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CAPITALISM OVERTHROWN?

understanding Labour's economic policy

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foreword
robin grainger

CEO

In the four years since Jeremy Corbyn was elected Labour leader and appointed John McDonnell as his Shadow Chancellor of the Exchequer, there is one quote that has been used almost universally in newspaper stories about him and his approach to the economy. The line from McDonnell's entry in *Who's Who* that cites his commitment to 'the overthrow of capitalism' neatly sums up how he has been presented by the media; a radical left-winger bent on upending the UK's political and economic orthodoxy. Whether on public ownership, taxation or regulation, what is often described as 'Corbynomics' really begins with McDonnell's thinking.

Yet Labour simultaneously builds up and plays down the radicalism of its policy agenda, caught between wanting to sell a drastic and fundamental break with the alleged consensus of the last four decades, and presenting its proposals for economic reform simply as a common sense, almost inevitable alternative to a capitalist system that even the Conservatives now appear to admit is no longer fit for purpose. In this context, McDonnell positions himself not as an anti-business agitator but as a conciliator and moderator, asking business leaders to co-operate in building a new consensus and fixing broken markets. Labour often appears to take a black and white view on the economy and domestic policy questions, but the underlying detail is usually more complex.

At GK, we are helping businesses and investors get to grips with Labour's plans for the economy. We and they are not just concerned with tax and spend and the macroeconomic impact, but how the party in power might drastically change the rules of the game for businesses and fundamentally shift the balance of power between the state and the private sector, and employers and workers.

In our previous paper, *What Would Jeremy Do?*, we took a broad look at what might be in store across a range of sectors in the first term of a prospective Labour government. In this report, we focus on John McDonnell, a Labour Treasury and the economic policy priorities of the party as it prepares for the possibility of power. With a general election around the corner, now is the time to think about what this might mean for your business and how you can best prepare.

John McDonnell and the development of Labour's economic policy

jamie cater, head of policy

When John McDonnell was appointed Shadow Chancellor in September 2015 after Jeremy Corbyn's election as leader, almost all of the media reports on him contained the citation from his *Who's Who* entry that described his aim of 'generally fermenting the overthrow of capitalism'. With Corbyn having spent much of his three decades on the backbenches focusing on foreign policy, national security and an array of lower-profile domestic issues, McDonnell has always actively engaged with economic policy questions. Despite some concerns over whether McDonnell's temperament made him suitable for the role, he was the natural choice for Corbyn to take on the role of Shadow Chancellor.

It has arguably been McDonnell's radical leftism, rooted in the politics, economics and culture of Marxism, that has characterised many of the perceptions of the Labour Party's transformation under Corbyn's leadership. From a starting point of breaking with the 'neoliberalism' of the Tony Blair and Gordon Brown years – and, many of Corbyn and McDonnell's supporters would argue, too much of Ed Miliband's leadership too – McDonnell and Corbyn's apparent desire to create a 'genuinely socialist' alternative for the British economy has both inspired the party's grassroots and raised the hackles of the business community.

The party's philosophy under the current leadership is, in many respects, uncomplicated. The belief that nearly a decade of Conservative-led government – and a longer period in which both Conservative and Labour administrations have pursued largely similar economic philosophies – has led to sustained inequality and a society in which wealthy individuals and corporations hold too much power, and workers and poorer households hold too little, is not new in British politics, and the current Labour leadership has managed to articulate the desire for change in a more coherent way than its immediate predecessor.

Yet for all of the rhetoric, McDonnell has also frequently tried to adopt a moderate, conciliatory tone; launching a so-called 'tea offensive' in the City of London to match Blair and Brown's 'prawn cocktail offensive' to charm the finance sector leading up to the 1997 election, as well as extending invitations to business leaders to take advantage of his 'open door' policy to discuss the detail of his plans for the economy. The edges of McDonnell's push for drastic change are softened by his attempts at civility, even if many in the City remain highly sceptical of his intentions.

Jamie joined GK 2014 from the office of a Labour MP and Shadow Minister. In his role as Head of Policy, he manages GK's research and analysis work for private equity investors, providing political and regulatory due diligence during the acquisition and sales processes, as well as ongoing advice on relevant policy developments over the course of their investments. Jamie works across a range of sectors, including education, employment, housing, health and social care, and financial services.

Perhaps most important to consider is the relationship between the development of the party's economic policy and its social policy. The debate in the party around policies such as public ownership, workers' rights and the role of private business is not centred on old-fashioned language around nationalising the commanding heights of the economy, but addressing areas where the market is deemed to have failed and there is consumer detriment that warrants significant political action being taken. It is rarely the traditional left ideological argument about the ownership of the means of production or even the level of profits made by private companies; rather, it is largely a question of providing a better deal for consumers and savings on household bills.

That is not to say that Labour's plans would not constitute significant upheaval and disruption across a range of sectors, and it is possible that the radicalism could increase over a term in government, but the party's plans for economic change are best understood as a reaction to the current political environment and public concerns in relation to specific markets rather than a long-term strategy based purely on an unchanging ideology.

the four pillars of labour's economic policy

The development of Labour's economic policy can be divided into four pillars: supporting low-income houeholds, transferring power to workers, transferring power to taxpayers, and tackling climate change. In all of these, it is clear that economic policy is viewed as a means by which to achieve wider social aims.

Supporting low-income households

This is primarily manifested in the commitments to reversing public spending cuts from the last decade, particularly in key areas such as education, health and social care, and social security. A higher minimum wage for workers of all ages – likely to be introduced immediately by a Labour government – is also a key tenet of this, and the presumed savings to household bills from bringing the utilities into public ownership also ties into this part of the economic strategy.

Transferring power to workers

In the context of the gig economy, the impact of Brexit on workers' rights regulations and the power held by the trade unions in the Labour Party, giving workers greater power and influence in their workplace is a clear priority for Labour's economic policy.

It is also where the party has arguably been at its most radical. The pledge to create inclusive ownership funds – effectively forcing companies to hand 10% of their shares over to a committee of employees with dividends distributed between them and the Treasury – is perhaps the closest the party leadership has come to committing to a truly radical overhaul of corporate governance and company law.

Transferring power to communities

The plans for public ownership are defined not only by savings in household bills and consumer costs, but also by the argument that it would create opportunities for local communities to be empowered.

This is important not just when considering the future shape of public ownership and how the party makes policy around initiatives such as the industrial strategy, but for its wider approach to the private sector and its role in the delivery of publicly-funded service provision. The party's commitment to backing community-owned alternative providers in markets such as energy supply is thin so far, but could extend into other areas.

Tackling climate change

The growing support within among the party's rank and file for an approach that more closely mirrors the Green New Deal proposed by left-wing Democrats in the US became apparent at the 2019 party conference where delegates supported a motion committing to ambitious carbon reduction targets through economic reform. Some of the leadership's support for a radical approach to environmental targets as part of its overall economic policy has been tempered by the scepticism of the trade unions, who argue that there would be a detrimental impact on jobs in areas of the country with high levels of employment in heavy industry or gas and coal power stations.

While McDonnell may have reined in his rhetoric on this particular area given these fears, he has been clear that environmental concerns are an influential part of Labour's economic policy-making. The current Government and the Bank of England have already spoken about increasing reporting requirements for businesses in relation to environmental impacts, and it is highly likely that Labour would go further along these lines.

deficit, debt and labour's fiscal rules

Between Corbyn's election as leader in September 2015 and the 2017 general election, Labour made a deliberate effort to sustain the narrative that it would restore prosperity 'for the many, not the few' while maintaining fiscal discipline. While there was little doubt that a Labour victory in 2017 would have meant a drastic increase in public spending as it pursued the strategy above, the party presented its plans as fully costed.

In October 2017, the party published its Fiscal Credibility Rule, which formalised the manifesto commitment to ensuring that borrowing for current spending would be eliminated in five years while maintaining the ability to borrow for investment. The overall commitment to achieving a balanced budget framed many of the policy commitments in the first two years of Corbyn's leadership. A number of spending pledges, whether on the abolition of higher education tuition fees, introduction of free school meals for primary school pupils or others, were made through the hypothecation of new tax revenues. The intention was not only to improve public perceptions of Labour's ability to manage the economy by demonstrating that it would be possible to achieve a balanced budget while increasing public spending, but also to convince sceptics within the party of particular tax rises that they would be used to fund policies that garner a wider political consensus.

However, recent announcements have had less regard for this approach. Several policy pledges made at the party's 2019 annual conference were significant in terms of public expenditure required but had less detail over how they might be funded; it is rare now that the party makes an explicit promise to keep within the bounds of its Fiscal Credibility Rule.

Arguably, the current Government's own approach to economic policy – not only the relaxed position on the impact of a no-deal Brexit, but the major spending commitments made by Boris Johnson on becoming Prime Minister that have led to the effective scrapping to its own fiscal rule of keeping borrowing below 2% of GDP – have given the opposition the political space to make such commitments with less fear of being pulled up on the details of how they might be funded. It is true that the Conservatives are still more trusted by the public to manage the economy than Labour which undoubtedly emboldens them to pursue the 'end of austerity' in office, but the move away from the austerity narrative also means that Labour seeks to be bolder to sustain its position as the radical alternative to the incumbent administration.

As both parties have shown over recent months, fiscal rules are primarily political constructs rather than wholly objective economic constraints, and there are two important considerations the party will make in relation to its position on public spending. The first is the room for manoeuvre that a Labour government might have in a coalition or minority government if Parliament has voted on its fiscal rules. While the political barriers to policies like public ownership are likely to be low even in a coalition government, an upfront cost that risks breaking the fiscal rule could lose political support. In practice this is unlikely as a Labour government could probably avoid keeping at least some of the costs of this off the balance sheet, but this could prove to be the biggest immediate political risk to the public ownership plans.

The second is the question of social value, broadly defined as the wider economic, social and environmental effects of an organisation's actions. The balancing of economic and social value is increasingly intrinsic to policy-making in government, and the significance of what Labour seeks to do on the economy – whether in relation to corporate governance and workers' rights, regulation of the private sector or public ownership – may be that it gives greater precedence to the perceived social value of a policy or programme than the upfront financial cost or other economic impact. This may be of particular importance when considering how valuations are made for private assets brought into public ownership. Discussion of Parliament deciding asset valuations typically veers towards companies being compensated below market value; however, it may be that a Labour government is prepared to pay above market value for these assets if Parliament votes for this or Labour judges the social benefit – through reduced household bills, smaller environmental impacts or other potential consumer benefits – to provide value for money where the cost borne is greater than the determination of market value.

This is an approach that is also likely to inform the party's efforts to re-write what is known as the Treasury's Green Book – the guidance published by central government on how public investment is evaluated and appraised. Therefore, a Labour government's spending priorities in areas like infrastructure is likely to pay much greater heed to environmental, social and governance considerations than is currently the case; more broadly, it is also likely to frame how it would think about awarding any public contracts to private companies or reforming corporate governance in the UK. A range of criteria – whether payment of employees, workers' rights, human rights, ethical supply chains or others – are likely to form a framework for decision-making on a variety of areas economic policy.

It is perhaps not a surprise that Labour's fiscal rules are likely to be subordinate to other political priorities given the urgency of the party's desire to increase investment across the public realm, its flagship policies in relation

to public ownership, and the desire to use economic policy as a tool to serve its wider social policy aims. A Labour government would also be neither the first nor the last in the UK to abandon a fiscal rule for political expediency. However, it is the significance of how it might think about the value of economic reforms from the perspective of achieving social change that is the best guide to weighing up Labour's approach.

considering social value

The concept of social value is an important political tool for the party. Like the hypothecated tax revenues, they help to persuade sceptics – inside or outside of the party – of the case for undertaking a potentially radical policy change. Just as some moderate MPs might instinctively be uncomfortable with the party's policy of imposing VAT on private school fees but are prepared to accept it on the basis that revenue will be used to fund free school meals in state schools, some may not be convinced of the ideological basis for reinstating public ownership of the utilities, for example, but it becomes harder politically to argue against a policy that is largely predicated on the argument that their poorest constituents would benefit from cheaper bills.

This also speaks to a broader theme of Labour's economic policy, and one that helps to make sense of where Corbyn, McDonnell and the team around the leadership draw the line between ideology and political pragmatism. For all the public and political discussion of the Marxist influences on the thinking of the Shadow Chancellor in particular, it is not immediately apparent that there is a consistent ideological underpinning to the party's economic policy-making. Rather, much of its policy development aims to address what Labour considers to be severe market failures – whether in the privatised utilities, rail, financial services – alongside reversal of cuts in public spending, and increasing minimum pay and workers' rights. It aims to improve the lot of workers and low-income households in response to the gig economy and continuing low pay, secure better local public services after nearly a decade of spending cuts, and increase scrutiny of company directors amid public concern over the behaviour of the likes of Philip Green, as well as the demise of large public sector outsourcers like Carillion and the apparent failure of existing corporate governance rules to address these.

It is an economic policy framework unquestionably of the left, involving a larger and more powerful state and public sector, and undoubtedly a significant departure from the recent approach of both of the main political parties, but it is both more reactive and less rigidly ideological than many commentators have assumed. Like all governments before it, a Labour government led by Jeremy Corbyn and John McDonnell would be subject to political pressures, parliamentary arithmetic and changing economic circumstances. This does not mean that once they have committed to a policy they are likely to change course – and does not mean that their radicalism may not increase over the course of a term in office – but they have made their policy positions knowing their party and the voters they want to mobilise. Whether it proves to be a winning strategy at the next election remains to be seen.

how should businesses and investors prepare for a labour government?

The first step

is to map policy-related risks on the basis of a rigorous assessment of policy detail (rather than rhetoric) and what Labour is likely to do in practice.

The second step

is to recognise that some changes might bring opportunity, especially due to increased public funding or shifts in public procurement – where Labour's antagonism is not about the independent sector per se but large scale outsourcing.

Opportunities should increase for SMEs in public procurement and for organisations that can demonstrate social value – by addressing the needs of local communities and vulnerable consumers, for example. Any business operating under a Labour government – or seeking work with Labour local authorities – would be wise to improve their social value offer and demonstrate that they are responsible businesses, especially in relation to Labour's key concerns.

Businesses and sectors that fail to meet Labour's expectations face a much higher risk of strict regulation and harsh public criticism than under the current administration.

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Between 2012 and 2015 he served as Minister of State for Schools and in a cross-departmental role in the Cabinet Office, and now sits as one of GK's Strategic Advisers. With his wealth of experience at the centre of British politics, David brings invaluable insight and expertise to GK's work. In addition to this, David is Chair of the Education Policy Institute, and advises Ark Schools' Education Partnerships Group on education in Africa and the Indian sub-continent.

david laws, strategic adviser

What might a Labour Treasury look like under Chancellor John McDonnell?

Traditionally, the left wing of the Labour Party has been suspicious of the Treasury - viewing it as part of the 'capitalist orthodoxy', and as an institution whose focus is more on public spending control rather than proactive policies to support industry and growth. However, once this 'commanding height' of British government is under their control, it is difficult to see the new Chancellor giving it up. An effective Chancellor can be as powerful – if not more so – than the Prime Minister, and politicians generally do not give up power.

How, then, might a powerful HM Treasury evolve under McDonnell management?

It is fair to say that the institutional Treasury would be nervous about Labour's new agenda. Changing the inflation remit of the Bank of England, big spending, much higher tax rates, and more economic interventionism are hardly what the Treasury instinctively recognises as good economic policy. And even under more left-wing governments, the Treasury has served more as a brake on radical change than an accelerator of it.

However, this reticence about key Labour policies would be offset by the natural default position of civil servants to serve the government of the day, and by the Treasury's desire to be the engine room of any government. And McDonnell will find allies in the Treasury in his attempts to boost infrastructure investment and treat capital investment more favourably.

A Labour Treasury would need to focus on four key areas. Firstly, public spending and public borrowing. What would the new spending plans be, how would they be paid for, and what would be the government's attitude to limits on borrowing?

Secondly, taxation. Under McDonnell, high earners and business would pay more. Loopholes would be closed, and McDonnell will need advice on how to extract more from firms and individuals who are well practised in avoiding paying the standard rates of tax.

Thirdly, economic policy and interest rates. The Treasury will be key in redesigning a more activist economic policy and rethinking the Bank of England's role. Treasury officials see the existing model as a success, so McDonnell should expect some push back in this area.

Finally, nationalisation. Here, even where individual departments should be leading on policy, they will be heavily guided by the advice and expertise of the Treasury. This could have a big impact on how Labour's plans are delivered.

A McDonnell Treasury will be the powerhouse of the domestic policy programme. There will be some difficult discussions between officials and the new ministerial team, given the large change in policy direction which is envisaged. But if he listens carefully to advice received, McDonnell will discover that his civil service team can help make his radical plans more deliverable.

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labour and taxation

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Overhaul of the taxation system is a major theme in the 2017 Labour manifesto and subsequent policy documents. While these measures are in part necessary to fund the party's spending pledges, Labour has been careful to highlight ways in which they increase fairness, and fit into the broader Labour vision of rebalancing the economy.

Broadly, Labour's tax policies aim to cut down on abuses and remove the regressive discrepancies between taxation on income from labour compared to financial assets. This sentiment is reflected in recommendations made by Labour-leaning think-tanks.

The priorities of an incoming Labour government are likely to be raising corporation and capital gains tax, as well as introducing a raft of anti-tax avoidance measures. These are unlikely to be controversial among the party's core voters, and in many cases are straightforward to implement via a finance bill.

In the accompanying document to the 2017 manifesto *Funding Britain's Future* Labour estimates that its tax measures could raise an additional £48.6 billion per year. This includes a £3.9 billion offset for behavioural change and uncertainty.

taxes on business

The UK has one of the lowest effective rates of corporation tax of the major developed economies, at 19 per cent for 2019-20. This compares to 21 per cent, plus a variable amount of state-level tax in the US, and 31-33 per cent in France.

In its 2017 manifesto, Labour said it would, 'ask large corporations to pay a little more while still keeping corporation tax among the lowest of the major developed economies.' At the time they proposed increasing the headline rate of corporation tax from 19% in 2017–18 to 21% in 2018–19, 24% in 2019–20 and 26% in 2020–21. This would return the rate to its 2011 level, with an estimated yield of £19.4 billion a year.

For companies with annual profits below £300,000, they would reintroduce a small profits rate at 20% in 2018–19, rising to 21% in 2020–21.

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Interestingly, in 2018 the left-leaning Institute for Public Policy Research (IPPR) proposed that corporation tax should be raised to 24 per cent, which they calculated would still make it the lowest effective rate of taxation in the G7. Though a Labour majority government is unlikely to have problems getting parliamentary approval for a rise to 26 per cent, 24 per cent could become an important anchor for those who oppose the rise.

Linked to the corporation tax rate, Labour has said it wants to crack down on incorporation avoidance – where individuals self-incorporate in order to pay the lower corporation tax, rather than the now substantially higher rates of income tax with national insurance contributions. OBR modelling puts this loss of revenue at around £1.7 billion for 2018-19, and £2.5 billion by 2020-21.

Turning to the local level, Labour's manifesto lays out plans to for a package of reforms to business rates – including switching from RPI to CPI indexation, exempting new investment in plant and machinery from valuations, and ensuring that businesses have access to a proper appeals process. In the longer term they commit to reviewing the entire business rates system, including considering new options such as a land value tax.

corporate tax reliefs

Along with the increase to headline corporate tax rates, Labour has consistently criticised the complex system of tax reliefs that are likely to be reviewed under a Labour government. In *Funding Britain's Future* Labour estimates that as a result of its review the Treasury could save £3.8 billion a year.

Entrepreneurs' relief

Entrepreneurs' relief was introduced in 2008 and was intended to encourage people to start or invest in new businesses by promising a lower rate of capital gains tax when they sold out. In its current form entrepreneurs pay half the 20 per cent rate of capital gains tax on up to £10 million of gains.

In the 2017 manifesto Labour promises a review of tax reliefs, and specifically mentions the need to review and evaluate Entrepreneurs' Relief against its effectiveness. The relief has also been criticised by the Resolution Foundation, who have said that at an estimated cost of £2.7 billion a year it is, 'expensive, ineffective and regressive,' and that there is, 'no evidence that it has led to any substantial increase in genuine entrepreneurship.'[1] The likes of the Institute Fiscal Studies, another non-partisan think tank, have also criticised the relief.

The scepticism around the relief makes it a prime candidate for a tax break to be scrapped under a Labour government. Philip Hammond reportedly considered its abolition during his time as Chancellor; John McDonnell is unlikely to have as many qualms as Hammond in calling time on the policy.

Research & Development Tax Relief

R&D tax relief provides up to 33 per cent cash back on every pound spent on research and development by businesses. Originally introduced in 2000 it is now one of a number of similar incentives including Patent Box and Creative Sector tax reliefs.

Unlike Entrepreneurs' Relief R&D relief is not mentioned in the 2017 manifesto, so whether and how it will be targeted by a Labour government is unclear. However an influential IPPR report, *Prosperity and Justice: A Plan for the New Economy,* which has been praised by the Labour leadership calls for 'the phasing down and eventual abolition of R&D tax credits other than for SME firms younger than seven years old, and the phasing down and abolition of the patent box.' John McDonnell has also previously suggested that Labour would scrap the Patent Box scheme on the basis that it only advantages large companies.

As noted above, diluting or scrapping incentives that help the UK remain competitive will be more politically contentious than headline corporate tax increases, and are likely to be a lower priority as a result. However, some reform to the system to reconfigure support for SMEs is likely to be on the cards.

capital gains

Labour plans to reverse cuts to capital gains tax in the 2016 and 2017 budgets – taking the higher rate from 20% back to 28%, and the lower rate from 10% back to 18%. Like increases to corporation tax these changes are likely to be pretty straightforward to make, and can be expected early in a Corbyn government's term.

Labour has also made it clear it intends to crackdown on tax avoidance involving capital gains. The party's 'Tax Transparency and Enforcement Programme' lists the 'Mayfair tax loophole' – i.e. the taxation of carried interest as capital gains – as a practice that is estimated to cost the exchequer £0.7 billion a year, and which allows equity fund managers to pay tax of 28 per cent or lower on much of their income.

This issue has been raised in Parliament as recently as March 2019, when rules were tightened as part of amendments to the 2015/16 Finance Bill. These ensure that investment fund managers will pay at least 28 per cent tax on the value of the carried interest they receive, but still allows it to be treated as capital gains.[2]

Although Labour has not been entirely clear on how it thinks carried interest should be treated, they have implied that it should be treated as income rather than capital gains. Moderate backbench MPs such as former deputy leadership candidate Stella Creasy have made similar calls in the past, and while it is unlikely to constitute an immediate priority for an incoming Labour government, it is something that could be achieved with relatively little opposition in Parliament should the party have a strong majority in the Commons.

In the controversial new Labour report 'Land for the Many', the authors suggest extending capital gains tax to increases on the value of people's primary residence, by scrapping the Capital Gains Tax exemption on the sale of main homes (worth £28 billion in 2017-18). This report is not currently Labour policy, and this particular suggestion seems like one that could disproportionally damage Labour during an election campaign.

It also stands at odds with the IPPR report mentioned above, which argues that the exemption should remain.[3]

income taxes

In addition to corporate and capital gains taxation, increasing personal income tax for the highest earners will be at the forefront of Labour's first steps on economic policy if it forms the next government. The 2017 manifesto commitments to increasing income tax for those earning over £80,000 are likely to endure, and the proposed top rate of 50% on earnings over £123,000 a year in the 2017 manifesto would be likely to move – through lowering the threshold or increasing the rate – over the course of a term in office.

There are more drastic steps an incoming Labour government could take; were it to consider a more radical policy on minimum pay and welfare by introducing a universal basic income – something McDonnell has committed to exploring – then this could be partly financed by abolishing the personal allowance, though this would be burdensome from an administrative perspective and involve bringing more taxpayers into the upper rate of income tax as the threshold is tied to the personal allowance. A higher

top rate of income tax where any increase in revenue is used to fund more generosity in the welfare system is probably more likely to be popular with Labour voters as well as being more redistributive and far simpler to implement, meaning this is likely to be the more attractive option to a Labour Treasury.

Outside of income tax, Labour committed to not increase national insurance contributions in 2017, but this would be a relatively easy option for the party to consider if it wanted to raise revenue for a specific spending pledge, like the Labour government in 2001 when it increased NICs to fund an increase in NHS spending. While there are also likely to be implications for NICs from any additional reforms it pursues around labour market reform – zero-hours contracts, self-employment – the party will aim to ensure that the tax burden from any reforms falls more heavily on employer than workers.

tax transparency and enforcement programme

Labour estimates that it can recoup between £6.5-8.5 billion annually through its program of anti-tax avoidance measures. Apart from the so-called 'Mayfair tax loophole', and incorporation avoidance described above, the party plans to crack down with measures including:

- Closing the Eurobond loophole which allows securities listed at the Channel Island Stock Exchange to be exempted from withholding tax (i.e. the UK company makes interest payments gross), even though the securities may be held by opaque companies. Labour cites independent estimates putting the tax lost at £0.5 billion per year.
- Clampdown on aggressive tax avoidance used by temporary recruitment agencies ('umbrella schemes'). Losses estimated at least £0.1 billion a year.
- Consulting on the introduction of a withholding tax levied against any dividend, interest and related payments to individuals or companies in abusive tax havens. This will be deducted at source before any payment is made and remitted to HMRC.
- Require public filing of large company tax returns and of wealthy individuals earning more than £1 million.
- Introduce a General Anti-Avoidance Rule to strengthen the current General Anti-Abuse Rule. The latter requires HMRC to seek permission from a business advisory panel before taking any legal action to stamp out abuses, which Labour says is a barrier to taking action. Under the new rule any transaction lacking economic substance will be considered to be a sham and thus not allowed for tax purposes.
- Create an offshore companies levy. This will capture purchases of UK property from offshore trusts located in tax havens.
- Co-operating internationally to introduce full country-by-country reporting across the tax jurisdictions
- Introduce comprehensive public registers of beneficial ownership to be set up in the Crown Dependencies and Overseas Territories.

'Land for the Many' report

In June 2019 Labour published a controversial report reviewing taxation of land and property in the UK. Although this is not official Labour policy, it was commissioned by the leadership, and is an indicator of how their platform might develop in advance of the next general election.

At the core of the report is the goal of removing the incentives to treat land and property as financial assets.

Apart from the removal of the capital gains exemption for the sale of first homes mentioned above, the report recommends replacing council tax with a 'progressive prosperity tax' paid only by owners, and based on annually updated property values. Empty homes and second homes would automatically be taxed at a higher rate, with a surcharge for properties owned by people not resident in the UK for tax purposes.

As discussed in our paper *What Would Jeremy Do?* Council tax reform would be highly controversial, and Labour's loose manifesto commitment to conduct a review probably reflects awareness of this.

Land for the Many also proposes replacing Business Rates with a Land Value Tax calculated on the basis of rental value, in line with the suggestion in Labour's manifesto.

Stamp Duty Land Tax would be phased out for those buying homes to live in themselves, offset by an increase in capital gains tax for second homes and investment properties in line with income tax rates.

The report also recommends abolishing inheritance tax and replacing it with a lifetime gifts tax levied on the recipient, at income tax rates. This is echoed in the IPPR report, which recommends a lifetime gifts tax with a lifetime allowance of around £125,000, and estimates that this could raise an additional £9 billion a year. Reform would be extremely difficult to achieve politically but, with increasing debate over the level of public funding for adult social care, it would be an appealing prospect for Labour to explore.

labour and business

ioan phillips, political analyst

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Private sector business dominates the UK economy and labour market.[4] In 2018, there were ~5.7 million private sector businesses in the UK - a ~60% increase since 2000.[5] Of these ~99% were small and medium-sized enterprises (SME). They employ ~16 million people - almost 50% of the UK's working population – and account for ~£1.9 trillion in yearly turnover.[6] Though few in number, large businesses have a similarly significant economic impact, employing ~6.2 million people and accounting for ~£1.6 trillion in yearly turnover.[7]

background: labour business policy from Blair to Corbyn

The period 1997–2010 saw convergence between Labour and the Conservatives on business policy, but a normative gap has reopened in the last decade. Successive New Labour governments accepted large tenets of Thatcherite economic philosophy, which was reflected through cuts to corporation tax; reducing the tax burden on business to make it more internationally competitive; and financial deregulation.[8] The break with New Labour started under Ed Miliband, with tax rises for higher earners, banking reform, and pledges to confront "predator" capitalism notable motifs of his leadership.[9] However, these were not fashioned into a coherent message, and any electoral traction was lost amid earnest but abstract talk of concepts such as "predistribution".[10] Under Corbyn and McDonnell, Labour says business policy favours the monopolistic "few" against the undercut "many".[11] In this respect, their critique is not new – just better articulated than Miliband's.

what does labour want to do and how should we read its offering?

The notion of the elite against the rule-abiding majority shaped Labour's offering on business in the 2017 general election. In its manifesto, the party promised to:

- raise income tax for those earning more than £80,000;
- raise corporation tax for large businesses;
- introduce more stringent regulations on public registers of beneficial ownership in the Crown Dependencies and Overseas Territories to tackle tax avoidance and evasion
- establish a National Transformation Fund to support the creation new, high-skilled, high–
- paid and secure work;
- establish a National Education Service in England;
- introduce free, lifelong education in further education colleges for anyone to retrain at any point in life;
- establish sector councils;
- encourage private investment in the UK manufacturing industry by removing new plant and machinery from business rate calculations;
- create a National Investment Bank;
- make the legal demarcation between investment and retail banking clearer via regulatory change;
- amend company law to ensure directorial remit includes social responsibility to employees, customers, the environment, and the wider public;
- amend regulations governing takeovers to ensure businesses identified as "systemically important" have contingencies to protect workers and pensions;
- introduce an Excessive Pay Levy to reduce pay inequality;
- scrap quarterly reporting for businesses with yearly turnovers of £85,000 or less;
- legally define a co-operative model of business ownership; and
- nationalise rail, utilities, and the Royal Mail.

Although dubbed by some commentators as the "most left-wing" manifesto in a generation, this failed to appreciate the substantial policy overlap between Corbyn and his predecessor on business.[12] Take rail nationalisation, for example. In 2017 Labour said it would only nationalise upon the expiration of franchises.[13] The party's 2015 manifesto pledged to increase public control over the rail network and review the franchising system to enable public sector operators to challenge private train operating companies (TOCs). While avoiding use of the word "nationalisation", the 2015 proposal still use the expiration of franchises as the primary mechanism through which to introduce publicly-owned train operators into the network. Labour's 2017 business platform also channelled the prescriptions of 2015 on banking reform and small businesses – albeit couching them in more radical rhetoric. Party policy on institutional investment regulation is a case in point. Whereas in 2015, Labour soberly pledged to "change takeover rules to enhance the role of long-term investors … [and] strengthen the public interest test"[14], its 2017 manifesto utilised the language of companies being "sacrificed for the sake of a quick buck" to make the same such pledge.[15]

inclusive ownership funds

Arguably the most radical policy that Labour has countenanced in relation to reform of corporate governance and workers' rights is that of inclusive ownership funds. Under the policy, 10% of shares in large companies would be transferred to an inclusive ownership fund managed by a committee of employees over the course of a decade; an annual dividend of up to £500 would be paid to employees, and the employee committee would be given the same rights as ordinary shareholders in the company.

Criticism of the policy as a 'stealth tax' – as the balance once the £500 has been awarded to each employee is collected and retained by the Treasury, even if this increases over time as the company grows – is unlikely to deter McDonnell and his team. In labelling this as a 'social dividend' reserved for public service funding, the party demonstrates again how arguments around social value run through its economic policy. Analysis of the policy by Clifford Chance suggests that the effect of the policy is to increase significantly the UK's corporation tax take; Labour is unlikely to see this as an argument against the policy. The chances of Labour rowing back on this policy ahead of a general election are extremely slim.

Where opposition could arise is if the party decided to extend the policy beyond the 10% shares allocated to inclusive ownership funds to enable employees to take control of the company. The party has been supportive of the establishment of more worker co-operatives but has stopped short of indicating that this could combine with the policy on inclusive ownership to push the prospect of employees taking control of their companies in this way. If the policy is popular with employees and brings in significant revenue for the Treasury it could be extended, but the prospect of it being altered to the extent of employees becoming significant shareholders in a company is likely to remain off the cards.

environmental criteria for public companies

One of the highest-profile policy interventions that John McDonnell made in 2019 was the suggestion that a Labour government would remove companies from the London Stock Exchange if they did not meet a set of criteria for mitigating their environmental impact. As noted previously, addressing climate change is one of the key pillars of Labour's economic policy in the context of arguments around social value, and this policy has cemented the importance of this in the party's thinking.

Although it is not clear precisely what the criteria would be, or what the intermediate penalties might be for companies who flout some of the rules before they are at risk of being delisted, what is most significant about this proposal is how it can provide a framework for how a Labour government would consider engaging with private sector employers more broadly. A framework is likely to be developed that sets stringent targets on environmental contributions as well as other aspects: McDonnell himself has previously called for companies to be delisted if they do not meet certain criteria on workers' rights and human rights. Treatment of employees, ethical supply chains and other criteria should be expected to be included alongside environmental targets; although delisting companies may prove to be a step too far, the overall approach is instructive as to Labour's thinking on what ethical business looks like, particularly those who might benefit from recourse to public funds.

reform of the Bank of England

The *Financing Investment* report published by economist Graham Turner has set the tone for Labour's evolving position on the future remit of the Bank of England. The envisaged role for the Bank would be the most significant change to its remit since the last Labour government made it independent in 1997. It would involve the Bank in more in policy areas that have typically been the domain of the Treasury, most notably in addressing productivity. Becoming involved in the Labour government's industrial strategy are not, in reality, a significant leap from the current relationship between the Bank and the Government – the Bank's Chief Economist, Andy Haldane chairs the Government's Industrial Strategy Council – but the reforms suggested to the Bank's remit, including credit guidance to direct investment into more productive sectors, would be a significant departure from the Bank's role over the last 20 years.

The expectation is that financial institutions in the round play a greater role in supporting the aims of an industrial strategy intended to boost productivity, especially in the tech sector, but the party has yet to commit to a detailed plan of how the financial sector beyond the Bank of England could contribute to this.

intellectual influences on labour business policy

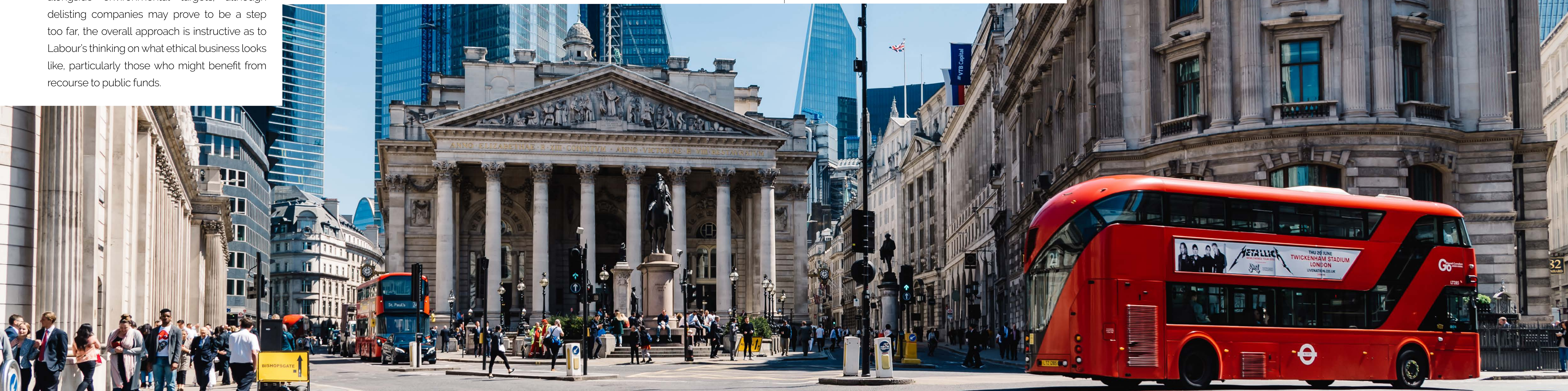
Milibandite roots aside, Labour's business offering has been shaped a number of left-wing think-tanks. These include Common Wealth, a new outfit aimed at radically overhauling the ownership of British business, and Autonomy, which examines the future of work. Meanwhile, established outfits such as the IPPR, which provided the ideological backbone of Blairism, have swerved leftward and called for a comprehensive reshaping of the British economy. The left's ascendancy at every level of the party has given such think-tanks space to develop policy.[16] Those involved with the think tanks acknowledge that policy development is inchoate. But the core emphases – employee ownership, nationalisation, and the future of work – give a solid indication as to the priorities of a future Labour administration for the business sector. This growing network of thinkers and institutions means these ideas will likely survive long after Labour's current leadership has gone.

business attitudes to labour business policy

Labour's better than expected showing in the 2017 general election and the Conservatives' transmogrification into champions of a no-deal Brexit have arguably compelled business into giving the party a greater hearing than many thought would be the case. The business community's attitude toward Labour is – on the whole – pragmatic. Take, for example, Labour's vow to "democratise" the economy. On this, bodies such as the CBI have tried to meet the party halfway. The CBI responded to the inclusive ownership funds announcement by advancing a hybrid model in the form of an ISA share scheme that would allow employees to enjoy tax breaks, while still meeting Labour's goal of employee ownership.[17] Widespread wariness endures - especially amongst larger businesses - toward policies such as nationalisation, with a recurrent critique being that Labour has not produced sufficient evidence to show it would deliver better service to users at lower cost than privately-run companies. There are, however, some policies that business like – including sector councils and workforce upskilling.[18]

will labour's agenda be implemented?

The viability of Labour's plans for business is hard to gauge. For a start, the practical aspects of implementation have yet to be fleshed out. For example, Labour is emollient about sector councils, describing them as the means through which to bring together government, employers, workers and trade unions as part of "a new era of economic cooperation".[19] But whether but these councils would be instituted to win support for Labour policies or to achieve consensus between different interest groups is unclear. Labour may well end up coming to power as a minority government, dependent on the support of other parties. This means it could have to neuter the more radical elements of its economic programme.



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labour and infrastructure

jamie cater, head of policy

As highlighted in our paper *What Would Jeremy Do?*, public ownership is at the top of Labour's agenda for government. It is a flagship policy, popular with voters in opinion polls and symbolic of the party's commitment to radical change, but what is the extent of Labour's ambition in this area?

There are three interesting aspects of the debate over public ownership and how it plays into wider economic policy development. The first is the cost of the changes in ownership – taking into account the coverage of the policies (i.e. precisely what assets are proposed to be taken over by the state) – and how this contributes to the national debt. The second is the question of what comes after the priority areas of rail, mail, energy and water. The third is the party's broader priorities for infrastructure and where this sits alongside the candidates for public ownership.

the cost of public ownership and labour's economic policy

It is worth considering the parameters that Labour has set for public ownership. In many areas the changes are not as drastic as might be first assumed. For example, when the party talks of bringing rail back into public ownership, it refers only to franchised passenger services, not to other areas of the system – it will not be a return to British Rail and the old way of running the rail infrastructure by central government. When it talks of the utilities coming into public ownership, the Big Six will not be nationalised; rather, the it is the transmission and distribution networks that will be run by local and regional boards, with publicly-owned local suppliers entering into the supply market to challenge the big players.

It is undoubtedly true that all of these measures constitute drastic changes in their respective markets, but also represent a slightly more restrained position than some of the public discourse around the policies might suggest. It is also not to say that the party could not become more ambitious and more radical over time, but for now this represents the immediate priorities for an incoming Labour-led administration.

The question of how assets will be valued is a difficult one. Labour has previously indicated that investors may not be compensated at full market value if assets are transferred to public ownership, but this would be highly unlikely to happen in practice. Not only does international law stipulate that compensation should be paid at market value, historic precedent in the UK suggests that nationalisation of assets has usually been compensated at market value, approved by Parliament. It has previously cited the example of Northern Rock as a precedent for full compensation not being issued to investors, but the business was insolvent at the time; the assets in question under Labour's plans would clearly be solvent. Even if Labour is able to make some deductions from compensation payments as it has proposed – which may be questionable – the likelihood is that it would end up paying close to market value at least.

It is true that Labour would not allow Parliament alone should determine the value of the assets; it will be heavily guided by the Treasury, specifically by a dedicated unit that Labour has pledged to establish on taking office. It should be assumed, given Labour's suggestion that it would want to disregard the standard idea of market value and the companies' own suggestions of their value, that the Treasury would essentially calculate its valuation of the assets to be acquired and seek Parliament's approval.

This is of course mitigated by the question of social value, and the prospect of a Labour government paying a premium rather than a discounted rate on the basis that there is a tangible social benefit to bringing the assets under public control. It is not unprecedented for the UK government historically – considering some of the nationalisations of the Labour governments in the 1970s – to pay above market value for assets. The perceived social benefit may provide the political justification for paying above the odds, not forgetting the popularity of the policy itself among the general public.

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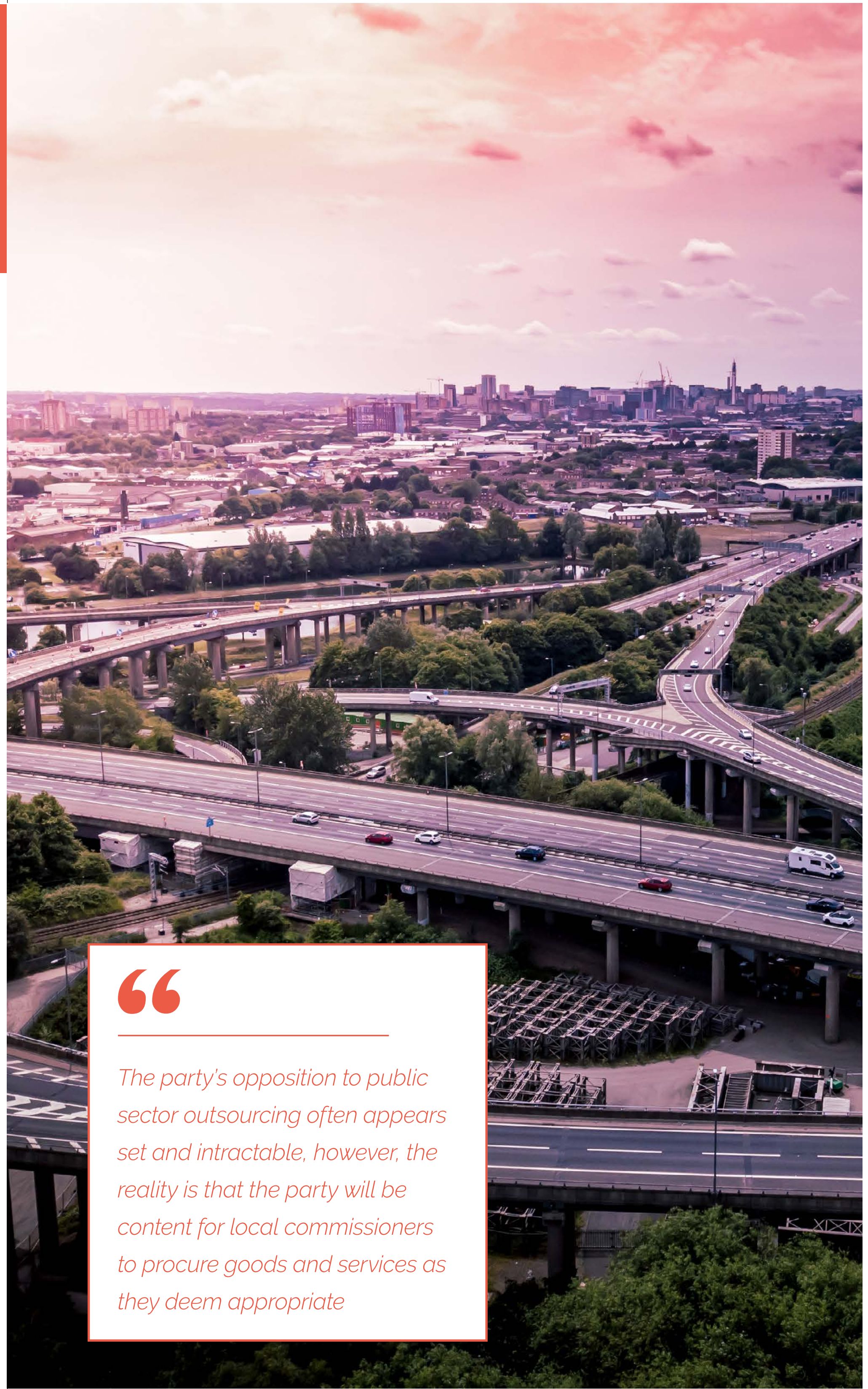

The party's opposition to public sector outsourcing often appears set and intractable, however, the reality is that the party will be content for local commissioners to procure goods and services as they deem appropriate

What this means for Labour's wider economic agenda is also difficult to discern. It is without question a political priority, but it will be difficult to square with It is likely that a Labour government could pass the changes in ownership without breaking its commitment to eliminating the deficit, but the national debt would almost inevitably rise as a consequence. However, whether McDonnell as Chancellor would be sufficiently concerned about the consequences for the UK's position in sovereign debt markets to row back on the policy appears unlikely.

other targets and public sector outsourcing

Labour's rhetoric around 'privatisation' of parts of the public sector appears to suggest that a harsher approach to for-profit providers of public services would immediately be at risk under a new government. Whether calling for an end to the 'privatisation' of the NHS, the creation of a National Education Service or the 'end' of local authority outsourcing of services for vulnerable people, the party's opposition to public sector outsourcing often appears set and intractable. However, the reality is that while there is a strong preference in the party for services to be delivered in-house and guidance will be developed to formalise this, very little will be directed by central government; the party will be content for local commissioners to procure goods and services from the private sector as they deem appropriate.

It is worth considering how Labour might extend the criteria it develops for LSE listings to public sector outsourcing. Environmental impact, as well as likely considerations around minimum pay and employment practices, could form an important part of how central and local government redesign their approach to procurement practices. A more local approach – explicitly favouring suppliers with a local footprint, and demonstrating the potential benefit to the local community and labour market – will also be a prominent part of this. In this as well as other areas, social value is likely to prove to be an important part of the party's strategy.

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> The clear priority is greater public investment in social housing.

infrastructure spending

Given the scale and ambition of Labour's commitments in relation to public ownership, there is likely to be little political or financial space for the party to consider additional large infrastructure projects from central government. In areas such as transport and energy, many areas simply fall behind the debate over ownership in the list of priorities. The clear priority is greater public investment in social housing, which will be primarily the responsibility of local authorities and housing associations.

In January 2019, the party published a strategy – devised by researchers at Sheffield Hallam University – for regional economic development, *Strong Economies, Better Places*. This re-frames the party's position on the industrial strategy to a more decentralised approach, although it focuses mostly on a small number of national policies, such as the creation of a national investment bank and a national transformation fund. The likely focus of these will be on areas of the country with high levels of unemployment and social deprivation, but again much of the decision-making is likely to be made at a local rather than national level in terms of the development of local infrastructure.

The proposed institutional change will also impact how infrastructure investment is considered. The planned re-write of the Treasury's Green Book will introduce new rules around how value for money is determined from public investment and, as noted above, the party's intention is for the Bank of England to adopt a more proactive role in relation to the industrial strategy and infrastructure. Businesses should be mindful of how the potential new powers for the Bank over capital allocations and political decision-making could affect how a Labour government thinks about future spending on infrastructure projects.

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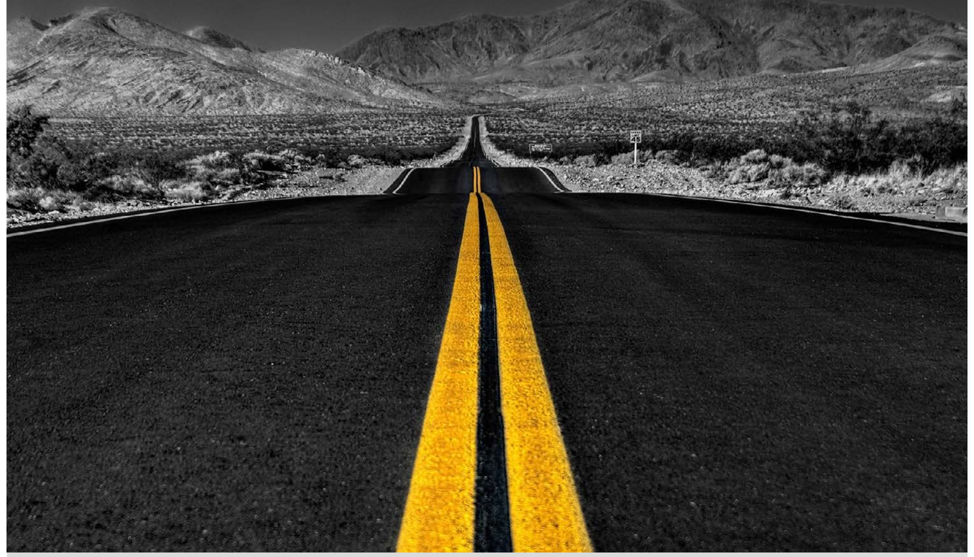
conclusion: capitalism overthrown?

There is little doubt that Labour's plans would amount to a significant shift in the UK's political economy. The scale of the party's ambition for government is undeniable, and much of the policy framework it has proposed is popular with the electorate. However long Corbyn and McDonnell remain at the helm of the Labour Party, the political shift that has occurred within the party over the last four years is likely to last beyond their leadership.

However, to interpret Labour's economic policy as driven by an uncompromising Marxist ideology is to misunderstand McDonnell as a politician. There is not only more flexibility in the party's positioning than is often assumed, but the party's economic policy is largely subservient to its social policy. Consideration of social value is vital in understanding how the party's policy positions are being developed, whether in public ownership, workers' rights or increases in public spending in specific areas.

A Labour government's purpose will not be to overthrow capitalism, but to directly address perceived market failures, overturn reductions in public expenditure and guarantee workers' rights. It is a big step change from recent economic consensus, and while it is not the fundamental system change that the party's rhetoric might sometimes suggest, there are undoubtedly risks to consider for businesses and investors.

> *A Labour government's purpose will not be to overthrow capitalism, but to directly address perceived market failures, overturn reductions in public expenditure and guarantee workers' rights.*



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