Ecosystem tax credits for a more distributed industrial policy

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Summary

This note proposes a complementary approach to conventional industrial policy that is less top-down, much more open, decentralised, agile, and responsive to business needs, and which reduces capture by well-connected incumbents. Distributed industrial policy would involve allowing businesses to "vote with their money" by directly allocating funds towards "public good" initiatives or programmes in the ecosystem and making those contributions fully tax-deductible through ecosystem tax credits. Practically, it entails the creation of an online crowdsourcing and crowdfunding platform for “public good” initiatives/activities that support productivity and innovation ecosystems, and making businesses’ contributions to these initiatives cost-neutral for businesses by reducing their tax liability by the same amount. This approach cuts out the middlemen, allowing businesses to quickly accelerate high-value initiatives based on immediate needs, and creating a space for novel policy programmes to emerge rapidly.

The challenge

Businesses don't operate in a vacuum. The ecosystem where they operate has a strong impact both on their performance and on aggregate economic growth. The public goods and externalities that ecosystems provide are crucial to support businesses to innovate and grow. However, governments and intermediary organisations in the ecosystem are often too slow to react to businesses' needs. While top-down industrial policy is necessary to address certain challenges, it is not always well placed to address in a timely and effective manner the needs that businesses face.

Under the current model, businesses identify the needs that they have (such as training programmes, testing facilities or supercomputer access). They then convey their needs to business associations, chambers of commerce, et al. These intermediaries aggregate the information they have received from businesses (prioritising the most common needs and/or those from well-connected businesses) and lobby governments in favour of certain policy interventions and investments (with larger corporations also using their direct access to influence governments' choices). Governments often set up consultation processes and structures (such as industry councils) to get feedback from stakeholders on what actions to prioritise, alongside using data, experts, and foresight. Eventually

policymakers develop a programme of work to address some of those needs and assign budgets to execute it. Bureaucratic, rigid and slow procurement processes follow, often prioritising lowest cost providers to deliver a tightly defined set of activities, rather than innovative providers delivering much better long-term outcomes. Eventually, the programmes are executed and implemented in the ecosystem...often many years after the initial needs were expressed. On top of that, programmes are often poorly designed and evaluated, with disappointing outcomes.

This approach is inefficient, too slow, and subject to capture by well-connected incumbents. It faces many of the well-known pitfalls of central planning approaches, fails to address business needs in a timely way, and also fails to encourage innovative approaches to address them.

An alternative

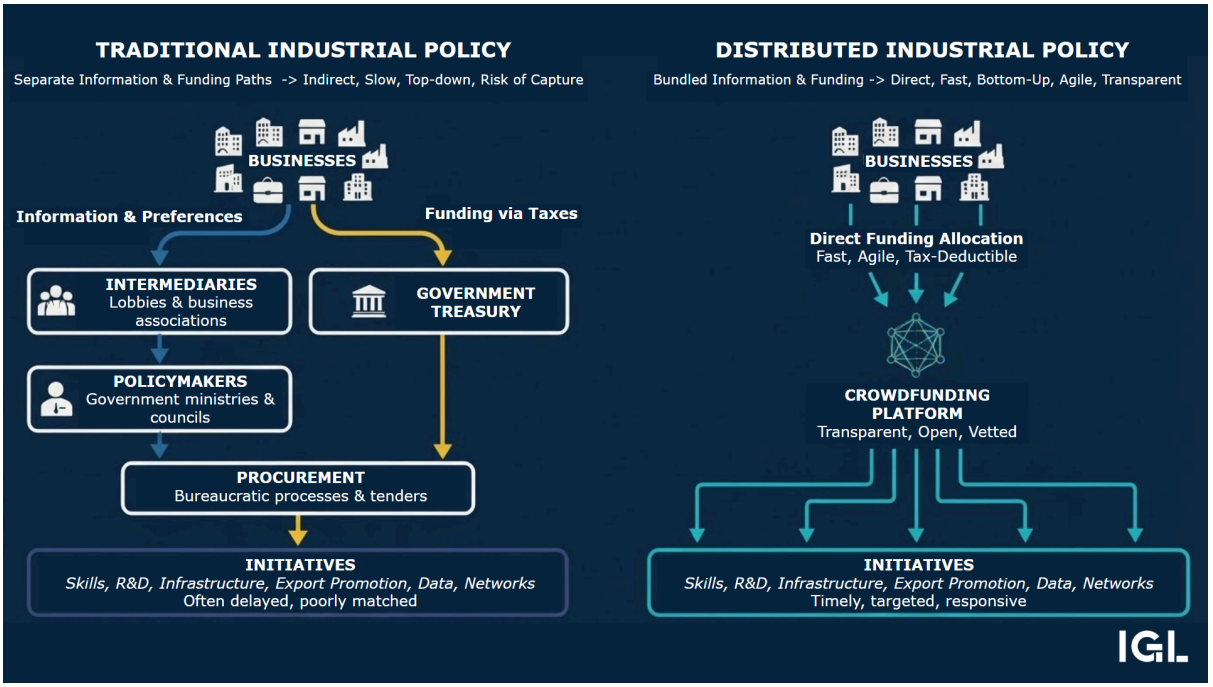
Ecosystem "public goods" (such as skills provision, networks or infrastructure) are important for business performance and economic growth. If left to the market, they would be underprovided. But central planning approaches used in traditional industrial policy can also be problematic, as discussed above. What could be an alternative?

Markets aggregate information from consumers and producers on preferences and costs, and allocate resources based on that. Could a similar approach work for industrial policy, one that allocates funding to the most needed interventions but simultaneously avoids the incentive to free-ride and let others fund the public goods?

One way to do so would be to create a system under which (a) information about business needs, (b) funding for solutions/interventions, and (c) the decisions on which ones to prioritise are all bundled together, going hand in hand. In other words, letting businesses directly "vote" by allocating a portion of their tax dollars to the ecosystem initiatives that they think would be most valuable to improve their competitiveness.

The role of intermediaries and bureaucratic processes would be greatly diminished, and information and funding would flow much more quickly towards the programmes and activities that businesses demand. With this bottom-up approach, governments would not need to always act as the intermediary that, with one hand, collects and aggregates information about business needs and, with the other hand, collects business taxes and decides how they will be spent.

This proposal for distributed industrial policy and ecosystem tax credits is inspired by Romer's self-organising industry boards idea, but adapted to the age of crowdsourcing, crowdfunding and participatory budgeting in a world with fuzzy industry boundaries. It also relates to some of the business levy schemes that some governments have implemented to address shared challenges, such as skills gaps.



This complementary channel for industrial policy would, given how it is designed, aggregate information on real business needs, crowdsource potential interventions to address them from a variety of organisations, and direct resources towards businesses' chosen priorities, all in a much more flexible and agile way than traditional industrial policy. It would also reduce coordination costs among businesses with common needs to be addressed, and encourage multiple organisations to propose innovative interventions to support their ecosystem.

How could it be implemented in practice? Basically, it would have two components:

1. An online crowdsourcing and crowdfunding platform for "public good" initiatives/programmes that support productivity and innovation ecosystems. Any organisation in the ecosystem could propose programmes or initiatives that they would like to take forward, and businesses would choose which of those to support with their funding.

2. A new ecosystem tax credit that makes businesses' contributions to these initiatives cost-neutral for them, by reducing their tax liability by the same amount they have contributed (with some limits).

This approach to distributed industrial policy (or crowdfunded industrial policy) could be implemented at the EU, national, regional and/or local level. For instance, you could imagine a city setting up a platform to let businesses pick what city-level actions to support, reducing local taxes for them proportionally.

Businesses could flexibly distribute their contributions to initiatives linked to their geography, their industry sector, and/or a specific challenge (e.g., skills availability,

technology development), with the option but not the obligation to partially or fully delegate their choices to a selected representative/intermediary.

In practice, there are a long list of interventions that governments currently fund and/or businesses often request, for which this approach could be valid. Some examples include:

- Addressing skills gaps (e.g., industry complaining that they are missing people with skills "x")
- Funding challenges (pull) or technology development (push) to address a particular industry need.
- Creating capital-intensive technology testing and/or prototyping infrastructure.
- Accessing new foreign markets (e.g., identifying export market opportunities and building networks throughout the supply chain)
- Providing access to anonymised data for product development (e.g., data sandbox such as Nesta's Open Banking challenge, or health data for biomedical research).
- Connecting businesses to the academic knowledge base through an effective matchmaking platform.
- Providing unbiased information for SMEs on the quality of business services providers (e.g., a "consumer reports"/"Which?" for business advisory services).
- Funding promotion campaigns, networks and events.
- Etc....

Compared to other policy tools, the implementation of this measure would be relatively straightforward. Obviously, there are many design features that would need to be considered on the structure of the platform and the tax deduction, such as how to screen the programmes, what role evidence and experimentation would play, whether the government could offer matched funding, and how best to prevent fraud. For instance, to be incentive-compatible and ensure that funding goes towards public goods, all the “fundable” programmes/initiatives would need to be screened by the government or a delegated party to ensure eligibility, organisations running support programmes could be prohibited from knowing which businesses had provided funding (so that it is not used under the radar to buy one-to-one advisory services instead of public goods), and some types of activities, like lobbying, would not be eligible to receive funding through the platform.

Ecosystem tax credits offer a complementary approach to supporting business growth and innovation. Departing from the constraints of traditional top-down approaches, this bottom-up policy tool leverages the collective wisdom of businesses themselves, allowing them to directly influence the allocation of resources towards initiatives that enhance their

productivity, competitiveness and innovation. By embracing the principles of crowdsourcing, crowdfunding, and participatory budgeting, distributed industrial policy offers a dynamic solution that is agile, responsive, and more effective at addressing business needs. Through an online platform where businesses can both propose and support initiatives aligned with their needs, this approach would ensure that funding flows swiftly to where it is needed most, unencumbered by bureaucratic hurdles or the influence of well-connected incumbents. Moreover, by making contributions fully tax-deductible, businesses are incentivised to invest in the collective well-being of their ecosystems, driving economic growth and prosperity.