



Overview

—Nov 19

Labour's Inclusive Ownership Fund (IOF) proposal has generated significant debate in recent months. Common Wealth has analysed the potential impact of a feasible version of the policy and the distribution of its benefits, a proposal we have advocated for in the past, along with NEF and The Democracy Collaborative.^[1] The critical point is that previous analyses were based on the assumption that a company's IOF would have a right to dividends from a company's global, rather than its UK-specific, economic activity.

Examining the Inclusive Ownership Fund

By focusing instead on UK economic activity, our analysis substantially addresses two of the main existing criticisms of the Fund proposal: that it hits some companies disproportionately for global economic activity with knock-on effects for UK pension wealth, and that the vast majority of the revenue goes to the state, rather than workers, due to the low individual cap. As set out in the table below, these criticisms are significantly weakened under a UK-based IOF, all while retaining the core thrust of democratising wealth and power within the company.

Table: Effects of Common Wealth proposal for IOFs to have rights to UK-based economic activity

Year and IOF share	2024 - 5%	2029 - 10%
Total 'pot' between workers and society	£2.7bn	£5.8bn
Worker 'pot'	£2bn	£3.6bn
Public 'pot'	£700bn	£2.2bn
Average pay-out	£181	£295

Note: The above results assume a £500 cap. The methodology is briefly described at the bottom of this note.



Transforming the company

—Nov 19

The UK's poor performance on investment, productivity and inequality stems in part from how – and in whose interest – British companies are owned and controlled. Shifting structures of shareholding – with shares of public companies increasingly held by institutional investors^[2] and concentrated ownership of private companies – has combined with the assertion of shareholder primacy in corporate governance to transform the behaviour of the company. This process has privileged the interests of shareholders over labour. Over time, this has resulted in increased inequality and under-investment, as the imperative of maximising shareholder value has come at the expense of rising real wages or investment.^[3] It has also generated a deep imbalance in decision-making. Labour has very little ability to influence corporate decision-

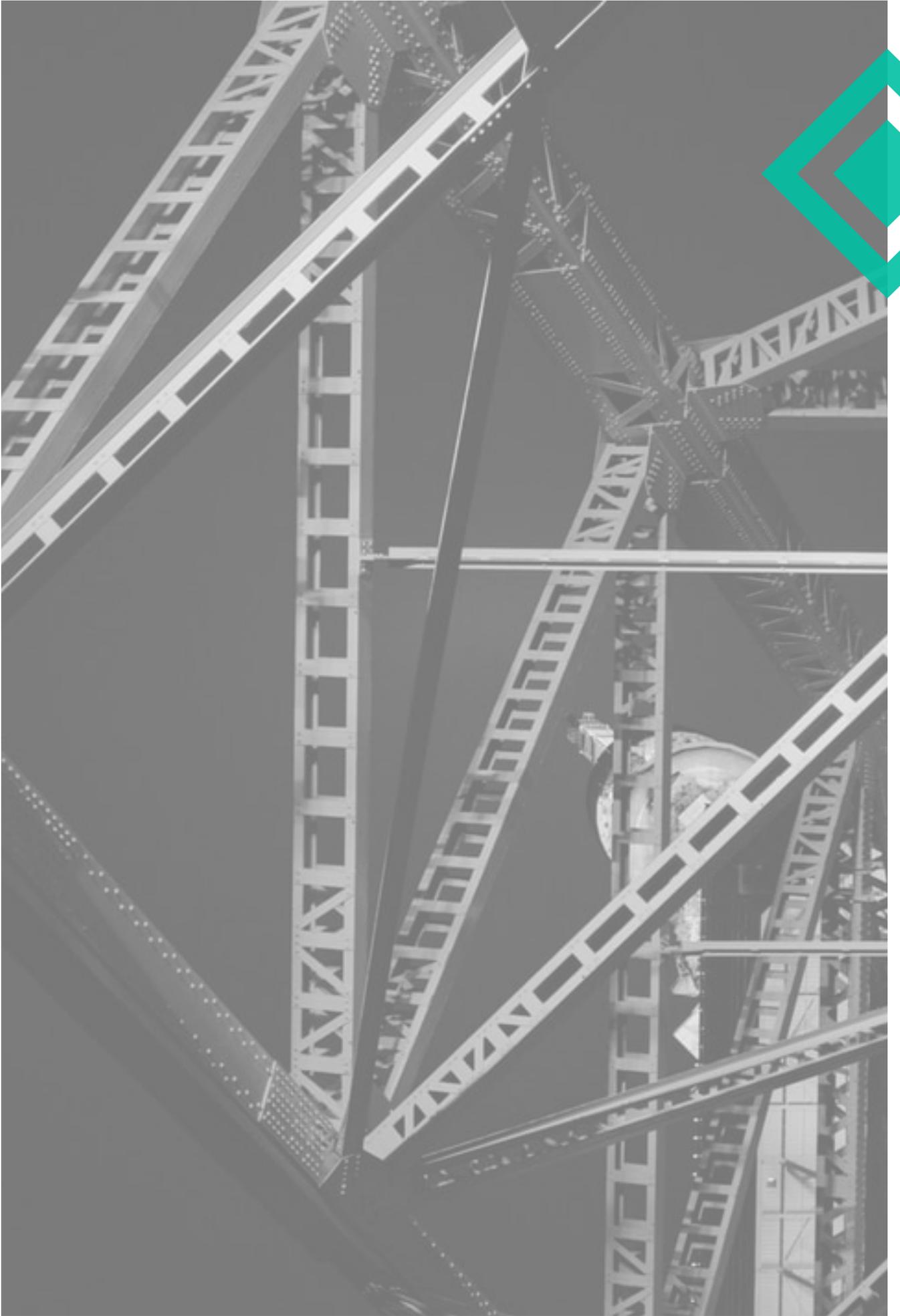
making or strategy, especially relative to distant institutional investors or large shareholders, with too few workers having a genuine stake and say.

Tinkering won't address these imbalances, as the *Financial Times* acknowledged only a few weeks ago^[4]. To build an economy that is democratic and sustainable by design, we need to transform how the company operates and for whom. Fundamental to this must be a deep institutional turn in ownership to redistribute not just wealth and income, but power and control within the firm.

The IOF proposal is one means to do this. First proposed in a 2018 NEF paper and supported by Common Wealth, a version of the Fund idea was adopted by Shadow Chancellor John McDonnell at Labour Party conference in 2018, and subsequently taken up by Bernie Sanders's presidential campaign. At its core, the Fund idea seeks to democratise the company by redistributing economic and political rights away from external shareholders and executive management toward the workforce as a collective. The proposal may appear radical but its intention is not. It simply aims to ensure

decision-making and the wealth generated by the company is shared more equally between all stakeholders within the firm: external shareholders, management, and workers. The truly radical position is the status quo, whereby workers are not guaranteed a fair stake and say in the companies they contribute so vitally to.

The policy's announcement has led to debate over its effects. Our version of the policy can be deployed through reform of existing rules around share issuance. Current investor principles of remuneration already allow for companies to issue new shares to employees – through executive remuneration and all-employee share schemes – up to 10% of the issued ordinary share capital in any rolling 10 year period.^[5] However, given inequalities in power within the company, new shares issued to employees disproportionately benefits senior executive management. This proposal therefore redraws existing principles of share dilution in a progressive direction, building a collective stake for the workforce over a finite period of time.



Impact of a UK rather than global scope

—Nov 19

Our version of the policy would limit the IOF share of dividend income to UK-economic activity. This would be distributed to the workforce as a whole, ensuring they benefit directly when their company does well.

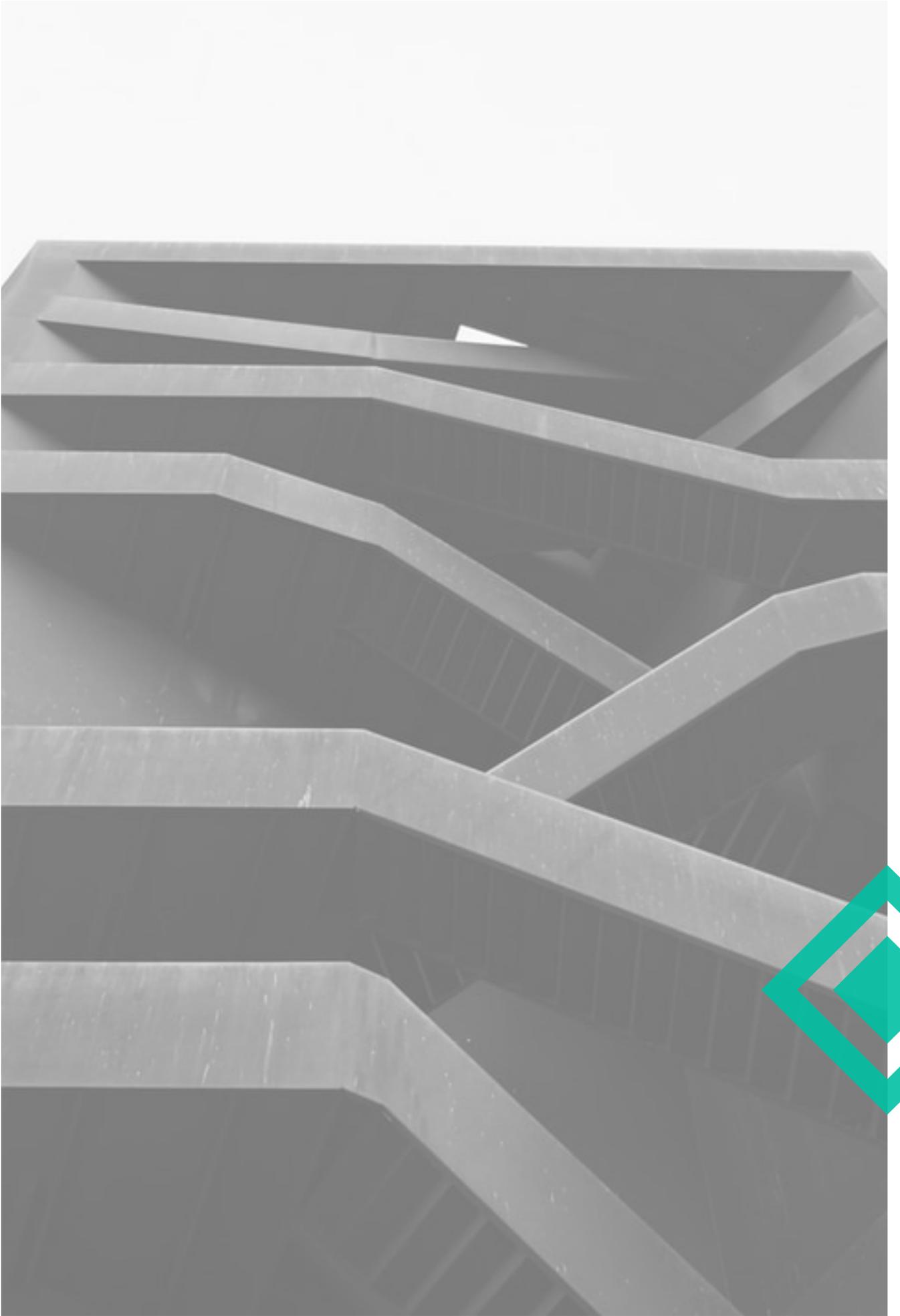
The IOF having rights to UK-based economic activity, rather than global activity, would have important consequences for the impact of the policy. By way of comparison, Clifford Chance's analysis, which assumed a global scope, estimated the total dividend payout to the IOF to be £10.7bn, relative to £5.8bn estimated here (for a 10% stake).^[6] Given the scope of economic rights is reduced, the effect on shareholders will, mechanically, also be reduced.

Another key difference between a national and international scope, provided a cap is set, is that the proportion of total dividends going to the government is significantly reduced in the national scope version. This is primarily based on the differential treatment of FTSE companies under a UK or global based IOF. Last year, the top five FTSE companies gave out £33bn in dividends.^[7] In other words, these five firms would contribute nearly £3.3bn to the total IOF pot under an international scope. In addition, these five firms only have roughly 60,000 UK-based employees.^[8] Without a cap, and with a 10% IOF stake, this would work out at roughly £55,000 per employee, a highly unequal outcome. With a cap, the worker share would be less than 1% of the total IOF of these companies, with the remaining 99% going to the state.^[9]

By contrast, a UK-activity based approach would avoid concentrating the policy's effect on such a small number of firms. By tying the policy to UK activity rather than UK headquarters, it would significantly mitigate the incentive on firms to relocate, as the policy's cost would be proportional to UK activity, and could not simply be avoided by

changing a company's registered headquarters. It would also be fairer as UK workers would share in the rewards most directly linked to their own work, rather than that of their international colleagues.

Linking the IOF stake to UK activity would also be administratively simple, as HM Revenue and Customs could use the same definitions and principles to calculate the IOF stake as it uses to determine UK activity for the purposes of calculating UK profits and UK corporation tax. While, of course, there are issues with the current framework and corporate tax avoidance is a definite concern, any improvements made to the framework could apply equally to estimating the IOF stake as to corporation tax receipts. Though the corporation tax information did not disclose the exact number of large firms, recent business population estimates suggest, that if it were implemented today, there would be 7,500 large firms employing 10.7m people who would be covered by an IOF^[10]. We therefore believe a UK-based model is the most effective design of the Fund.^[11]



Moving the debate onwards

—Nov 19

There are, of course, still important questions of design to explore and debate, but our analysis suggests a viable roadmap toward building more inclusive, democratic and productive companies, and one we hope all political parties will consider.

Common Wealth is publishing further details of its design of the ownership fund proposal shortly, in partnership with The Democracy Collaborative. This will explore the design and potential implications of this policy in more detail, as well as exploring similar related options such as the Fund having income rights based on profit-sharing, with a mechanism akin to the Employee Ownership Trust, which allows tax-free bonuses to be paid to beneficiaries out of company profits. This bonus could be paid in relation to IOF shares, and could help mitigate for the fact that certain firms may not regularly pay-out dividends. By attaching the payment to profits, rather than

dividends, workers would always be rewarded where their firms performs well. Regardless of the design, the impulse of our proposal is clear: the company is a vital institution, its rights and privileges publicly defined, and to ensure it best serves prosperity and justice, rethinking who controls it, how it operates, and who has a claim on its surplus, is a critical question.

Note on methodology

To estimate a UK-based economic activity IOF, we relied on HMRC's Corporation Tax receipts and the Office for National Statistics's Business Population Estimates.^{[12][13]} From the Corporation Tax receipts, we approximated post-tax profits.^[14] At a high-level, the UK corporation tax regime is based on the principle that only profits derived from UK activity should be subject to UK corporation tax. In practice, the rules are a little more complicated, but we are here assuming that the same rules currently applicable to the calculation of UK corporation taxes would apply to the calculation of the IOF share. In other words, it would apply to both UK and non-UK resident companies. With these estimates of UK profits, we approximate the associated UK dividends, using a relatively conservative dividend to post-tax profits ratio of 52.8%.^[15] This allows us to estimate the total IOF pot. To approximate the distribution of that pot between workers and the state, assuming a £500 cap, we estimate the (pre-cap) payouts at the sector level and

redistribute any excess from the worker pot to the state pot.

The final stage of the analysis was to project existing data forward. In the interest of both simplicity and transparency, we use the Office for Budget Responsibility's most recent forecasts of population and profits to approximate the sector-level pay-outs in future years, assuming no behavioural change. We then use their GDP deflator to ensure all our estimates are in 2019 money.

In short, our methodology provides a reasonable and transparent 'first pass' estimate of the revenue implication of a UK-based IOF. The main drawback to our analysis is that it can only provide an upper-bound on the sectoral worker share since firm-level profits per worker can differ from sector average. However, as firm-level corporate tax records aren't available, it wasn't possible to do the analysis at the firm-level. In practice though, any government implementing this version of the IOF would have access to firm-level tax receipts and could estimate the worker/state share more precisely.

About the authors

Mathew Lawrence is director of Common Wealth.

Loren King is a consultant at Frontier Economics but undertook the research and writing in a personal capacity.

References

[1] Gowan P and Lawrence M (2019) *Democratic Ownership funds: creating shared wealth and power*. Common Wealth / The Democracy Collaborative.

<https://common-wealth.co.uk/Democratic-ownership-funds-creating-shared-wealth-and-power.html>

[2] ONS (2017) *Ownership of UK quoted shares 2016*

<https://www.ons.gov.uk/economy/investmentpensionsandtrusts/bulletins/ownershipofukquotedshares/2016> Ownership of UK quoted shares: 2016

[3] IPPR (2018) *Prosperity and justice: A plan for the new economy - The final report of the IPPR Commission on Economic Justice*. <https://www.ippr.org/research/publications/prosperity-and-justice>

[4] “How to build a more responsible corporate capitalism” (2019) *Financial Times*. https://www.ft.com/content/8b282346-eea3-11e9-85f4-d00e5018f061?e_mailld=5da6e1bd76a585000460a044&segmentId=27d43a35-5735-2068-096c-93634f74e431

[5] The Investment Association (2018) *The Investment Association Principles of Remuneration*. <https://www.ivis.co.uk/media/13874/Principles-of-Remuneration-Nov-2018-FINAL.pdf>

[6] And even then, their analysis only included publicly listed firms and the top 350 private ones. By contrast, this analysis includes *all* large firms.

[7] According to Link Asset Services’s Dividend Monitor. <https://www.linkassetservices.com/file.axd?pointerid=5c48a2118bcbe70e4068f57b&DocumentName=UK%20Dividend%20>

[Monitor%20Q4%202018.PDF](#)

^[8] For many global firms, UK employee numbers are not readily available so we used their gender pay reports. As these did not always have specific numbers, the above estimate is only approximate. For the top five, the reports are available [here](#), [here](#), [here](#), and [here](#).

^[9] Clearly, with a cap at £500, there will still be some high-productivity firms for which the share of the IOF pot going to the state will be higher than the share going to workers. However, the change from international to UK scope makes it quite unlikely that this will be a 99-1% split. In addition, workers in higher productivity firms are already likely to be higher earners. The cap can therefore help ensure the policy is more progressive.

^[10] ONS (2018) Business population estimates 2018. <https://www.gov.uk/government/statistics/business-population-estimates-2018>

^[11] Corporate tax avoidance can be addressed through a range of measures, including a General Anti-Avoidance Rule.

^[12] We made an FOI request to obtain large firm corporation tax receipts by sector. This request was made on April 24th 2019, the Freedom of Information reference is: FOI2019/00990.

^[13] See the detailed tables here: <https://www.gov.uk/government/statistics/business-population-estimates-2018>

^[14] At a high-level, the UK corporation tax regime is based on the principle that only profits derived from UK activity should be subject to UK corporation tax. In practice, the rules are a little more complicated, but we are here assuming that the same rules currently applicable to the calculation of UK corporation taxes would apply to the calculation of the IOF share. Note also that firms can apply for deductions to their CT bills (e.g. R&D tax-credits), so their 'effective' CT rate could be below the headline rate. In practice, this means our estimate of post-tax profits, and therefore, of the IOF overall pot, is likely to be conservative.

^[15] In their analysis of the IOF scheme (published in September 2019 but no longer available online), Clifford Chance assumed roughly 50% of pre-tax profits were paid out as dividends. This works out at 62% post-tax, so our estimate is slightly more conservative.

