

# Alternatives to Austerity

INVESTMENT, INNOVATION AND RECONSTRUCTION

Dexter Whitfield  
February 2014

Report prepared with the assistance of Don Dunstan Foundation and Public Service Association of SA

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Informing Decisions





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Published February 2014.

ISBN: [978-0-9923617-5-4]

Suggested citation:

Whitfield, D. 2014. *Alternatives to Austerity: Investment, Innovation and Reconstruction*, Adelaide: Australian Workplace Innovation and Social Research Centre, The University of Adelaide.

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## KEY FINDINGS AT A GLANCE

### **The alternative economic and political strategy to Austerity should consist of:**

- Economic stimulus strategies, industrial investment and innovation, the reconstruction of the state and public services, more rapid reform of banks and financial markets, radical reduction in corporate welfare and an increase the labour share of national income are a viable and sustainable alternative to austerity measures.
- Financial reforms, progressive taxation, a Financial Transactions Tax, increased corporate and high-earner tax rates, a big reduction in tax avoidance and a radical reduction in corporate welfare subsidies and grants would provide enormous new resources for investment and innovation. Plus, new European Union, national and local bonds could further increase investment programmes.

### **Economic stimulus and investment**

- Public infrastructure investment increases growth and output, reduces the cost of production, increases productivity, improves access, enhances the quality of services, creates jobs and generates further economic activity and jobs in local and national economies.
- Public spending on infrastructure, goods and services has a much larger multiplier effect than personal and corporate tax cuts.
- European Union and national economic stimulus strategies should stimulate growth and jobs by targeting sectors such as renewable energy; the production and dissemination of knowledge and application of information and communications technology; health, welfare and caring; sustainable solutions to food, public transport, construction, energy, water and waste.
- New industrial strategies and more proactive and interventionist government agencies are needed to increase and target research and development to sustain innovation.
- Public investment in renewable energy projects and retrofitting homes and buildings could advance a clean energy economy, reduce emissions, stimulate economic growth and jobs and improve the quality of life.
- Alternative economic strategies should focus on reducing inequalities by extending and improving universal health, social care, education, childcare, social security, and access to good quality affordable housing.
- International cooperation is essential to tackle financial market reforms, tax avoidance, collective bargaining and to challenge the purpose and scope of free trade agreements currently being negotiated.

### **Reconstructing the state and public services**

- The closure of the pathways to privatisation would have an immediate effect at relatively low cost. Measures should include in-house Service Innovation and Improvement Plans; a ban on transfers of public services to trading companies or social enterprises; an end to public sector market-making activities; phasing out vouchers, direct payments, personal budgets and public sector involvement in the social investment market; and terminating planned Public Private Partnerships and nationalising/buying-out existing projects.
- Representative, participative, accountable and transparent government at international, national and local levels must have a vital role in an alternative economic strategy.



### **Reform of the financial system**

- Debt reduction is a slow process and must take account of increasing uncertainty about economic growth, interest rates, long-term public spending pressures, the effectiveness of financial reform and costs arising from future financial crises.
- More radical and faster reform of banks, shadow banking, credit rating agencies and financial market regulatory regimes is urgently needed.

### **Radical reduction in corporate welfare**

- The corporate welfare system of tax reliefs, subsidies, guarantees and regulatory concessions to business must be radically reduced and redirected to direct public investment. The corporate sector should invest a significant proportion of their cash hoardings in sustainable development projects.
- Reverse the significant decline in corporate income tax rates and the average effective tax rate.

### **Increasing labour share of national income**

- Austerity policies, financialisation, welfare state retrenchment, the growing gap between average wages and productivity increases and declining union density, have led to a reduction in the labour share of national income and increasing inequality.
- The labour share of national income could be increased by a combination of increased national minimum and living wage rates, reduction of the gender pay gap, a cap on excessive financial and business sector salaries, increased trade union membership and collective bargaining, together with policies to create full employment.
- Trade unions, community and civil society organisations must be closely involved in the drawing up of alternative economic strategies to ensure they are comprehensive and fully incorporate their needs and interests.
- Staff/trade union and user/community organisation involvement in the planning, design and delivery of services, workforce development, childcare provision, equalities mainstreaming, good quality pensions and collective bargaining are essential parts of the reconstruction strategy.
- Alternative economic strategies should provide a springboard for the preparation of more detailed visions, plans and strategies for sectors, services, regions and localities that could be integrated into trade union, civil and community organisation and protest movement organising and action strategies.



# 1 THE ALTERNATIVE TO AUSTERITY

This is the third of three briefings examining the impact of austerity policies in Europe and North America (Unmasking Austerity, Briefing No. 1 and Opposing Austerity, Briefing No. 2).

This briefing sets out an alternative to austerity through economic stimulus, reconstruction of public services and the welfare state, faster fundamental reform of banks and financial markets, the elimination of corporate welfare and strategies to increase the labour share of national income.

## 1.1 THE NEED FOR AN ALTERNATIVE

The financial crisis was caused by the failure of markets and deregulation. It was a private sector failure, not a sovereign debt crisis caused by excessive government spending. Neoliberal ideology and values, such as free trade, competition, debt-driven consumerism, tax cuts for the wealthy, deregulation and privatisation, underpinned economic policies and attitudes (Unmasking Austerity, Briefing No. 1).

Austerity policies have led to soaring economic costs, rising unemployment, public sector job losses, cuts to wages, pensions and benefits, closures and business failures, financial crises in towns and cities, foreclosures and house price slump, damage to health, poverty and widening inequality (Unmasking Austerity, Briefing No 1). These are not temporary impacts, because austerity measures are being implemented for a longer period than originally intended and have long-term consequences. Furthermore there is no plan to 'restore' wages and benefits or to reverse the 'reforms' (Opposing Austerity, Briefing No 2).

## 1.2 SHORT-TERM FISCAL STIMULUS INITIATIVES

Virtually all G20 countries had announced fiscal stimulus policies by March 2009. Fifteen planned to increase infrastructure investment, mainly on transportation networks between 2008-2010 (International Monetary Fund, 2009). However, most measures were temporary, short-term and subsequently replaced by austerity policies.

For example, the American Recovery and Reinvestment Act (ARRA) comprised 35% transfer payments, mainly unemployment insurance, 24% tax cuts, 22% for state and local government education and health care, and 19% for infrastructure. The ARRA contributed to GDP each year (2009-2011) and unemployment would otherwise have been up to 1.8% higher. However, the US\$782bn (A\$860bn) programme failed to generate a strong recovery because it relied too heavily on tax cuts as a means of bolstering private spending; household wealth declined dramatically during the recession, which in turn weakened the willingness of households to increase spending; and credit markets were locked up, especially for smaller businesses (Pollin, 2012a).

The 2012 European Union Summit launched a €120bn (A\$180bn) Compact for Growth and Jobs. It comprised €10bn (A\$15bn) capital increase in the European Investment Bank to increase its lending capacity to €60bn over four years, the redirection of €55bn (A\$825bn) unspent EU Structural Funds to tackle youth unemployment and the launch of a pilot phase of Project Bonds to increase investment by €4.5bn (A\$6.75bn) in transport, energy and broadband projects (European Council, 2012).

The Compact was described as *"...full of hot air ....and little more than window dressing for voters and financial markets"* after French President Hollande promised voters a growth pact *"...to counteract Germany's obsession with austerity"* (Der Spiegel, 2012). A later review of progress concluded *"...a half-hearted implementation of the half-hearted EU summit decisions"* (Griffiths-Jones and Kollatz-Ahen, 2013).

These initiatives were limited to fiscal stimulus policies and could not be described as alternative economic strategies.

**New objectives are needed to provide a framework for an alternative economic strategy and reconstruction of the state and public services and to replace the failed neoliberal objectives (see Briefing 1 and Table 1).**

*“Three decades in which market liberals have pushed policies based on ideas of efficiency and claims about the efficiency of financial markets have not produced much in the way of improved economic performance, but they have led to drastic increases in inequality, particularly in the English-speaking world. Economists need to return their attention to policies that will generate a more equitable distribution of income” (Quiggin, 2012).*

**TABLE 1: RECONSTRUCTION OBJECTIVES**

<b>Neoliberal objectives</b>	<b>Alternative economic strategy and reconstruction objectives</b>
Free trade, competition & markets to allocate resources and deliver services and state control of money supply	<b>Economic stimulus, increased public investment, re-industrialisation and innovation policies, closure of pathways to privatisation</b>
Deregulate to create new opportunities for accumulation	<b>Public ownership with re-regulation of financial system and markets</b>
Deconstruct democracy to partnership between state and finance/business and consolidate corporate welfare	<b>Democratic governance, accountability, participation, transparency and minimal corporate welfare</b>
Reconfigure the role of the state to reduce functions and cut taxes	<b>Increase capacity of state to fulfill functions, strengthen welfare state and progressive taxation</b>
Reduce the cost and power of labour	<b>Quality employment and pensions, collective bargaining &amp; trade union recognition</b>

The financialisation, personalisation, marketisation and privatisation of life, resources and economic and social relations must be challenged in the economy, not just in the public sector and welfare state.

## 2 ECONOMIC STIMULUS AND INVESTMENT

This section begins with a summary of four economic strategy proposals.

### **ALTERNATIVE ECONOMIC POLICY FOR EUROPE**

The European Economists for an Alternative Economic Policy for Europe propose that governments should be released from a highly restrictive fiscal policy with higher levels of public spending financed by reversing the repeated tax cuts. The objective should be full employment with decent work. Government deficits should be financed through Eurobonds.

A new industrial policy would consist of a Europe-wide public investment plan for socio-ecological reconstruction to boost European demand; a drive to develop new environmentally sustainable, knowledge intensive, high skill and high wage economic activities; a reversal of privatisations and substantial public-sector support for new

activities at the EU, national, regional and local level; *“...a new trend towards a different kind of 'security' connected with disarmament, greater cohesion and reduced imbalances within the EU and individual countries; and the creation of a major new policy tool for an ecological transformation of Europe”* (EuroMemo Group, 2014).

Targeted sectors should include the protection of the environment and promotion of renewable energy; the production and dissemination of knowledge and application of information and communications technology; health, welfare and caring; sustainable solutions to food, mobility, construction, energy, water and waste (ibid). Funding arrangements should vary depending on the ‘public’ dimension as *“...public funds should go to public investment in non-market activities; public funds and long term private investment combined to fund new “strategic” market activities, such as the provision of public capital for new activities in emerging sectors; public support could stimulate financial markets to invest in private firms and non-profit organisations developing “good” market activities that could more easily repay the investment”* (Pianta, 2013).

*“In all cases, the rationale for financing industrial policy cannot be reduced to the financial logic of the ‘return on investment’. The benefits in terms of environmental quality, social welfare, greater territorial cohesion, more diffused growth at the European level have to be considered, and the costs have to be shared accordingly”* (ibid).

#### NEW PATH FOR EUROPE

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The European Trade Union Confederation’s ‘New Path for Europe’ would invest an additional 2% of European Union GDP per year over a 10-year period. In the short term the plan would increase employment by 1.7m people in 2015 and by nearly 6.0m in 2019. Output in the EU-27 countries would increase by 1.6% in 2015 rising to nearly 5% per annum after five years.

Over a ten-year period the plan could increase Europe’s GDP by €312bn (A\$468bn) and create between 7.2m - 8.8m full-time jobs. It would increase tax revenue by €83bn (A\$124.5bn), social security contributions by €45bn (A\$67.5bn) and make a €16bn (A\$24bn) saving in unemployment benefit. It would save €300bn (A\$450bn) in fossil fuel imports. The initiative could be financed through the European Investment Bank, or a new body, via increased share capital and the issue of long-term bonds to take advantage of *“...the large volumes of saving both within and outside the EU seeking secure investment opportunities”* (European Trade Union Confederation, 2013).

#### MARSHALL PLAN FOR EUROPE

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The Marshall Plan for Europe would focus *“...investments in sustainable power generation, in reducing energy consumption, in sustainable industries and services, in training and education, in research and development, in modern transport infrastructures, low-emission cities and municipalities”* (Confederation of German Trade Unions, 2012).

The 10-year plan would seek to eliminate the need for fuel imports in the long term and achieve large reductions in CO<sub>2</sub> emissions in Europe. The plan proposes direct public sector investment, investment grants for companies and incentives for consumer spending. It would be financed through a new ‘European Future Fund’ which would issue ‘new deal bonds’ to attract the €27,000bn (A\$40,500bn) cash assets in Western Europe. Interest payments on the bonds would be funded from the planned Financial Transactions Tax.

#### PLAN B FOR UK

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A new public investment agency is similarly proposed in Plan B for the UK, launched by Compass. It calls for a British Investment Bank to invest in low carbon, high unemployment sectors such as housing, transport and renewable energy (Compass, 2011). The government has since launched a Green Investment Bank *“...a feeble and anaemic version of what Plan B suggested”* (Reed, 2012). Plan B calls for a new round of

quantitative easing to invest in Green New Deal projects “...rather than blindly buying up government debt and other assets and hoping that some proportion of the extra cash punted out to the commercial banks gets lent out to productive businesses rather than fuelling speculation and financial intermediation” (Reed, 2012).

Plan B called for the full separation of retail and commercial banking, mixed ownership of the banking sector with a larger role for mutual and co-op banks, and a substantial state-owned sector under democratic control. Labour market reform would include a living wage, reduced pay differentials, and enhanced industrial democracy and comprehensive affordable high-quality childcare.

Reform of the tax and benefit system would provide a basic minimum standard of living in or out of work and higher tax rates for those on high incomes (Reed, 2012). Unfortunately, the ‘social investment state’ proposals in Plan B do not take account of the scope of neoliberal transformation, and the implementation of proposals for a ‘new state that spends better’ could perversely accelerate this process (Whitfield, 2012a).

*“...it is equally important to move beyond an economy of need, in which work is seen as a burden only undertaken under the stimuli of reward or deprivation, towards one aimed at improving the quality of work; that is intrinsically satisfying because it is creative and meaningful” (Radice, 2012).*

## 2.1 INDUSTRIAL INVESTMENT AND INNOVATION

France established a new Bank of Public Investment in 2012 to provide financial support for small and medium-sized enterprises. The €20bn (A\$30bn) capital gives a €20bn (A\$30bn) lending capacity, €12bn (A\$18bn) for credit guarantees and €10bn (A\$15bn) for equity investment. It incorporates three existing state agencies – FSI, a strategic investment fund, the OSEO fund for small business development and the business lending arm of the Caisse des Depots et Consignations (Financial Times, 2013).

France followed up with a re-industrialisation strategy with €3.7bn (A\$5.5bn) to invest in new technologies in 34 sectors ranging from robotics, renewable energy, medical biotechnologies and electrical transport. Each sector or project has a state appointed ‘industrial officer’ or project leader, mainly chief executives from major French companies. The strategy aims to create 475,000 jobs over ten years (Invest in France Agency, 2013 and Reuters, 2013).

*“There is nothing in the DNA of the public sector that makes it less innovative than the private sector” (Mazzucato, 2013).* The state has played a central role in funding, supporting and development of computers (for example, Apple), the Internet, biotechnology, green technology, pharmaceuticals, aeronautical and space industries and even in research and development in the nineteenth century.

The state should not be limited to “...‘de-risking’ the private sector and correcting ‘market failures’” but should also reap returns from the risk taking. *“Reaping the returns is crucial, because the innovation cycle can thus be sustained over time (with returns from the current round funding the next round – as well as the inevitable losses along the way) and be less susceptible to political and business cycles” (ibid).*

Mazzucato (2013) recommends a large increase in research and development in national innovation agencies, more proactive interventionist approach to green technology innovation together with an increased green budget. These policies would be partly financed by the closure of enterprise zones, the termination of direct transfers to small firms, such as small business rate relief, limit research and development tax credits to actual spending on innovation, and require part of the return on investment financed by the public sector to be returned to government.

## 2.2 CLEAN ENERGY ECONOMY

Economic stimulus policies provide a unique opportunity to take a big step towards a clean energy economy. Government investment and regulatory frameworks in clean energy stimulates economic growth with environmental benefits. It creates more jobs, dollar for dollar, than equivalent spending on road construction, fossil fuel energy projects or tax cuts (United Nations Environment Programme Sustainable Energy Finance Initiative Public Finance Alliance, 2009).

A UK plan to reduce emissions by 80% in electricity, buildings and transport over twenty years could create one million new climate change jobs. A National Climate Service would be established by the government to employ teams of construction workers to refit homes and buildings, engineers to design and build wind farms and to plan, build and operate public transport systems (Campaign Against Climate Change, 2010).

Increased production of renewable electricity would create 425,000 jobs, refitting buildings to make them adaptable to climate change (150,000 jobs), changing transport (325,000), industry and landfill (50,000) and education (50,000). A further half-million jobs would be created in the supply and service industries, plus the new jobs will generate additional employment through increased household spending on goods and services in the local economy. The net effect would be a gain of 1.33m jobs in the economy after 20 years of the programme (ibid).

The net cost of the programme would be about £18bn per annum after taking account of higher tax and social insurance revenue from the new jobs, lower unemployment benefit costs, energy payments and public transport fares (ibid). Some UK local authorities are developing new municipal energy plants that add to the stock of district heating schemes (Hetherington, 2013).

Freiburg and Hamburg (Germany), Aarhus and Copenhagen (Denmark), Vienna (Austria) and Gothenburg (Sweden) are examples of European green cities. Bristol City Council is the first UK local authority to own a wind farm. It will generate electricity to 2,500 households, cut the city's annual carbon footprint by around 5,000 tonnes per annum generate £200,000 (A\$360,000) income (LocalGov, 2013).

In the Republic of Ireland, Tralee Town Council operates a biomass district heating scheme using woodchip from a nearby 55,000 hectares of forest and has made significant fuel bill savings. It originated in a regeneration scheme, was extended to more houses, a day care centre, library and primary school and phase two will include Kerry General Hospital and supply heat to over 7,000 people and public buildings. The Town Council maintains the district heating plant and purchases wood chip through a producer cooperative that created over 100 jobs (Sustainable Energy Authority of Ireland, 2011).

Hamburg plans to re-municipalise electricity, gas and district heating distribution grids when concessions are up for renewal in 2014 and 2016. Since 2007, 44 new local public utilities have been set up in Germany with more than 100 energy distribution network concessions now publicly operated (Hall, 2012). The planned return of water services to public provision in Berlin follows the highly successful re-municipalisation of water services in Paris in 2010.

Many municipally-owned US Public Utility Districts have provided electricity, and often water, for over a century. For example, Sacramento Municipal Utility District generates, transmits and distributes electric power to a 900 square-mile area of California. Residential electric rates were up to a third cheaper than other utilities in the state, 28% of supplies came from renewable resources and nearly 50% came from non-carbon emitting sources (Sacramento Municipal Utility District, 2013).

Although a clean energy economy will retrofit buildings and infrastructure nationally, it must take account of regional equity issues, such as differences in climate and

topography and the disproportionate negative impacts in more fossil fuel dependent regions (Pollin, 2012b).

## 2.3 PUBLIC OWNERSHIP AND PROVISION

Governments should ensure that state owned corporations and public bodies operate to public service principles and management practice, have democratic and accountable governance and continuing training and education on the function, objectives and political economy at all levels of the organisation.

Programmes of re-municipalisation and re-nationalisation could reverse the privatisation of state owned corporations, health and social care, education, public housing, land and public buildings. They could include the termination or buyout of Public Private Partnerships that privatised the design, build, finance and operation of eleven types of public infrastructure (Whitfield, 2010).

Public infrastructure investment is vital for the economy and to improve quality of life. Improving public transport (rail, tram and bus); primary healthcare facilities; public housing; low carbon construction, renewable energy, renovating buildings; integrated multi-use facilities for education, sport and leisure, library, childcare and other community services should be prioritised. Production and supply chains, for example, trains and rolling stock, ICT and other equipment, furniture, goods and services, should be integrated with industrial policies, economic development and employment strategies. A public design initiative would set new standards for the design and planning of public buildings and infrastructure (Whitfield, 2012b).

Austerity policies have highlighted the need for governments to maximise control over natural resources, such as oil and gas reserves and forests. Privatisation also means the potential loss of significant longer-term tax revenue.

## 2.4 WELFARE STATE TACKLING INEQUALITIES

Alternative economic strategies should focus on reducing inequalities, particularly since women, and disabled and elderly women and men in particular, have borne the brunt of austerity measures and widened inequalities. Strategies need to address income and wealth inequality, discrimination in access to services, the restoration/strengthening of legal rights and taxation inequalities.

The welfare state has a vital role in addressing risk and uncertainty through social insurance, income redistribution, public goods and the provision of basic needs. *“Collective risk management through the welfare state helps to stabilize the aggregate economy”* (Quiggin, 2012).

The welfare state must be strengthened with investment targeted to extend and improve:

- Universal health and social care, education and training;
- Universal childcare for all preschool children;
- Universal social security through state and occupational pensions with a responsive benefits system to protect against unemployment and other unforeseen circumstances;
- Access to good quality affordable housing; and
- Public delivery of public goods.

The comprehensive case for universalism is cogently set out in Danson et al (2012).

The EU has favoured indirect taxation on goods and services, but this *“...tends to compound income inequalities: it has a regressive, rather than progressive, effect, especially if basic goods are not exempted, because poorer families spend a higher proportion of their household income on consumption and are able to save less. A more*

effective, long-term solution, to both fiscal modernisation and to social justice, is the establishment of an efficient and fair system of progressive direct taxation, in which the rate of taxation rises in proportion to the level of income. In this area of direct taxation, the EU and its member states have arguably been very poor examples of both principle and practice” (EuroMemo Group, 2012).

Governments should carefully monitor prices, income/loan ratios and the buy-to-let sector in housing markets and consider effective measures, such as increased interest rates and/or control of planning permissions, to prevent further housing and property bubbles, foreclosures, evictions and crash of the construction sector.

## 2.5 THE BENEFITS OF PUBLIC INVESTMENT

There is an enormous amount of economic evidence that public investment has a significant positive effect on private sector productivity – hence growth in average living standards – and increases both output and jobs (Bivens, 2012). Analysis of government purchase multipliers for a large number of OECD countries concluded “...that fiscal policy activism may indeed be effective at stimulating output during a deep recession, and that the potential negative side effects of fiscal stimulus, such as increased inflation, are also less likely under these circumstances.” A one billion dollar increase in US government spending is estimated to create approximately 44,000 jobs (Auerbach and Gorodnichenko, 2011).

Despite different models, evidence, assumptions, economic conditions and time periods there is broad consensus on the output multipliers for different types of expenditure. For example, multipliers range from 0.5 to 2.5 for purchases of goods and services by the Federal Government under the ARRA, 0.4 to 2.2 for infrastructure and 0.1 to 0.6 for a one-year tax cut for higher income people (Congressional Budget Office, 2012).

A guide to specific spending measures is provided by Zandi (2010). A US\$1.00 (A\$1.10) increase in US infrastructure spending is estimated to result in US\$1.57 (A\$1.73) change in real GDP one-year after the spending actually occurs - significantly larger than the multiplier effect of personal and corporate tax cuts – see Table 2.

**TABLE 2: DIFFERENT EFFECT OF SPENDING INCREASES AND TAX CUTS**

<b>Multiplier effect</b>	
One-year \$ change in real GDP per \$ increase in spending or reduction in Federal tax revenue	
<b>Spending Increases</b>	
Temporarily Increase Food Stamps	1.74
Extend Unemployment Insurance Benefits	1.61
Increase Infrastructure Spending	1.57
Issue General Aid to State Governments	1.41
<b>Tax Cuts</b>	
Non-refundable Lump-Sum Tax Rebate	1.01
Refundable Lump-Sum Tax Rebate	1.22
<b>Temporary Tax Cuts</b>	
Payroll Tax Holiday	1.24
Across the Board Tax Cut	1.02
Accelerated Depreciation	0.25

<i>Permanent Tax Cuts</i>	
Extend Alternative Minimum Tax Patch	0.51
Make Bush Income Tax Cuts Permanent	0.32
Make Dividend and Capital Gains Tax Cuts Permanent	0.37
Cut Corporate Tax Rate	0.32

Source: Zandi, M., *Moody's Analytics* (2010)

## 2.6 INTERNATIONAL CO-OPERATION

The European Trade Union Confederation (ETUC) called for increased European co-operation on tax avoidance, evasion and tax havens through comprehensive information sharing and cooperation between national tax authorities and harmonisation of the corporate tax base. Greater cooperation on financial market reform is needed to 'rebalance' the EU's economy and between national authorities, civil services and public services to promote long-term quality public services. The ETUC called for social partners to strengthen social dialogue, collective bargaining and worker participation, particularly in relation to the economic governance process at national and EU level, plus education and training and labour market reform. European social standards should be strengthened to fight precarious jobs and promote decent, quality jobs (ETUC, 2013).

Cooperation is needed to challenge the free trade agreements currently being negotiated – the Transatlantic Trade and Investment Partnership (TTIP) Trans-Pacific Partnership (TPP) and the Canadian Canada-European Union Comprehensive Economic and Trade Agreement (CETA) – to remove or re-write draft clauses on investor privileges, market competition, undermining of standards and rights, compensation and the power shift to corporations (Corporate Europe Observatory, 2013).

An EU alliance of over 50 civil society organisations launched an Alternative Trade Mandate in late 2013 demanding a paradigm shift in EU trade and investment policy. Twelve principles range from food production, jobs and labour rights, climate change, public procurement and democratising the initiation, to negotiation and finalisation of trade and investment agreements (Alternative Trade Mandate, 2013).

## 2.7 BASIC PRINCIPLES

Alternative economic strategies need a framework of principles to prevent policy drift and implementation diversion or failure – see Table 3.

**TABLE 3: PUBLIC SECTOR PRINCIPLES**

Public sector principles
<ul style="list-style-type: none"> <li>• Democratic accountability, participation and transparency with a commitment to user, civil society and employee/trade union involvement in the planning, design, delivery and policy-making processes.</li> <li>• Social justice to eliminate victimisation and discrimination and to eliminate or mitigate adverse impacts and inequalities.</li> <li>• Good quality integrated, responsive and flexible services that meet social and community needs.</li> <li>• Solidarity and collective responsibility through universal provision for health, education, welfare, transport and the environment.</li> <li>• Sustainable development to take account of global, national and local economic impacts, production and supply chains and conserve natural resources.</li> <li>• Climate change policies to reduce emissions, prioritise renewable energy and retrofit homes and infrastructure.</li> </ul>



- Quality employment with good terms and conditions, pensions, equalities and diversity, training, workforce development and the right to organise.
- Evidence-based policy making with economic, social, health, equalities and environmental impact assessment and cost benefit analysis.
- Public goods, infrastructure and services should be designed, financed and delivered by skilled in-house staff.

### 3 RECONSTRUCTING THE STATE AND PUBLIC SERVICES

The benefits of economic stimulus and financial reforms will be limited, and could ultimately be eroded, if national and transnational companies gain increasing power through public sector contracting, marketisation and privatisation of the welfare state. 'Business as usual' will inevitably drive down service and labour standards, further weaken the role of trade unions in the economy, with drastic economic and social consequences.

The core functions of the state must be strengthened – they include democratic governance and civil society; national and international responsibilities; human needs and development; economic and fiscal management; and the regulation of markets, firms and organisations.

#### 3.1 CLOSING THE PATHWAYS TO PRIVATISATION

Neoliberal transformation of public services, particularly in the UK, has created pathways to financialise, personalise and marketise services. They were designed to accelerate the mutation of privatisation to enable core services to be sliced and diced into contracts, transfer assets to trading companies, trusts, social enterprises or voluntary organisations and to impose individual choice mechanisms in marketised services (Whitfield 2012b and 2012c). It is vital to close these pathways to privatisation, to de-commodify services, to improve in-house provision and replace neoliberal public management.

A series of measures to close the pathways to privatisation would have an immediate effect at relatively low cost.

1. Abolish commissioning and re-integrate client and service provision functions with a commitment to in-house provision, would rapidly stem the flow of outsourcing contracts and PPPs. Rigorous monitoring and evaluation of current contracts could lead to terminations and/or buy-outs.
2. Service Reviews and Service Innovation & Improvement Plans should be required in all services with automatic involvement of staff/trade unions and service users/community organisations.
3. Full options appraisals and business cases undertaken before procurement (with in-house options and bids if it proceeds).
4. Terminate the transfer of public services to arm's length trading companies, trusts and social enterprises. The transfer of public services to social enterprises, mutuals or cooperatives is privatisation, irrespective of the ownership model, staff and user engagement, democratic structures and community support. Resources should be redirected to create social enterprises in the *private* sector (Whitfield, 2013a).
5. Public sector market-making, corporate subsidies and other commercialisation activities should cease, with resources redirected to innovation, improvement and the creation of choice within in-house provision.
6. Vouchers, direct payments and personal budgets should be rapidly phased out for all but the high-dependency social care users for whom they were originally designed. Charges for 'additional' services in health, social care and education should be stopped immediately.

7. Public sector involvement in the social investment market with venture capitalists, social bonds and payment by results should cease. Innovation within the public sector could achieve the same objectives with greater public benefit.
8. Terminate planned infrastructure Public Private Partnerships and buyout or terminate operational projects. The risks, costs and benefits of economic development, housing and regeneration partnerships should be re-assessed.
9. A Living Wage introduced in all sectors together with reduced pay differentials, defined benefit pensions safeguarded, affordable childcare and trade union recognition and collective bargaining rights.
10. Contractor and consultant bids must be rigorously assessed to determine quality standards and economic, social, environmental and equality impacts and the 'whole contract price' and community cost.

Public bodies will face strident opposition from corporate and financial interests, business and trade bodies and right-wing policy organisations that will attempt to undermine and challenge their legality. Contractors such as Veolia, IBM and Serco are almost certain to react negatively when the flow of public sector contracts starts to decline.

These measures need to be embedded through fundamental long-term changes, such as stronger regulatory frameworks and new public service management which centres on democratisation and participation, public planning, new innovation and improvement strategies and flatter accountable organisational structures.

### 3.2 PUBLIC SECTOR INNOVATION

Public sector principles and values provide a framework to develop public sector innovation (see Table 3). New methods of service delivery could require changes to working methods, new equipment and/or digitisation, staff redeployment and/or retraining and the development of options/choices within public provision. New and expanded services could address unmet needs or respond to market failures. Organisational innovation might include flatter management structures and team working or the formation of new sections/teams to undertake specific tasks. Democratic innovation could widen involvement in the policy making process or strengthen scrutiny and review by seeking written and verbal evidence from community organisations and trade unions.

Financial innovation could pool budgets, increase income generation and find new ways to raise public finance, such as bonds. Access innovation could address inequalities in service design and delivery. Workforce development innovation could range from new training and learning programmes to cross cutting service and boundary skills.

Service user and employee involvement, accountability, transparency, dialogue and negotiation are essential to build in-house capability, so that innovative ideas are part of a continuous development process in community needs analysis, service reviews and service improvement and innovation plans.

The priority must be to embed public enterprise and innovation at all levels of government. The ideology must be challenged that innovation and 'entrepreneurialism' only has value when private and third sector organisations seek to hive off functions and services to create 'mixed markets' and thus effectively dismantle the public sector and welfare state.

### 3.3 DEMOCRATIC GOVERNANCE, ACCOUNTABILITY, PARTICIPATION AND TRANSPARENCY

Representative, participative, democratically accountable and transparent government at national, regional and local levels must have a vital role in reconstruction. Improved

integration of functions and services, real innovation and aligning services to meet social need are direct outcomes of participative and accountable governance.

Social justice strategies should seek to eliminate victimisation and discrimination, and to eliminate or mitigate adverse impacts and inequalities; quality integrated services of a good standard, responsive and flexible that meet social and community needs through in-house provision; universal provision available for all unless specifically targeted; sustainable development to take account of global, national and local economic impact, production and supply chains, and to conserve natural resources.

### 3.4 QUALITY EMPLOYMENT AND COLLECTIVE BARGAINING

Staff/trade union and user/community organisation involvement in the planning, design and delivery benefits the quality of services, jobs, innovation and the effectiveness of services. A large volume of studies has found a direct correlation between the quality of employment and the quality of service in public services and service industries. For example, job satisfaction has a significant impact on service quality and, ultimately, on organisational effectiveness in a service organisation (Snipes et al, 2005); linking employee satisfaction to customer satisfaction and perceived service quality (Brown and Lam, 2008); sustaining good working conditions for nurses is crucial to increase retention, enhance performance and productivity and promote safe nursing care (Almalki, 2012).

A direct and positive relationship was found between employee satisfaction and the quality of hospital patient experience (Peltier et al, 2009). Higher employee engagement levels improved the quality of care and increased patient satisfaction, increased productivity, improved relationships with management, reduced job stress, increased employee satisfaction and increased retention; and lowered employee recruitment, retention and training costs and possibly lower costs in the delivery of patient care.

Workforce development, childcare provision, equalities mainstreaming, good quality pensions, trade union representation, collective bargaining and facility time together with service and workplace democracy are an essential part of the reconstruction strategy.

### 3.5 PUBLIC FINANCE AND FISCAL CRISIS OF CITIES

Governments must have the resources and ability to fund, plan, provide and regulate for the medium and long term, taking account of generational interests, innovation and transformation of the economy, redistribution, and the need to legislate and enforce regulations, protect rights, advance a social justice agenda and protect the environment. For example, a series of UK tax measures could provide £85.2bn (A\$153.4bn) revenue annually by reducing tax avoidance, a Financial Transaction Tax, restoring corporation tax to 28%, scrapping higher rate pension tax relief and a series of other measures (Compass, 2013).

*“Tax systems around the world have become steadily less progressive since the early 1980s. They now rely more on indirect taxes, which are generally less progressive than direct taxes, and within the latter, the progressivity of the personal income tax has declined, reflecting most notably steep cuts in top marginal tax rates” (IMF, 2013b).*

Progressive direct taxation, in which the percentage tax rate increases as income rises, has an important role in promoting social justice. The breadth of the tax base is equally important. However, the move towards reduced corporate and personal income tax rates, whilst increasing taxes on goods and services, is regressive. A user-pays taxation model will prove much more expensive than public provision through general taxation. It is inequitable, regressive and significantly reduces collective provision and hastens the demise of public services and the welfare state.

A new EU investment programme, the Investment-led Recovery and Convergence Programme, co-financed by bonds issued jointly by the European Investment Bank (EIB) and the European Investment Fund (EIF), would invest in health, education, urban renewal and green technology and power generation (Varoufakis et al, 2013). Borrowing should be 'europeanised' and not count towards national debt – the EIB has issued bonds since 1998 without national guarantees. The authors also propose a Limited Debt Conversion Programme in which the European Central Bank would offer member-states the opportunity of a debt conversion for their Maastricht Compliant Debt (up to 60% of GDP) and an Emergency Social Solidarity Programme to guarantee access to nutrition (based on the US food stamp programme) and basic energy needs (ibid).

It is vital that local and regional public bodies, collectively and/or individually, are able to finance investment to complement EU and national programmes. Municipal bond agencies have been established in Sweden and Finland and an agency is being developed in the UK after the Coalition government suddenly hiked Public Works Loans Board (the main source of local authority borrowing) interest rates in October 2010 (Local Government Association, 2013).

The fiscal crisis confronting many, particularly US, cities, urgently require government action and support. The solution cannot be punitive and be left to the market forces that had a major role in creating the problem and to the narrow exploitative interests of vulture funds. Detroiters Resisting Emergency Management have demanded the termination of interest rate swaps with Wall Street banks and repayment; mandatory collection of local income tax; increased state-wide revenue sharing; cancellation of corporate tax relief in economic incentive programmes; and comprehensive city and neighbourhood economic development plans (<http://www.d-rem.org>). Despite claims to the contrary, Detroit's public pension funds are well funded by national standards (Long, 2013).

Fiscal challenges are expected to continue for many more years (Pew Charitable Trusts, 2013) and whilst increasing sales and income tax revenue is important, more fundamental action is needed, for example, to address continued de-industrialisation, city planning and economic development and the continued fragmentation of local government by the privatisation of public education.

### 3.6 DEBT REDUCTION AND RESTRUCTURING

Additional publicly financed investment may increase public debt in the short-term, but it will create economic benefits that will ultimately reduce national debt in the long-term. It is vital to challenge the demands of right wing deficit hawks for governments to adopt a rapid debt reduction strategy. It is important to reduce public debt, *"...although it will inevitably be a slow process"* (IMF, 2013b).

The average public debt ratio in advanced economies is expected to stabilize in 2013–14 at slightly below 110% of GDP, 35 percentage points above its 2007 level. *"Simulations show that maintaining the overall budget at a level consistent with the IMF staff's medium-term advice would bring the average debt ratio to about 70 percent of GDP by 2030, although in a few countries it would remain above 80 percent"* (IMF, 2013b).

Debt reduction must take account of increasing uncertainty about economic growth rates, interest rates, and long-term public spending pressures.

Faster growth is an important route to reduce debt. *"...a country with a debt ratio of 100 percent of GDP could reduce its debt by 30 percent of GDP in 10 years with one additional percentage point of potential growth. This could eventually give rise to a virtuous circle in which lower debt levels would raise potential growth, further facilitating debt reduction"* (ibid). Progressive direct taxation could also help to reduce debt. High inflation would erode the real value of the debt, but would have economic and social costs.

Debt restructuring is another option. The 2012 Greek debt restructuring led to a €100bn (A\$150bn) transfer from private creditors to Greece, corresponding to 50% of GDP in 2012. Although “...the Greek debt restructuring approach can be useful in specific cases, but it falls far short of providing a template that could be a permanent fixture of the European financial architecture” (Zettelmeyer et al, 2013).

Iceland has launched a €900m (A\$1,350m) mortgage debt relief programme with a maximum limit of €24,000 (A\$36,000) for 100,000 households over a four-year period. In addition, employees will be able to redirect a supplementary pension, usually 2%-6% of wages, to pay off mortgages for a three-year period, free of tax (News of Iceland, 2013). The government estimates that mortgage holders who benefit from principal reduction and tax exemptions could reduce their mortgage principal by up to 20% by 2017 (Fitch Ratings, 2013). The IMF believed Iceland had “...little fiscal space for new measures and that across-the-board measures are costly and may not provide sufficient relief to households in most distress” (IMF, 2013c). The programme “...appears fiscally neutral” (Fitch Ratings, 2013).

The debt relief programme will be funded by a levy on Iceland’s failed banks (debts now held by hedge funds) and the three new banks, which acquired their loan portfolios priced at a value that took account of need for write-downs (see Briefing No. 1). The previous government had introduced a moratorium on foreclosures, rescheduled payments, restructured debt and wrote-down mortgages to 110% of household assets for the most indebted households (IMF, 2013c).

The International Citizen Audit Network is supporting Citizen Debt Audits in several countries to analyse the origin, composition, management and impact of public debt to identify illegitimate debt under the banner of ‘We don't owe! We won't pay!’

## 4 REFORM OF THE FINANCIAL SYSTEM

The reform of financial markets and institutions is essential to ensure alternative policies are effective and sustainable. Although some financial reforms have been implemented, much remains to be achieved five years after the crash.

The European Stability Mechanism (ESM) was established by Eurozone member states in 2012 to fund future financial crises and bailouts, replacing the temporary European Financial Stability Facility, and can lend up to €500bn (A\$750bn). The ESM raises funds by issuing short-term securities and long-term debt. It provided €41.3bn in 2012-2013 to the Spanish government to recapitalise the banking sector and €4.5bn to Cypress to recapitalise and restructure the two largest banks (<http://www.esm.europa.eu>).

### 4.1 REGULATION AND REFORM OF BANKS

New global banking regulations (Basel III or Third Basel Accord) are being phased in between 2013-2018 that require banks to be more resilient to financial shocks, improve risk management, governance and transparency. Banks are required to increase capital reserves to 3%-7% of risk-weighted assets. The regulations are also intended to significantly reduce off-balance sheet financing, one of the causes of the financial crisis.

Banks buy and sell stocks, bonds and other securities on behalf of clients. New ‘Volcker’ rules take effect in April 2014 and will limit their ability to trade their own cash, restrict investment in high-risk hedge and private equity funds and impose compliance obligations.

Questions remain about the effectiveness of these regulations. There are concerns about how banks define assets, measure the risk of losses, determine what is off-balance sheet gross or net and the potential for gaming capital requirements. Much depends on how

the regulators interpret and enforce the regulations (Wall Street Journal, 2013 and Brunnsden, 2013). The complexity of the new regulations – Basel III was 616 pages and the Volcker rules over 900 pages – led Andrew Haldane, Bank of England to conclude “...we moved from what was effectively a regulatory framework to what has become a self-regulatory framework—of banks, give or take, marking their own exams” (Zhong, 2013).

The risk of taxpayers funding further bank bailouts led to Eurozone finance ministers agreeing the terms for a 17-member single currency banking union in December 2013. A Single Resolution Mechanism will provide a centralised system for winding down failing banks. An industry levy will create a €55bn (A\$82,5bn) fund by 2026 with a network of national resolution funds in the transitional period (Financial Times, 2013). Germany opposed taxpayer funded Eurozone bailouts. “It means there will be no additional taxpayer-funded eurozone safety net for the next decade, leaving any bank’s home state largely to foot the bill if its collapse overwhelms the embryonic resources of the banking union system” (Barker and Spiegel, 2013).

*“...we need a new culture of a ‘will to supervise’ in the financial oversight system” ...First, the supervisory bodies need to be given further-reaching rights to intervene in the banks (e.g. to scrutinise business models); second, they must make effective use of these rights to intervene; third, they must have enough staff of the right quality; and fourth, they must be obliged to inform the government, the parliament and the public early on about any signs of gaps in their supervisory powers, and to ask for this to be remedied” (Troost and Hersel, 2012).*

## 4.2 SHADOW BANKING

The shadow banking system consists of non-bank financial institutions and activities outside the regular banking system. It includes hedge funds, money market funds, special purpose vehicles and structured investment vehicles. Investment banks may conduct much of their business in the shadow banking system, although they are not shadow banking institutions themselves. The sector grew globally by 8.1% or \$5tn (A\$5.5tn) (in 2012 to reach \$71.2tn (A\$78.3tn), which represents 24% of total financial assets (Financial Stability Board, 2013a). Real estate investment trusts and funds (+30%), other investment funds (+16%) and hedge funds (+11%) were the fastest growing shadow banking sectors in 2012.

The complex task of mapping the web of transnational connections between funds and identifying systemic risks continues. In September 2013 the European Commission published a roadmap to regulate the shadow banking sector and draft regulations for money market funds. It stipulates funds should hold a cash buffer (3% of their assets), when they guarantee constant value per share, hold financial instruments that can be converted into cash daily (10% of their assets) or weekly (an additional 20% of their assets), and have better risk assessments systems of their assets and their clients (European Commission, 2013a).

A number of critical issues remain, including the strategy to mitigate spill-over effects between shadow banking and the regular banking system, transparency, how to disentangle banking from shadow banking, and “...the pivotal role of Luxembourg, the Netherlands and Ireland in shadow banking activities since these countries are in practice offshore centers where capital is routed between shadow banking entities” is absent from the roadmap (SOMO, 2013).

Both the EU and US strengthened regulation of hedge and private equity funds. The EU’s short selling (speculative sale of securities not owned by seller and repurchase at lower price) transparency regulations, effective from 1 November 2012, had “...mixed effects on liquidity and a slight decrease in price discovery” (European Securities and Markets Authority, 2013).

The G20 Pittsburgh summit agreed to reduce systemic risk, improve transparency, support financial stability and combat market abuse in derivatives markets (financial

contracts). A comparison of US and EU regulations found that they led to broadly similar regulatory outcomes in 15 aspects of trading (Deloitte, 2013).

The UK is challenging the legality of the ESMA powers and the Financial Transactions Tax and has sued the European Central Bank claiming its policies push the clearing of some derivatives away from the City of London and into the euro area.

The planned EU-US Transatlantic Trade and Investment Partnership has already raised disagreements over draft clauses on financial market liberalisation: *"...everything that has been achieved in recent years in the area of financial market regulation could be endangered by the inclusion of financial services in the agreement"* (World Economy, Ecology and Development, 2013a).

### 4.3 CREDIT RATING AGENCIES

Three entrenched Credit Ratings Agencies (CRA), Standard & Poor's, Moody's, and Fitch rate 96% of the world's bonds. Ratings agencies are US private companies with an 'issuer pays' business model, with financial institutions and banks paying the charges for ratings, not investors. They validated the transformation of subprime mortgages into triple A-rated securities, a gross miscalculation and a prime cause of the financial crisis.

Reform has been very slow despite CRAs being heavily criticised. The Financial Stability Board (Bank of International Settlements), responsible for international coordination of national financial authorities and implementation of effective regulatory policies, established a roadmap for reducing reliance on CRA ratings (Financial Stability Board, 2013b and G20, 2013). However, proposals to establish a European public sector ratings agency, break the oligopoly by supporting new entrants to increase competition and other proposals are still under discussion.

There is a strong case for significantly restricting the activities of credit agencies. *"...the false incentives deriving from the fact that the agencies are paid for their supposedly 'objective rating' by the very people they are rating must be ended"* (Troost and Hersel, 2012). Banks could develop capacity to self-assess loans and projects.

### 4.4 FINANCIAL TRANSACTIONS TAX

Eleven European countries, including Germany and France, are pressing ahead with a European Commission proposal for a Financial Transaction Tax (FTT) after other countries opposed the move. It will impose a 0.1% levy on stock, bond and 0.01% on derivative transactions between financial institutions if at least one party is located in the European Union. It could raise between €30bn - €35bn (A\$45bn – A\$52.5bn) annually after allowing for a reduction in trading volumes after its introduction (European Commission, 2013b). The UK, US and the financial institutions strongly oppose the tax.

### 4.5 TAX AVOIDANCE/EVASION REFORM

The European shadow economy results in an estimated tax revenue loss of €864bn (A\$1,296bn) per annum, nearly 20% of total economic activity, plus a further €150bn (A\$225bn) per annum loss through tax avoidance (Murphy, 2012).

US income tax evasion was estimated at US\$500bn (A\$550bn) per annum in 2008 (Celuba and Feige, 2011). Canada's 'underground' economy was estimated to be C\$35bn (A\$36.7bn) in 2009, equivalent to 2.3% of GDP (Canada Revenue Agency, 2012). However, another analysis estimated lost tax revenue from the underground economy to be significantly higher at US\$79.6bn (A\$87.6bn) per annum, with a further C\$81bn (A\$85bn) in tax evasion (Tax Justice Network, 2011).

Tax evasion in Europe and North America totals about €1,600bn annually. If a good proportion of this revenue were collected it would transform public finance in the

respective countries. Yet several governments have systematically cut tax collection budgets and staffing levels. For example, over C\$250m (A\$262.5bn) was cut from the Canadian Revenue Agency's budget up to 2015-2016 (National Post, 2013).

The Organisation for Economic Co-operation and Development (OECD) Action Plan on corporate tax avoidance, endorsed by the G20 Summit in September 2013, to strengthen international tax rules is supported by the Tax Justice Network (Organisation for Economic Co-operation and Development, 2013). However, the Tax Justice Network believes this is "...a path strewn with obstacles, and leading ultimately in the wrong direction" because it tries "...to tax transnational corporations (TNCs) as if they were loose collections of separate entities operating independently in each country. This is a system built on a fiction: the OECD knows as well as anyone that these firms are not bunches of separate entities – but unified firms under central direction" (Tax Justice Network, 2013a).

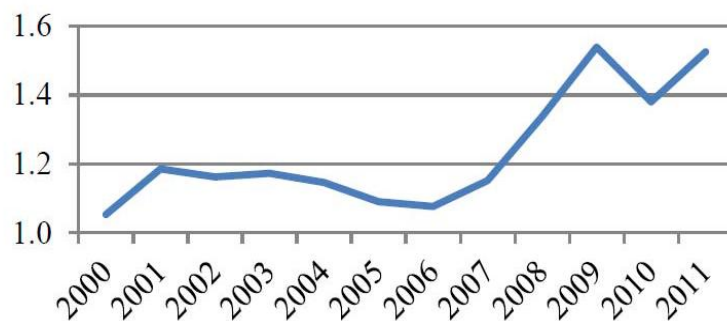
The "...alternative is to take a Unitary approach to taxing multinational firms. This involves taking a multinational's total global profits and apportioning them out between the states where it does business according to its genuine economic presence in each country" (Tax Justice Network, 2013b). This would require a combined and country-by-country report to each tax authority, apportioning profits to different jurisdictions and a procedure to resolve disagreements and conflicts (ibid).

## 4.6 VALUE ADDED TAX GAP

The Value Added Tax (VAT) Gap increased significantly in many member countries since 2008 as a result of the economic crisis. The gap is related to non-compliance under national tax rules and was €193bn (A\$289.5bn), or 1.5% of GDP for the 26 Member States in 2011 or 18% of the theoretical VAT (European Commission, 2013c).

Italy (€36bn – A\$54bn), France (€32bn – A\$48bn), Germany (€26.9bn – A\$40.3bn) and the UK (€19bn – A\$28.5bn) contributed over half of the total VAT Gap in quantitative terms, being the largest EU economies. A reduction in the VAT gap could provide states with significant additional resources.

FIGURE 1: EUROPEAN UNION 26 COUNTRIES VAT GAP (PER CENT OF GDP)



Source: European Commission, 2013c

## 5 RADICAL REDUCTION IN CORPORATE WELFARE

The corporate welfare system of tax reliefs, subsidies, guarantees and regulatory concessions to business must be radically reduced and redirected to direct public investment. For example, capital grants to business, low-wage subsidies, training and research grants, trade marketing and advice, tax subsidies such as capital allowances and various types of credits total over £100bn (A\$150bn) per annum (excluding financial market and bank support, tax avoidance and evasion) in the UK alone (Farnsworth, 2014).



Outsourcing, PPPs and privatisation lead to a contract culture and ‘regulatory capture’, when regulators are aligned to business interests as a result of lobbying, political pressure and ideological sympathy, and consequently prioritise and protect business interests. This ‘protection’ often includes refusing to identify the contractors responsible for poor performance (Whitfield, 2012b).

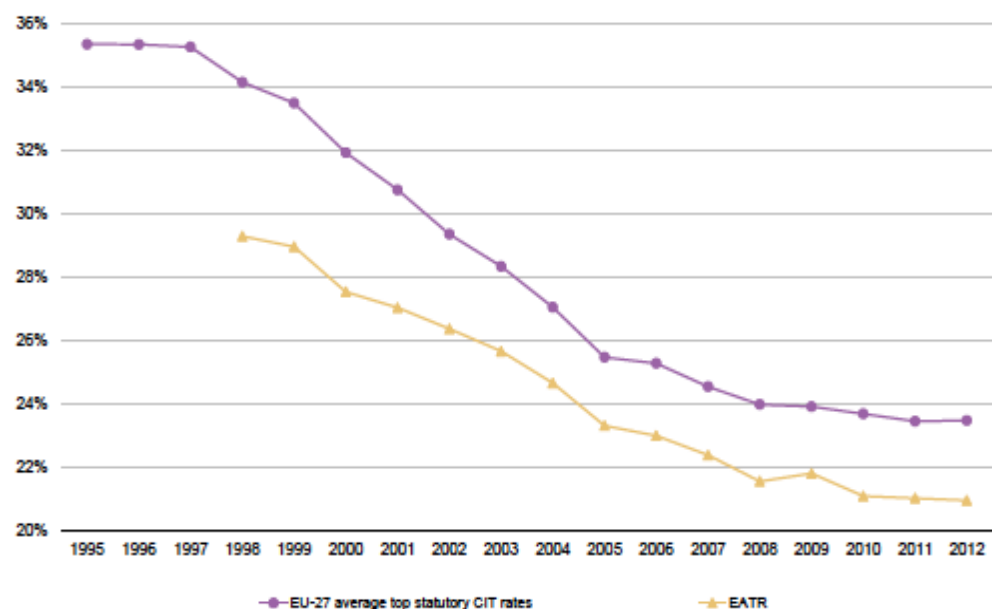
### 5.1 REVERSING CORPORATE TAX CUTS

Corporate income tax rates and the average effective taxation have been significantly reduced in most European countries in the last decade. The average EU-27 corporate tax rate fell from 35.3% in 1995 to 23.2% by 2013, a 12.2% difference (Eurostat, 2013). The Effective Average Tax Rate, the percentage tax rate companies actually pay, had fallen to 20.9% in 2012.

Corporate tax rates in Canada declined from 40.5% to 26.1% between 2010 and 2013 (includes Provincial tax rate). The US rate remained at 35% in the same period, excluding State taxes. However, the US Effective Average Tax Rate is significantly lower at 12.6% of worldwide income (Government Accountability Office, 2013). *“Even when foreign, state, and local corporate income taxes are included in the numerator, for tax year 2010, profitable Schedule M-3 filers actually paid income taxes amounting to 16.9 per cent of their reported worldwide income”* (ibid). Nearly 55% of all large US-controlled corporations reported no federal tax liability in at least one year between 1998 and 2005 (Government Accountability Office, 2008).

There is significant scope to increase corporate income tax rates, the average effective tax rate and to reduce harmful economic development competition between states and regions.

**FIGURE 2: CORPORATE INCOME TAX RATES AND AVERAGE EFFECTIVE TAXATION INDICATORS, EU27 1995-2012 (5)**



Source: Taxation Trends in the European Union, Eurostat, 2013

### 5.2 RE-INVESTING CORPORATE CASH HOARDINGS

Capital investment by the private sector would create jobs, generate supply chain activity, stimulate demand and increase tax revenue. However, non-financial companies have been hoarding cash since the beginning of the financial crisis.

The total deposits of non-financial companies in the Euro Area increased to €1,763bn (A\$2,644.5bn) in July 2013, a 23.5% rise since January 2008. The UK rise was a staggering 455% to £419bn (A\$628.5bn) between the end of 2008 to July 2013 (Burke, 2013). The cash hoard of the one thousand largest US companies rose to \$981bn (A\$1,030bn) in 2011, up 61% over five years (Unmasking Austerity, Briefing No. 1). In Canada “...because corporations are taking in so much more than they are spending, liquid cash assets in the non-financial corporate sector continue to swell, and now total almost [C]\$600 billion” (Stanford, 2013).

The declining proportion of profits directed to investment is revealed in the fall in the investment ratio. The Euro Area ratio fell from 53.2% in 2008 to 47.1% in 2012 with an even bigger decline in the UK from 53% in 2008 down to 42.9% in 2012 (Burke, 2013). Corporate tax rates have been cut over the same period on the assumption that they would encourage increased business investment, but precisely the opposite has occurred.

Three stark facts are evident. Firstly, corporate welfare subsidies and grants have continued to increase. Secondly, corporate cash hoarding in Europe and the US has soared. Thirdly, governments have dramatically cut corporate tax rates and/or effective average tax rates, resulting in ever decreasing corporate sector tax obligations. This indicates there is significant scope to increase both corporate and effective average tax rates through international cooperation, terminate or reduce many of the subsidies, grants and tax relief to business and demand that a substantial part of cash hoardings are invested in sustainable development projects.

## 6 INCREASING LABOUR SHARE OF NATIONAL INCOME

### 6.1 FALLING LABOUR SHARE OF GDP

Austerity policies have led to a further decline in the labour share of national income, whilst a greater share of labour income is going to those with highest incomes, thus increasing inequality (Onaran and Galanis, 2012). The median labour share of national income fell from 66.1% to 61.7% between 1990 and 2009 in 26 out of 30 developed countries (Organisation for Economic Co-operation and Development, 2012b).

This is a significant shift in the distribution of national income between labour (wages, salaries and fringe benefits) and capital (corporate profits, income of small businesses and professional partnerships, rents from land and property and net interest on bank deposits, bonds and loans). The trend is quantified in several studies (International Institute for Labour Studies, 2011; Onaran and Galanis, 2012; Bassanini and Manfredi, 2012; International Labour Organisation, 2013; Lansley and Reed, 2013).

Australia has the highest reduction in labour share of GDP between 1970 and 2007 (see Table 4) followed by the UK and Sweden and a narrowing of the gap in Japan and Denmark.

**TABLE 4: THE WAGE SHARE IN TEN ADVANCED ECONOMIES, 1970-2007**

Country	labour share (% of GDP)		Change
	1970	2007	
Australia	60	53	-7.1
UK	65	60	-5.3
Sweden	66	61	-4.9
Canada	59	55	-3.8
Germany	59	55	-3.7
USA	64	60	-3.1
France	56	57	+0.9
Finland	55	56	+1.0
Denmark	59	65	+6.1

Japan	41	49	+8.2
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Source: Reed and Mohun Himmelweit, 2012, based on OECD data

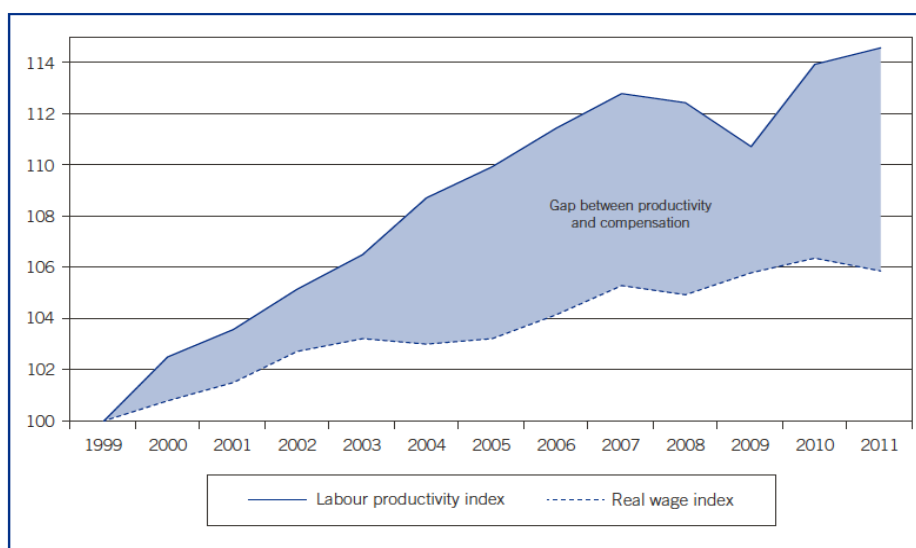
## 6.2 CAUSES OF FALLING LABOUR SHARE

Financialisation (the increased role of financial markets, the aggressive short-termism of financial institutions and rising indebtedness of households) was the main cause of the fall in the labour share of national income. A study of 71 countries (28 advanced and 43 developing and emerging economies) between 1970 and 2007 found financialisation accounted for a 3.3% decline in the wage share, a 1.9% decline for welfare state retrenchment, a decline of 1.3% and 0.7% for globalisation and technological change respectively in the advanced countries (Stockhammer, 2013).

Another study had similar findings by examining data for 71 countries in two selected periods 1990-2004 and 2000-04 – financialisation contributed 46% of the fall in labour share, 25% by welfare state retrenchment and union density, 19% by globalisation and 10% for technology (International Labour Organisation, 2013). “...the relationship between financial globalisation and the wage share is consistently negative across the majority of high-income countries” (International Institute for Labour Studies, 2011).

The gap between productivity and pay is a key factor. “Based on the wage data for 36 countries, we estimate that since 1999 average labour productivity has increased more than twice as much as average wages in developed economies” – see Figure 3 (International Labour Organisation, 2013). It starkly illustrates how capital captured the bulk of the benefits of increased productivity.

**FIGURE 3: TRENDS IN GROWTH IN AVERAGE WAGES AND LABOUR PRODUCTIVITY IN DEVELOPED ECONOMIES (INDEX: 1999=100)**



Note: Since the indices refer to a weighted average, developments in the three largest developed economies (United States, Japan and Germany) have a particular impact on this outcome. Labour productivity is measured as output per worker (see note 9).  
Sources: ILO Global Wage Database; ILO Trends Econometric Model, March 2012.

Productivity in the USA increased 245.3% between 1948 and 2010 compared to a 113% increase in hourly wage rates. Growth rates were comparable up to 1973, but after that, productivity grew strongly whilst wage rates were relatively stagnant (Mishel, 2012).

The privatisation of network industries (telecommunications, electricity, gas, airlines, railways, roads and postal services) is another contributing factor. A study of privatisation in eighteen OECD countries between 1970 and 2001 concluded “...the wave of privatization in OECD countries is a significant part of the declining share of labour in the network industries — accounting for a fifth of the fall on average, but over half in Britain

and France” (Azmat et al, 2012). This is due to large falls in employment, offset by higher wages (outsourcing and privatisation of other services experience both job and wage cuts).

Another study concluded “...massive privatisation of network industries since the early 1990’s can explain about 33% of the decline of the labour share in these industries” (Bassanini and Manfredi, 2012). Since many countries privatised state-owned corporations in other sectors of the economy, the impact of privatisation is probably “...at least as important as that of globalisation” (ibid).

The reduction in bargaining power of labour contributed to the decline in the labour share of national income (International Institute for Labour Studies, 2011).

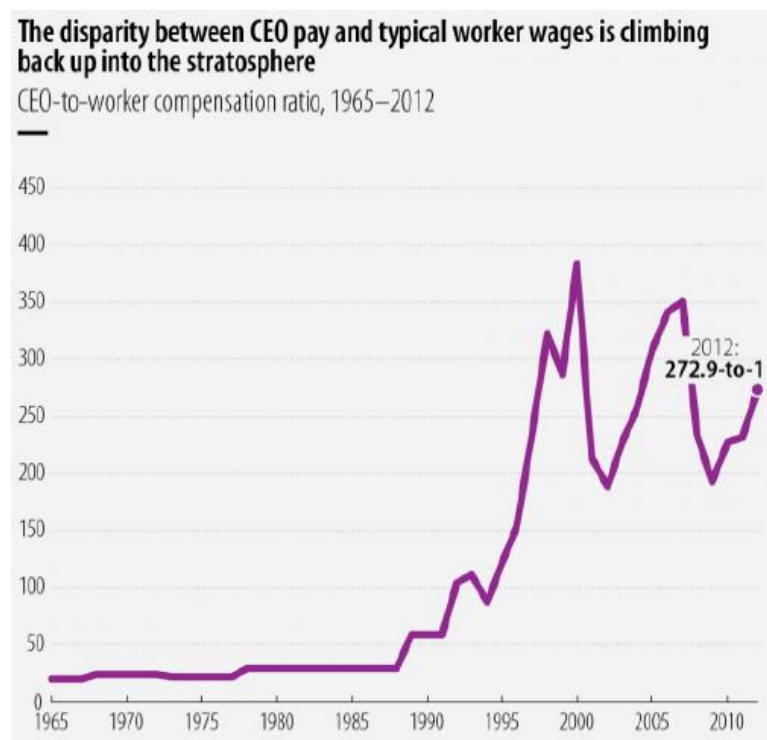
The fall in labour share of national income led to a decline in workers purchasing power, but financial deregulation provided a short-term solution for capital. Consumption booms in the US and a lesser extent in the UK, Australia and the bailout countries (Greece, Ireland, Portugal and Spain), were underpinned by soaring household debt rather than rising wages. “...changing financial norms, new financial instruments (credit card debt, home equity lending) and deterioration of creditworthiness standards, triggered by the securitization of mortgage debt, made increasing amounts of credit available to low-income, low-wealth households, in particular. **Household debt thus became a substitute for higher wages as a source of demand and consumption**” [my emphasis] (International Labour Organisation, 2013).

Not only has the labour share of national income been in decline, but inequality has been rapidly increasing within the labour share. The top 1% of US households had 59.9% of the increase in income between 1979 and 2007 compared to only 8.6% for the bottom 90.0% (Mishel and Bivens, 2011). The top 1% of incomes grew by 31.4% between 2009 and 2012 in stark contrast to only a 0.4% increase for the bottom 99% - thus the top 1% captured 95% of the income gains in this three-year period (Saez, 2013).

*“...inequality in income distribution is one the major causes of the crisis along with financial deregulation at a national and international scale. In the face of falling wage share across the world, a global stagnation was avoided thanks to an increase in debt, mostly private, and global imbalances. After the collapse of the debt-led model with the global recession, the wage moderation policies of the last three decades proved to be unsustainable. Reversing inequality would bring us a step closer to eliminating a major cause of the crisis; it would also be a way of making the responsible pay for the crisis” (Onaran and Galanis, 2012).*

The gap between chief executive’s pay and typical worker wages is growing rapidly again after shrinking during the recession. The ratio of annual pay received by chief executives of the largest 350 U.S. firms relative to annual wages of production/nonsupervisory workers in those firms’ industries was roughly 20-to-1 in 1965. By 2012, it was 273-to-1 – see Figure 4 (Economic Policy Institute, 2013).

FIGURE 4: THE GAP BETWEEN US CHIEF EXECUTIVE AND TYPICAL WORKER WAGES 1965-2012



Source: Economic Policy Institute, 2013

### 6.3 WAYS TO INCREASE THE LABOUR SHARE OF NATIONAL INCOME

A quarter of US workers and one-fifth of workers in the UK, Canada, Ireland, and Germany were in low-wage jobs (earning less than two-thirds of the national median hourly wage) compared to 11.1% and 8.0% in France and Italy respectively (Schmitt, 2012).

Employers should be required to pay a living wage, and a cap imposed on excessive salaries in banks and businesses would help to increase the labour share of national income. Contract compliance, including employment conditions, minimum use of zero-hour contracts and defined benefit pensions are vitally important.

The multi-billion dollar benefits paid to working people on low incomes/wages, such as the UK Working Tax Credit and US Earned Income Tax Credit are, in effect, a public subsidy to corporate employers who will otherwise have no incentive to improve their employee’s terms and conditions. These tax credits could be systematically reduced in parallel with wage increases.

Policies to create full employment, increased national minimum and living wage rates, reduction of the gender pay gap, increased trade union membership and representation, extended collective bargaining and workplace participation have an important role in increasing the labour share of national income. Pension privatisation must be strongly resisted together with all further moves to close or erode defined contribution schemes.

## 7 KEY LESSONS

Alternative economic stimulus strategies alone will be only partially effective. They must be accompanied by industrial investment and innovation, the reconstruction of the state and public services, more rapid reform of banks and financial markets, a radical reduction in corporate welfare and ways to increase the labour share of national income.

The fixation with rapid public debt reduction is a ploy to accelerate neoliberal transformation of the public sector and welfare state. The political focus is on public, not private debt, yet little has been done to address the continuing high level of household debt.

Trade unions, community and civil society organisations must be closely involved in the drawing up of alternative economic strategies to ensure they are comprehensive and fully incorporate their needs and interests.

Alternative economic strategies should provide a springboard for the preparation of more detailed visions, plans and strategies for sectors, services, regions and localities that could be integrated into trade union, civil and community organisation and protest movement activities.

Building coalitions and alliances and jointly developing alternative policies and integrating them into organising and action strategies should be standard practice.

More substantive and frequent interventions to challenge local policies and procurements are urgently needed in which alternative plans and policies have a key role in building public support. The financial crisis, rapidly evolving technology and demographic change mean that the status quo is rarely tenable. Alternative policies can strengthen organising and combine proactive, interventionist and defensive tactics.

Clarity of language and objectives is essential (Whitfield, 2006). Policies can be rapidly watered down and apparent support can vaporise at the legislative and implementation stage. It is therefore vital to retain 'ownership' of alternative policies and strategies, to constantly develop and improve them, revise their costs and benefits and assess the economic, social justice, environmental, health and employment benefits.

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