be required to support these retail activities, with an implicit guarantee of government support in the event of difficulty. George Osborne has said he will introduce legislation in line with the Commission's recommendations. However, it will not take effect until as late as 2019. And the recent experience of the sovereign debt crisis suggests that no government would allow a major investment bank or banking arm to fail, for fear of the knock on effects on the wider financial system. The bankers for their part have complained that the new capital requirements will put British banks at a disadvantage in comparison with their international competitors, and will reduce further their capacity to lend to small and medium size businesses, or SMEs.³

Concern continues to be expressed about the difficulty experienced by SMEs to get bank loans, or about the terms on which they are offered. The so-called 'Project Merlin' agreed between Osborne and the five largest UK banks in February committed the banks to specific targets for lending, and linked their executives' pay to the achievement of these targets, though without any enforcement mechanism. Figures for their lending since are disputed (£100bn according to the banks, £53bn according to the Bank of England). In August Sir Mervyn King reported that 'the amount of lending by the banking system to non-financial companies has been falling for some while...and it's particularly problematic for small companies.'⁴ And in an exchange with the Commons Treasury select committee on 25 October he implied that the state-owned banks should be forced to lend more to small businesses to help revive the economy.⁵

Research published by Incomes Data Services on 26 October showed that the FTSE100 directors (including the major banks) had seen their total earnings increase by an average of 49 per cent each in the last financial year, to an average of £2,697,664 per annum.⁶ This figure contrasts with an average pay award for private sector workers of 2.6 per cent, half the current level of inflation. The EU Commissioner for financial services recently proposed to introduce tough new limits on bankers' pay and bonuses across the EU, which the City of London reportedly fears would result in 'an exodus of talent to Asia and America'.⁷

³ Independent Commission on Banking (2011) [Final Report](#), London: ICB.

⁴ Bank of England (2011) [Quarterly Inflation Report Q&A, 10 August 2011](#), London: Bank of England.

⁵ J. Treanor (2011) '[Banks should get incentives to lend to small businesses, says Mervyn King](#)', *Guardian*, 25 October.

⁶ J. Treanor (2011) '[FTSE 100 directors' earnings rose by almost half last year](#)', *Guardian*, 26 October.

⁷ O. Wright (2011) '[EU: We'll make UK cut bank bonuses](#)', *Independent*, 5 November.

The idea of a 'Tobin' tax on financial transactions, compelling traders to contribute to the public coffers and to international aid from their trading activities, is strongly backed for the EU by Germany, France and other countries. It has recently been endorsed by figures as diverse as Bill Gates and the Archbishop of Canterbury. David Cameron, while claiming to support the idea 'in principle', will only agree to it if it is implemented at a global level, something very unlikely given the opposition from the US and Canada. The City of London is strongly opposed on the grounds that it would reduce the UK's competitiveness in relation to financial centres outside the EU.⁸

A survey of financial service professionals carried out for the St. Paul's Institute to mark the 25th anniversary of the 'Big Bang' showed that:

- a majority believe City professionals are paid too much and teachers too little;
- 75 per cent agree that the gap between rich and poor is too great;
- 51 per cent think deregulation has resulted in less ethical behaviour;
- for 64 per cent salary and bonuses are the most important motivation for working in the financial sector.⁹

Publication of the survey results was delayed until 7 November, after the stand-off between St. Paul's and the tent protesters had come to an end.

2. Tax avoidance

Research published by ActionAid on 11 October showed that 98 of the 100 FTSE companies use overseas tax havens for roughly a quarter of their subsidiary businesses. Among these the large UK banks (Barclays, HSBC, Lloyds and RBS) have a total of 1,695 companies registered in tax havens, with Barclays having 174 registered in the Cayman Islands alone.¹⁰

The 2011 Financial Secrecy Index published by the Tax Justice Network on 3 October, while showing the UK itself as one of the most open jurisdictions, gives it the highest secrecy rating if the British Crown Dependencies and British Overseas Territories are included with it.¹¹ The justification for including these ten ultra-secretive jurisdictions with the UK is that they serve as a network feeding financial business into the City of London, comprising a third of the global market in offshore financial services. 'Through capturing offshore business from countries around the world,' TJN comments, 'this British network of secrecy

⁸ See, for instance, G. Parker and B. Masters (2011) '[Cameron pours cold water on Tobin tax](#)', *Financial Times*, 2 November.

⁹ St. Paul's Institute (2011) [Value and Values: Perceptions of Ethics in the City Today](#), London: St. Paul's Institute.

¹⁰ ActionAid (2011) [Addicted to tax havens: The secret life of the FTSE 100](#), London: ActionAid.

¹¹ Tax Justice Network (2011) [Financial Secrecy Index](#), Brussels: Tax Justice Network.

jurisdictions has been, since the era of globalisation began in the 1970s, among the most important reasons for the reach and power of the City of London.¹²

A report by the Commons Public Accounts Committee on Private Finance Initiative (or PFI) projects, released on 1 September, showed that City investors had made bumper profits by buying up PFI contracts for schools and hospitals, and taking the profits offshore to avoid tax. The Committee identified 91 projects held in overseas tax havens, including 33 owned by HSBC Infrastructure based in Guernsey. Speaking on the publication of the report, the Committee Chair, Margaret Hodge, said: 'The Treasury assumes tax revenues when assessing value for money of a PFI project, yet does not monitor whether taxes are paid.....In our evidence we found that tax revenue is being lost through the use of off-shore arrangements by PFI investors. The Treasury should ensure that this is taken into account in future assessments of PFI against conventional procurement.'¹³

Another meeting of the Public Accounts Committee on 12 October learnt that, following an earlier notorious deal between HM Revenue and Customs and Vodafone, Goldman Sachs had been let off £10m in interest payments on a failed scam to avoid paying national insurance on its bonuses by 'seconding' its employees to the British Virgin Islands.¹⁴ Another HMRC move strongly criticised by the Tax Justice Network was a deal cut with Swiss bankers whereby they agreed to pay over an arbitrary sum to cover tax unpaid by UK citizens, in return for anonymity for their clients.¹⁵

3. Lobbying and 'revolving doors'

The disclosure that Adam Werritty was using his position as travelling companion and confidant of Liam Fox to facilitate access to the Defence Secretary for the clients of lobbying companies has thrust the lobbying industry once more into the public spotlight. The fact that clients of lobbying firms pay large sums to ensure them access to ministers and senior civil servants is worrying from a democratic point of view on several counts. It means that access to public decision makers can in effect be bought. It encourages the 'revolving door' between ministers and officials on one side and business and lobbying firms on the other, with inside knowledge and contacts rated at a premium. And lobbying activities remain shrouded in secrecy. In response to the Werritty affair David Cameron has promised legislation in the next session of Parliament to create a statutory register of lobbyists, though they in turn are lobbying hard to have the information it will contain kept to a minimum. In the meantime information on lobbying can be obtained indirectly from a

¹² Ibid.

¹³ Public Accounts Committee (2011) '[Committee publishes report on Private finance initiative](#)', 1 September.

¹⁴ See Public Accounts Committee (2011), [HM Revenues and Customs Accounts 2010-11, 12 October](#), HC-1531i, evidence; P. Inman (2011) '[Revenue chief accused of misleading MPs on Goldman Sachs deal](#)', *Guardian*, 12 October.

¹⁵ Tax Justice Network (2011) [The UK-Swiss tax agreement: doomed to fail](#), Brussels: Tax Justice Network.

variety of sources: the websites of lobbying organisations; the quarterly published departmental records of ministerial meetings with interest groups; the register of outside interests of parliamentarians and their staffs (see below).

A report on 25 leading lobbying organisations by the *Independent*, published on 22 October, revealed a total of 61 former ministers, MPs, political aides and advisers, as well as a few relatives of these, on their combined payrolls. Their clients include most of the major UK corporations, as well as many US ones.¹⁶

Using the records of meetings between ministers and interest groups published by departments between May 2010 and March 2011, researchers from the *Guardian's* Data Blog reported their breakdown as follows:

- with corporate representatives, 1537
- with trade bodies, think tanks and other interest groups, 1409
- with charities, 833
- with trade union representatives, 133¹⁷

These figures exclude several hundred round table meetings where numerous companies were represented. It should also be noted that many think tanks promote a free market, pro-business agenda, and some are registered charities, so the lines between categories are blurred.

Another report by the *Guardian's* researchers, published on 9 November, found that 125 pass holders in the House of Lords were being paid by outside organisations to promote their interests. Organisations represented included BP, defence contractors, the Countryside Alliance, evangelical Christian groups and many others.¹⁸

Although the number of ex-ministers transferring to private sector directorships has sharply declined this year, there remains a steady trickle of former civil servants, ambassadors and military personnel into the private sector, typically in the City and with defence contractors. A full breakdown of the latest figures from the Advisory Committee on Business Appointments will be given in a later update. A notable transfer in the other direction has been Stephen Green, former CEO and Executive Chairman of HSBC, who was ennobled and appointed trade minister from January this year. He has just been given a further job at the Treasury, advising George Osborne on financial services and banking issues. His original

¹⁶ J. Cusick and C. Milmo (2011) '[The shady world of lobbying](#)', *Independent*, 22 October.

¹⁷ Guardian Data Blog (2011), '[Links between government and business: full data](#)', 16 October.

¹⁸ Guardian Data Blog (2011) '[Which lobbyists do members of the House of Lords favour?](#)', 8 November.

appointment was widely seen as giving the banking industry a powerful voice at the heart of government.¹⁹

A further recent paper by Deniz Igan and Prachi Mishra of the IMF on lobbying in Washington prior to the 2008 financial crisis found that ‘lobbying expenditures by the US financial industry were directly associated with how legislators voted on key bills in the years before the crisis – and that bills proposing regulation that the industry considered unfavourable were far less likely to pass than bills proposing financial deregulation.’²⁰ This is important for refuting the claim that money and access do not mean influence. It is relevant to the UK, not only as a parallel example from a much more transparent lobbying system, but because regulatory standards in the US are repeatedly used by UK banks as an argument for resisting more stringent standards here and in the EU.

¹⁹ See, for instance, G. Parker, P. Jenkins and S. Goff (2010) ‘[Green swaps board power for political clout](#)’, *Financial Times*, 7 September.

²⁰ D. Igan and P. Mishra (2011), ‘[Making Friends](#)’, *Finance and Development*, 48 (2), pp. 27-29.

ABOUT DEMOCRATIC AUDIT

Democratic Audit is an independent research organisation, established as a not-for-profit company, and based at the University of Liverpool. Our core objective is to advance education, and to undertake and promote research into, the quality and effectiveness of UK democracy. We are grant funded by the Joseph Rowntree Charitable Trust to conduct research into the quality of democracy in the UK and are currently conducting the fourth full Audit of UK democracy (the previous three Audits were published in 1996, 1999 and 2002). We also monitor democracy and freedom in Britain through a series of democracy assessments, reports and commissions, and through evidence to Parliament and official bodies. The Director of Democratic Audit is Dr Stuart Wilks-Heeg, who is also a Senior Lecturer in Social Policy at the University of Liverpool.

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