Government Intervention 2.4

Economic Systems

- **Free Enterprise**
    - Sometimes called capitalism.
    - Based on theory developed by Adam Smith which said that an economy develops better when individuals are allowed to pursue their own self-interest.
    - Under this system producers produce goods which they perceive will be purchased in sufficient quantities to earn a profit. They react to consumers' needs and wants. The consumer dictates what goods will be created
- **Centrally Planned**
    - Resources are publicly owned.
    - Government controls all areas of economic activity to eliminate the inequalities in the distribution of wealth.
    - Central planners determine the assortment of goods to be produced based on their predictions about consumer behaviour with any profits to be redistributed to all citizens
    - Central planners allocate resources for the production of goods, fix the quantities of the goods to be produced, and set the price of the goods.
    - The benefits of production are allocated according to social needs of individual units such as families and towns
- **Mixed Economy**
    - Falls between the two extremes of free enterprise and centrally planned
    - Most decisions are made by the private sectors (the market), but the government intervenes to ensure the supply of essential goods to everybody through the public sector
    - Government is also involved in planning the organisation of the economy and its future development
    - **Ireland is a mixed economy – where is the evidence for this?**

Role of the Government in the Economy

- **Achieve Full Employment**.
    - Full employment is a situation where everyone who wishes to be employed has a job at existing wages level. This is usually considered to be at 4% unemployment – why?
    - What role does our government play in ensuring this aim is achieved?

- **Achieve sustainable economic growth**.
    - By economic growth we mean an increase in output per person in the economy (expansion of the productive capacity of the economy). Thus an increase in output per person implies an increase in income per person and therefore an increase in the standard of living
    - Why was the growth of the early to mid 2000s not sustainable?
    - What are the threats to our current period of economic growth?

- **Control government finances / reduce borrowing / manage the national debt**
    - Government spending has a major influence on the economy.

- When faced with a deficit the government may have to cut spending which can have a contractionary effect of the economy – why?
- Some argue (Keynesian economics) that when faced with a contracting economy the government should borrow money to invest in capital infrastructure projects to help stimulate aggregate demand. This is called a **fiscal stimulus.** The thinking is that the fiscal stimulus acts as a kick start to the economy and has a multiplier effect (find out what I mean by this!).
- However borrowing is never ideal and it places a burden on generations to come in terms of repaying the loan and the interest on the loan. Ireland's current National Debt (Oct 2019) is €215bn or 65% of our GDP – it was €35bn in 2007 – why the increase?
- The annual cost of servicing this debt is around €5bn. If interest rates were to rise it would have a significant effect on this figure

- **Boost exports / improve competitiveness / attracting investment**
  - By taking steps to improve competitiveness, the government hopes that Irish exports will continue to grow and so help facilitate the creation jobs.
    - What steps can the Irish Government take to continue to improve our international competitiveness?
  - Our government also aim to control the cost of utilities and insurance costs for businesses
    - How?
  - Attracting investment (FDI) is the role of the IDA. Over 190,000 workers in Ireland are employed by companies who are clients of the IDA.
    - What supports to the idea provide to its clients? Find out here
    - Spin off jobs may also be created as a result of the establishment of these companies.

- **Broaden the tax base**
  - Many believe that we relied too much on the property boom for taxation revenues and we do not want to repeat those mistakes.
  - The government must introduce taxes that are difficult to avoid, hit those who can afford to pay while working to minimise tax avoidance by large corporations.
  - The government has introduced the local property tax, septic tank tax inspection charge but there more options including
    - A minimum effective corporate tax rate;
    - A financial transactions tax;
    - Increased environmentally friendly taxes; and
    - Increasing the minimum effective tax rates on high earners.

- **Promote balanced regional development**.
  - The government must try to ensure that employment opportunities and development is distributed throughout the country. The IDA plays a key role in achieving this aim with extra supports available for foreign businesses that set up it in areas outside of the main urban centres.
  - The government has a role in ensuring that the appropriate infrastructure is in place in this less developed regions to make these area attractive to FDI.
  - See Center Parcs investment in Longford – they received IDA support.

- **Improve infrastructure.**
    - The further development of the road infrastructure, provision of public transport, development of the airports and seaports is vital for Ireland's long term development.
    - See Project Ireland 2040
    - See Interactive Map of Infrastructure Projects taking place

- **Improve state services: health/education services / achieve a just social policy**.
    - Increasing emphasis is being placed on the improvement in health services, the provision of further places in primary schools, improvement in school buildings and the development of third level education.

- **Achieve a more equitable distribution of income and a just social environment**
    - The government must continue to ensure that social welfare recipient's standard of living is maintained, that it provides adequately for future pensions and helps to redistribute income within the state, given the current constraints on government current spending. Increasing the levels of pensions and improving social welfare payments are attempts by the government to help re-distribute wealth.
    - However it is important that social welfare does not create disincentives to work
    - TASC report on Inequality in Ireland

- **Control price inflation**.
    - The government must try to reduce the pressure on rising prices within the economy.
    - Our government DOES NOT HAVE control over its monetary policy which ia major tools in combatting inflation
    - However the government can control prices by
        - Stabilising the cost of living/business costs
        - Moderating wages demands
        - Taxing income

- **Achieve environmental objectives**
    - The Irish government has committed to reducing the carbon footprint of the nation by signing up to the Kyoto protocol target and under the EU2020 targets
    - Citizens Assembly on Climate Change
    - Government's Climate Action Plan

How does the government intervene in the economy

- **Collecting Taxes**
  - **Direct taxes** refer to taxes on incomes and wealth. The following are examples of direct taxes. Examples include:
    - Income tax/Pay As You Earn (PAYE)
    - Deposit interest retention (DIRT) tax
    - Capital Gains Tax
    - Capital acquisitions tax
    - Corporation tax
  - **Indirect taxes** are taxes on goods and services. Indirect taxes are paid indirectly to the government by the final consumer. Examples include:
    - Value added Tax (VAT)
    - Excise duty
    - Customs Duty
    - Stamp duty
  - The total tax take in Ireland for 2018 was over €55bn

- **Paying social welfare/Redistributing Income**
  - The Irish government uses some of the tax revenue to pay social welfare.
  - Types of social welfare payments include
    - Child benefit – universal payment
    - Job Seeker's Allowance
    - State Pension
    - Housing Assistance Payment
    - Fuel Allowance
    - Illness Benefit
    - Disability Benefit
    - Maternity/Paternity Benefit
  - The social welfare budget in Ireland is €21bn
  - See notes above re: inequality and wealth distribution
  - A **progressive tax** is a tax that **takes into account the ability to** pay of a tax payer. A progressive tax system take a higher percentage of tax from a higher income earner.
    - For example in Ireland high earners pay more in PAYE than low earners. When one earns over circa €35000 they begin to be taxed at the marginal rate (40%) as opposed to the standard rate of 20%.
    - Is someone on €34000 a high earner?
    - What is the impact of adjusting the rate bands?
    - Why not introduce more rate bands above €35000?
  - Minimum Wage
    - The government has legislation which sets minimum wage rates in Ireland
    - See more information here
    - In theory it allows a minimum standard of living for all citizens
    - How does the minimum wage differ from the living wage?

- **Providing grants and subsidies**
  - The government provides grants and sibsidies for a range of businesses and industries
    - Local enterprise offices provide grants to start up business
    - IDA provides grant and subsidies to foreign firms setting up in Ireland
    - Enterprise Ireland provide grants to Irish businesses seeking to export
    - Irish Rail, Bus Eireann and Dublin Bus are subsidized by the government to provide cheaper public transport
    - The cost of private childcare is subsidised by the government

- **State companies**
  - The government often acts a business owner to provide essential services that would not otherwise be profitable. In the past state companies were often monopolies in their markets but this has since changed with de-regulation.
  - See list of Irish State-Owned companies
    - Bus Eireann operates a number of routes in rural parts of the country that are not profitable but are seen as socially beneficial to those communities.
  - **Privatisation**
    - This is the **sale of a state owned company** to private owners.
  - **Nationalisation**
    - The purchase of privately owned assets by the government/exchequer

    - **The advantages of privatization**
      - **Improved quality / choice of services**
        - Privatised firm may improve the quality / efficiency / choice of the service provided.
      - **More competitive prices**
        - Consumers may be offered more competitive prices on goods / services.
      - **Continuity of supply**
        - The newly privatised companies may have access to new sources of funds and as they are not subject to government interference their long term prospects for survival may improve –ensuring continuity of supply for consumers.
      - **Employment opportunities**
        - If the new firm increases its market share then this may result in a growth in employment within the industry / additional job security for existing employees.
      - **More rewards/Incentives for innovation**
        - Employees may reap more rewards for their innovations within the privatised industry e.g higher bonuses etc.
      - **Revenue from sale /reduce borrowing**
        - The government could **use** the revenue from the sale of the firm to help reduce its level of borrowings.
      - **Shedding of loss making companies**
        - By selling loss making companies the financial burden on the state / taxpayers is removed.

- **The disadvantages of privatisation**
  - **Loss of non-profit making services**
    - Non-profit making services may be discontinued in an effort to reduce costs.
  - **Standards of service / increased prices**
    - The quality of services provided by the new company may deteriorate in an effort to save costs. Prices may be increased to increase revenue. Charges for services which were considered ‘free’ may be introduced.
  - **Curtailment in Pay / Pensions increases /Changes to working conditions**
    - The new owners may limit the pay / pension increases due to its employees or change its employees’ conditions of employment resulting in a worsening of these.
  - **Loss of jobs / reduced job security /increased social welfare bill**
    - Jobs may be lost through rationalisation of services, meaning higher social welfare costs.
  - **Loss of a state resource / critical infrastructure**
    - This company has been financed by taxpayers in the past. With its sale, taxpayers now lose critical infrastructure, which they once owned.
  - **Costs of the Sale**
    - All costs in preparation for the sale such as legal work must be paid for by the taxpayer.
  - **Foreign ownership**
    - Overseas buyers can become owners of a previously Irish company and so control of the asset can go outside the state.
- **Advantages of Nationalisation**
  - **Stability to economy / investor confidence**
    - It may signal to domestic and international investors that the state seeks to protect an important resource and so attract investment.
  - **Employment / consumer protection**
    - Jobs currently under threat may be protected by state intervention.
  - **Continued provision of services to the community/ prevent foreign ownership**
    - The nationalised company may continue to provide services to those communities which in the past were only provided if it was profitable to do so.

- **Running the civil service to help provide public services**
  - State services are often provided with the administrative backing of Government Departments and Local Authorities
    - The Department of Health is responsible for the delivery of public health services through the HSE

            - What is the alternative to the Department of Health (through the HSE) directly providing healthcare to citizens?
        - The Department of Education is responsible for the delivery of education is all state funded pre-schools, primary schools, secondary school and third level institutions
            - What is the alternative to the Department of Education (through directly providing education services to citizens?
        - Local Authorities have responsibility for Planning, Parks, Road Maintenance, Waste Management and Recycling, Tourism, Libraries, Water provision, Social housing provision

- **Represent the country at EU level**
    - The EU is a powerful organization that has the power to create laws that supersede Irish Law. It is the Irish Governments responsibility to represent the interests of the Irish people at all levels of EU Government (EU Parliament, EU Commission, Council of EU Ministers, The European Council)
        - Donald Tusk is president of the EU Council
        - Jean Claude Juncker is president of the EU Commission
            - Irish citizens do not get a direct day in electing our EU Commissioner of the presidents of the Commission and Council therefore it is imperative that our elected politicians fully represent our interests at EU level.

- **Acting during National Emergencies**
    - The government has a responsibility to its citizens during any national emergency whether it be a weather or economic related event
        - Ireland was on the brink of financial collapse in 2010 before our Government sourced loans from the EU, IMF, UK, ECB, Denmark and Sweden
        - See article re 2018 drought

- **Promoting Ireland as a business/tourist destination**
    - Through the IDA and the Department of Foreign Affairs Ireland is promoted around the globe as a destination for global business
    - Tourism Ireland is a government funded body whose responsibility is to promote Ireland as a tourist destination abroad.

- **Control prices or factors affecting pricing**
    - At times the Irish Government intervenes in market to control prices for the public good
        - For example Minimum Unit Pricing with regards to alcohol
        - Currently insurance premiums across the country are rising as a result of the courts awarding be compensation packages that some deem to be too high relative to awards in other countries
            - See here and here
            - People are calling on the government to intervene with regards to compensation awards but intervention is not as easy as the government passing a law

- **<u>How does regulate the economy</u>**
  - Regulation is the mechanism by which consumer's and the public interest can be safeguarded to ensure services are delivered in a safe, fair and sustainable manner.
  - The government appoints regulators who can impose price controls, sanction businesses, open up markets
  - Free market economists criticise the scale of regulation in the economy arguing that it creates an unnecessary burden of costs for businesses – with a huge amount of "red tape" damaging the competitiveness of businesses
  - The main reasons for policy intervention by the government are:
    - To correct Market Failures
      - Interesting article about market failure in the housing sector
    - Improve public welfare
    - Achieve a more equitable distribution of wealth
    - To improve the performance of the economy.

  - The government regulates markets through laws generally come from two sources:
    - Irish government departments
    - EU in the form of directives or regulations

  - The government has established a number of regulatory agencies to ensure the laws it draws up are being adhered to. These regulatory bodies set standards, monitor behavior and enforce law with sanctions where appropriate.

    - **Financial Services**
      - The Irish Central Bank regulates the entire financial industry in Ireland
    - **Communications**
      - The communications market is regulated by Comreg
    - **Food Industry**
      - Food Safety Authority
    - **Workplace Health and Safety**
      - Health and Safety Authortiy
    - **Environmental Issues**
      - Environmental Protection Agency
    - **Consumers**
      - Consumer and Competition Protection Commission
    - **Worker's Rights**
      - Workplace Relations Commission
    - **Planning and Building**
      - Local Authorities and An Bord Pleanala
    - **Public Sector**
      - Ombudsman for Public Services

- **These regulatory bodies serve to:**
  - **Improve public welfare:**
    - Consumers
    - Environment
    - Planning
  - **Correct Market Failure**

- **The consequences of regulation include**
  - Increased business costs
  - Increased prices passed on to consumer
  - Increased cost in government administration