

# PARLIAMENTARY DEBATES

HOUSE OF COMMONS  
OFFICIAL REPORT

European Committee B

VALUE ADDED TAXATION

*Tuesday 21 February 2017*

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**The Committee consisted of the following Members:**

*Chair:* PHILIP DAVIES

- |   |  |
|---|--|
| † Baker, Mr Steve ( <i>Wycombe</i> ) (Con)                                | † Green, Kate ( <i>Stretford and Urmston</i> ) (Lab)       |
| † Barclay, Stephen ( <i>Lord Commissioner of Her Majesty's Treasury</i> ) | † Rees-Mogg, Mr Jacob ( <i>North East Somerset</i> ) (Con) |
| † Blackman, Kirsty ( <i>Aberdeen North</i> ) (SNP)                        | † Robinson, Mary ( <i>Cheadle</i> ) (Con)                  |
| † Cartlidge, James ( <i>South Suffolk</i> ) (Con)                         | † Smith, Nick ( <i>Blaenau Gwent</i> ) (Lab)               |
| † Dowd, Peter ( <i>Bootle</i> ) (Lab)                                     | † Williams, Craig ( <i>Cardiff North</i> ) (Con)           |
| † Ellison, Jane ( <i>Financial Secretary to the Treasury</i> )            | Kenneth Fox, <i>Committee Clerk</i>                        |
| † Goodman, Helen ( <i>Bishop Auckland</i> ) (Lab)                         | † <b>attended the Committee</b>                            |

## European Committee B

Tuesday 21 February 2017

[PHILIP DAVIES *in the Chair*]

### Value Added Taxation

[*Relevant documents: 30th Report of Session 2015-16, HC 342-xxix, Chapter 2; 17th Report of Session 2016-17, HC 71-xv, Chapter 1; 26th Report of Session 2016-17, HC 71-xxiv, Chapter 7; 28th Report of Session 2016-17, HC 71-xxvi, Chapter 11; 30th Report of Session 2016-17, HC 71-xxviii, Chapter 4.*]

8.55 am

**The Chair:** Before we begin, it may be helpful to remind Members of the procedure in European Committees. The whole proceeding must conclude no later than two and a half hours after we start. First, I shall call a member of the European Scrutiny Committee to make a brief statement about why the Committee decided to refer these documents for debate. Secondly, I shall call the Minister to make a statement, followed by questions for up to an hour, though I have some discretion to extend that if there is an appetite to do so. Thirdly, the Committee will debate the Government motion, and I will put the question on the motion when debate or the time available is exhausted, whichever comes first.

I understand that the hon. Member for North East Somerset would like to make a brief explanatory statement about the decision to bring the documents to the Committee.

**Mr Jacob Rees-Mogg** (North East Somerset) (Con): It is a great pleasure to serve under your chairmanship, Mr Davies. It may be helpful to the Committee if I take a few minutes to explain the background to this document and why, nearly a year ago, the European Scrutiny Committee recommended it for debate.

The EU has a common system of value added taxation, governed principally by the 2006 VAT directive. The VAT directive, in its present and earlier versions, is meant to be a temporary arrangement, pending member states' agreement on a permanent and definitive VAT system. The Commission has accepted that the existing system contributes to VAT fraud in cross-border trading.

Following extensive consultations begun in late 2010, the Commission published in April 2016—it works very swiftly—an action plan to establish a

“VAT area that is fit for purpose in the 21st century.”

It sets the direction of travel the Commission envisages for VAT and presents a set of ideas for wider EU debate under four headings: “Recent and ongoing policy initiatives”, “Urgent measures to tackle the VAT gap”—that is the difference between expected revenue and revenue actually collected, a significant part of which results from fraud—“Medium term measure to tackle the VAT gap” and “Towards a modernised rates policy”.

The European Scrutiny Committee has considered the document twice. In April 2016, it said that the document might prove to be the catalyst for the EU finally achieving a definitive VAT system. Accordingly, we recommended that it be debated in this Committee

and that Members might wish to explore whether such a VAT system is indeed now in prospect in the foreseeable future; what difficulties for other member states the Government see in agreement on a definitive system; the extent to which the existing regime has contributed to cross-border fraud and the extent to which the proposal might remedy that; and what difficulties there may be for the UK in reaching such an agreement.

When we reconsidered the matter in November 2016, we deplored the Government's inexcusable failure to schedule this debate in a timely manner. However, we also added further matters that Members might wish to explore in this debate, which include: details of the Council conclusions on the action plan and their implications for the UK; what the prospects are now for implementation of the Commission's undertaking in relation to zero rating of sanitary products; and to what extent the Government expect there to be continued UK and EU harmonisation of VAT rules post-Brexit. I look forward to hearing contributions on those issues in the debate and to the Minister's response.

**The Chair:** I call the Minister to make an opening statement. I remind colleagues that interventions are not allowed during a statement.

8.59 am

**The Financial Secretary to the Treasury (Jane Ellison):** It is a pleasure to serve under your chairmanship, Mr Davies. Good morning, colleagues. I am pleased to be here to discuss the European Commission communication on an action plan on VAT, “Towards a single EU VAT area—Time to decide”, which my hon. Friend the Member for North East Somerset outlined. I apologise that it has taken so long to schedule this debate and, indeed, has spanned two Ministers. We are here now, and we will have a chance to look at these issues and cast our minds ahead to the new challenges, as circumstances are very different from when the debate was first called for.

The action plan on VAT provides an update on progress and identifies the next steps to be taken to improve the system. As we have heard, the Commission's Green Paper on the future of VAT, published back in December 2010, launched an EU-wide consultation on the future of VAT in the EU. The subsequent White Paper in 2011 set out the Commission's vision of a simpler, more efficient and robust VAT system that is tailored to the single market. The White Paper was presented to this Committee in an explanatory memorandum in December 2011 and the Committee debated it in 2012. The Commission's communication, published in April last year, is the continuation of that work.

Like the preceding Green and White Papers, the action plan contains no legislative proposal, but sets out the Commission's vision for the future of VAT—in the Commission's words:

“A VAT area that can support a deeper and fairer single market, and help to boost jobs, growth, investment and competitiveness. A VAT area that is fit for purpose in the 21st century.”

The overall approach in the plan is aligned with the UK's approach of reducing burdens on business and developing a practical and workable system. The plan identifies the areas in which the Commission feels that further reform is necessary and presents a range of ideas for future EU work.

The ideas are grouped under four headings, as has been mentioned. Under the heading, “Recent and ongoing policy initiatives”, the plan highlights the shortcomings of the current EU VAT system in dealing with cross-border e-commerce. It outlines the Commission’s intention to present legislative proposals that would modernise and simplify VAT rules for cross-border e-commerce, and highlights the Commission’s intention to produce a package of legislative proposals this year, with the aim of improving the VAT environment for small and medium-sized enterprises to facilitate growth and encourage cross-border trade.

Under the heading “Urgent measures to tackle the VAT gap”, the plan proposes improvements to co-operation between EU member states and between EU and non-EU countries. It suggests that such changes would improve the efficiency of tax administrations and improve levels of voluntary compliance and co-operation between businesses and tax authorities. The plan also identifies potential measures to improve co-operation between tax administrations and customs law enforcement bodies and to strengthen tax administrations’ capacity in the fight against fraud, which I know has been at the forefront of the Committee’s thinking over the past few years.

The plan then focuses on moving towards a robust single European VAT area. As has been alluded to, the current VAT system is technically a temporary one. As members of the Committee know, when VAT was first established the aim was for goods to be taxed in the country of origin. At that time, however, an origin-based system was not possible for technical and political reasons, so transitional systems were adopted. Various attempts have been made to move towards an origin-based VAT system, but all have been unsuccessful. The Commission’s 2011 White Paper concluded that the origin principle remained unachievable and confirmed that the destination system would instead be pursued. The action plan committed the Commission to produce a legislative proposal for a definitive VAT system based on that principle this year.

The final section of the plan focuses on moving “Towards a modernised rates policy”. Parliament has a particular interest in that and in some of its implications. It highlights the constraints of the existing VAT directive in limiting member states’ freedoms to set VAT rates. Those rules were designed for a VAT system based on the origin principle and were therefore intended to guarantee the neutrality of the system. Given the agreement to pursue a final system based on the destination principle, the plan highlights that there is now an opportunity for member states to be given greater autonomy in setting rates.

The plan outlines two possible options that would give member states that additional flexibility. The first involves extending the current range of reduced rates legally applied in any member state to all member states; the list of goods and services eligible for the reduced rates would then be regularly reviewed. The second involves removing the existing reduced rate list and granting member states much greater rate-setting power.

The Commission has recently produced a number of the proposals that were trailed in the plan. In the context of the digital single market initiative and the May 2016 conclusions on the plan, the Commission published a proposal on e-publications in December

last year. That was presented to the European Scrutiny Committee in explanatory memorandum 38344. Helpfully, that proposal has generated some discussion on VAT rates more generally and on the level of flexibility and autonomy that should be enjoyed by member states in setting domestic rates. That is important in the context of the wider rates review trailed in the action plan, which is expected by the end of the year. That is specifically relevant to the UK’s pursuit of the legal changes necessary to allow the introduction of a zero VAT rate on women’s sanitary products. We explored that issue in detail during Report stage of last year’s Finance Bill, and I know that Members across the House feel strongly about it.

As Members will be aware, the Government broadly welcome the action plan, most of which follows the UK approach to reducing the burdens on business and developing a system that is practical and workable, as seen in a number of the changes in the digital single market proposals presented to the European Scrutiny Committee in explanatory memorandums 38341/2/3, and specifically the introduction of a threshold for cross-border supplies of digital services and the “soft landing” easements for small businesses.

Of course, these and any other legislative proposals emerging as a result of the action plan are and will be subject to scrutiny in the normal way. They will also be subject to negotiation, and the unanimous agreement of member states will be required before any legislative changes can be made. As always, the key will be in the details of further work and proposals. The plan provides a basis for member states to explore the future of the EU VAT system and, in particular, a basis for a way forward on key UK priorities on simplification and on VAT rates.

**The Chair:** We now have until 9.55 am for questions to the Minister. Although I may allow the shadow Minister some leeway, I remind hon. Members that questions should be brief. Subject to my discretion, it is open to a Member to ask related supplementary questions.

**Peter Dowd (Bootle) (Lab):** It is a pleasure to serve under your chairmanship, Mr Davies. I thank the hon. Member for North East Somerset for his presentation and the Minister for soldiering on with a cold or virus.

Reference was made to “Time to decide”. I think that was 23 June last year, actually. That is symptomatic, in that many hon. Members are exercised by the fact that the Government are in assent on this matter and for so long have been all at sea—I think mid-channel might be where they are. Of course, the European Scrutiny Committee showed its exasperation on this matter and wagged its finger at the Government for not being able to debate this in due time to tease out many of these very important issues. However, we are where we are.

I think that in the last Committee of this nature that I was at, I raised the fact that we are now, in the light of the referendum, just going through the motions; I think we are all going through the motions. Before the hon. Member for North East Somerset got up and spoke, I thought, rather quaintly, that some Members do not grasp that, but clearly everybody is now beginning to grasp it.

[Peter Dowd]

On a more positive note, we have before us a framework in relation to the operation of a VAT system that simplifies things by reducing bureaucracy and so on. No one can disagree with that, but within a couple of years we will not be a member of the EU. We will not be in the single market, I suspect, or in the customs union and all the other institutions, so the debate that we are having, to some degree or another, will all be pretty obsolete. Unless the Government can push this along in the next two years—so pretty sharpish—it is pretty pointless, but of course by that time we will, I assume, have gained complete sovereignty over our tax affairs. We will not be beholden to the Commission—presumably. We will be able to have whatever VAT rate we want—presumably. We will be able to be as flexible as we want with the rates—presumably. Conservative Members, who wear subsidiarity as an amulet, will even be able to get rid of the descriptive name of the tax and call it something other than VAT. I am sure that Members will have their own monikers and acronyms ready: WOT, the “We’re off” tax, or GOT, the get-out tax. I suspect that it will be the legacy of some Conservative Members to get rid of the last vestige of European colonialism. It will be similar to when the Irish painted their red postboxes green.

Anyway, VAT arrangements will still exist. The bottom line is that we need certain assurances that over the next two years there will not be more loss of tax from the VAT regime as a result of aggressive tax avoidance or evasion, especially given that Her Majesty’s Revenue and Customs’ ready reckoner indicates that a 1% change to the standard rate is worth about £5.7 billion. We really have to keep our eye on that. As we move into this transition, we have to keep our eye on that. We have to put markers down in relation to green tax as well. I am talking about commitments not to put too much tax on green issues. We do not want tax hikes by the back door.

On the tampon tax, my hon. Friend the Member for Dewsbury (Paula Sherriff) and many women’s groups have fought hard to abolish the tax, and we need to push on and get an unambiguous commitment from the Government.

**The Chair:** Order. We will have a debate after the questions. I was prepared to give the hon. Gentleman some latitude but I ask him to crack on. I do not want him to use up his debate material during the questions. He might want to save it up for the debate.

**Peter Dowd:** I have raised the issues of tax avoidance and the green tax. On the optimism about getting the measure through, do we believe that we will be able to introduce it within the next two years? How long is a piece of string in relation to this matter? I hope that we do not have to hold our breath for too long.

**Jane Ellison:** I will make a general point and then respond with a bit more detail on fraud. I could not disagree more with the shadow Minister, although I thank him for his kind words on the state of my voice—I apologise to colleagues. It is certainly not the case that the vote to leave the European Union makes the debate “obsolete” and our participation in and engagement with the agenda pointless. For a start, there

are UK businesses that have EU subsidiaries that will continue to be affected by the VAT rules within the EU, so it is important that the rules work well and are subject to sensible reform. The UK has always been a good influence for pragmatic reform in all such regards.

The precise arrangements under which we operate outside the EU will be subject, as we all know, to detailed and complex negotiation once article 50 has been triggered, but the EU will remain a major trading partner. We are leaving the EU; we are not leaving Europe. It will be an extremely important commercial relationship. The extent, therefore, to which the direction of travel on EU VAT rules aligns with our own priorities regarding simple and pragmatic regulation that is not burdensome to small businesses is, and will remain, extremely important.

Before we came into the debate, I asked my officials about how we will influence policy once we are outside the EU. The reality is that there are people who are not in the EU now who will influence and have a view about the EU’s VAT proposals. Equally, the OECD does a lot of work in that respect. There is a broad alignment of direction of travel between that organisation and the EU, and to that extent we are an important influence within the OECD. I reject the idea that the debate is obsolete and that our interest ceases once we are outside the EU. It remains the case that we need the rules to function sensibly and in a way that is as unburdensome as possible and addresses fraud, to which I now turn.

No system will be entirely fraud-free, and the concern for the UK and member states more generally about any move to a new system is that any change could introduce a new type of VAT fraud. In all aspects of the tax system, we have to consider where people might look to exploit the gap created by a change. In the UK, the level of VAT fraud attributable to criminal attacks on cross-border trade has fallen from a peak of between £2.5 billion and £3.5 billion in 2005-06 to between £500 million and £1 billion in 2014-15. The Commission has done various studies, and the one from 2013 estimates that such supplies amount to about €184 billion-worth of VAT for the UK alone, in terms of intra-EU supplies. Any change to the VAT rules on intra-EU supplies that would introduce a new type of fraud has, therefore, the potential for huge losses and it is important that we tread carefully. Within any proposal for a definitive VAT system, that will be an area for great scrutiny. We welcome the Commission’s engagement with us and its acceptance that member states will need to work very closely together to explore and evaluate.

**Peter Dowd:** I was trying to make a point about the obsolete nature of this debate. Would the Minister agree that there is a big difference between having a debate when a member of the European Union, with access to the single market and so on, and when outside the Union? We have been discussing it for several years; we are moving out and the EU know that, so this debate is to some extent pretty obsolete.

**Jane Ellison:** Without rerunning the referendum campaign, those issues were explored. I do not accept the basic premise, for the reasons I have given. Many businesses will continue to trade within the EU and have EU subsidiaries. The EU will remain a hugely significant trading partner and, as with all our trading

partnerships around the world, we would look to bring UK influence to bear in a way that would support our own economic goals. There is a mutual benefit in having rules that work for everyone. We will also be a major trading partner for many EU members when we are outside the EU. Those are also important trading relationships. To that extent, there is mutual interest in making sure that we continue to move in a broad direction of travel and that we bring UK influence to bear.

When I was Europe Minister in the Department of Health, my experience was that the UK perspective on regulation, particularly with regard to the burden on business, was always felt to be a pragmatic and valuable contribution. I have no reason to think that that will change afterwards, albeit that relationships are clearly going to be in flux over the coming period of negotiation.

**Peter Dowd:** I take the Minister's point, but the first sentence in the document is:

"This action plan sets out the pathway to the creation of a single EU VAT area."

That is in the context of the single market. Does the Minister not agree that she is putting her head in the sand in the way that she is continuing to discuss this matter?

**Jane Ellison:** I am not sure I can add a great deal more. No, I do not have my head in the sand. I am being practical, as many of us now have to be. As Ministers, many of us are engaged on a day-to-day basis with the practicalities of how we move forward.

To reiterate, when we are outside the EU, it is probably going to remain our most important trading relationship. Therefore, it is vital that we continue to be good EU members while we are in, and that we continue to be engaged, practical and positive once we are out.

**Mr Steve Baker (Wycombe) (Con):** To level-set people's expectations, when in the process of the next few years do we expect to regain sufficient control over VAT so as to be able to end, for example, the hated tampon tax?

**Jane Ellison:** On Report of the Finance Bill last year, we included provisions to legislate by this spring or by the time that we had left the EU, whichever was legally possible and feasible. We have continued to engage with the Commission at official and ministerial level quite extensively since that debate. We are not likely to be in a position to move this spring, for the reason I spelled out in my comments, but we have given a commitment. We have the same view on this matter in all parts of the House; we want to deal with this long-standing anomaly. I am sure Members of all parties would also support the fact that we are equally committed to abiding by the rules for as long as we are in the club. We will not, and cannot, act outside the rules—that would be counterproductive to a negotiation in good faith—but we have included legislative provisions to move on this matter as soon as we are legally able. The clock is ticking on it. We are not moving towards a distant and unsighted point—we have a sense of the backstop date.

**Kate Green (Stretford and Urmston) (Lab):** I have two questions. The Minister said a few moments ago that she looked forward to European Union alignment, after we have left, with our own VAT successor system,

but that is surely the wrong way round. We will want to look at the opportunities to align our systems with a very large trading bloc sitting on our doorstep. First, to what degree does the Minister accept that the Government will wish to continue down a route of as much harmonisation as possible post-Brexit between our VAT system and whatever is developed in the European Union?

My second question is a prosaic one on behalf of my constituents who are trying to understand how their travel arrangements and holidays in the European Union might be affected after Brexit. Does the Minister envisage it will be possible to reclaim VAT paid in European Union countries as consumers leave the European Union to return from their holidays to this country?

**Jane Ellison:** On the first point, I did not express a specific aspiration about harmonisation. I said there was a clear national interest in continuing to engage with the EU. As I said before, the OECD and the EU are moving broadly in the same direction around VAT systems. There is therefore a wider interest in the UK's continuing to pursue some of its key objectives around simplification and making the arrangements less burdensome, particularly for smaller businesses. The precise aspects of VAT arrangements are, as with so many things, a matter for the detailed negotiations ahead, once article 50 has been triggered.

It is reasonable to say that we would look to have arrangements in future that allow us to continue to trade easily and successfully with all our major trading partners, of which the EU will be an incredibly important one. It remains the case that it is sensible for us to stay engaged with the debate, but the detail of all of those things once we are outside the EU, including issues around things such as harmonisation, are for the negotiations. We cannot be clear yet, but I assure the Committee that the Government will seek the best deal, obviously. It is clear that, after we have left the EU, VAT will continue to be a major contributor to the Exchequer. In the UK we estimate we will raise £120 billion this year, which is important revenue for the Treasury.

Although the exit from the EU will offer the UK greater flexibility, it is important to manage expectations just a little. Colleagues might be interested to learn that requests for reliefs have already been flooding into the Treasury in anticipation of our leaving the EU—to date, a total of more than £30 billion—so the ready reckoner is already ticking over. Colleagues will have done their mental arithmetic and realised that £30 billion is rather a large proportion of the estimated £120 billion that we hope to raise this year. That is on top of the range of zero and reduced rates that have already been applied, estimated to be slightly less than £45 billion in 2016-17.

The issues around future rates for us outside the EU and all other issues have to be carefully considered, not only in terms of our trading relationship with the EU, but in terms of our domestic policy and economic and budgetary constraints. As with all such things, it is a complicated picture, but we will continue to engage with the debate. It is worth putting on the record that UK officials are not only engaged but making an extremely positive contribution to the wider debates on the technical policy-making areas, and we will continue to do that to good effect.

**Mr Rees-Mogg:** May I take it from the answer given to the hon. Member for Stretford and Urmston that there is at least the possibility that we will get back duty free when we have left the European Union? It would be a wonderful gift to the British people and would increase their joy when they travel.

**Jane Ellison:** It seems unusual for a Government Minister to draw attention to the fact that she did not answer a question, but since I did not answer that question, I made no such speculation or comment. As I have said, all these matters are for the negotiations ahead and a range of different outcomes are possible.

**Mr Rees-Mogg:** I merely asked if it were possible, and the answer, being answerless, indicates that it must at least be possible.

**Jane Ellison:** I will reflect and try to understand what was just said.

**Peter Dowd:** Just a final question from me. The Minister also did not answer the question from the hon. Member for Wycombe about the tampon tax. Although the Government have legislated to get rid of the tampon tax, depending on whether we are in or out of the Union, does the Minister believe that we will be able to implement a zero rate on the tampon tax before we leave the Union? What is the real possibility of that happening?

**Jane Ellison:** We have taken the House's instructions very seriously. There was not just the debate on Report last year, to which I responded; this has been a live debate probably for my adult lifetime, and there have certainly been a lot of debates in the House in recent years, so we have been actively pursuing this issue. I recently detailed in a written answer some of the extensive engagement we have had at ministerial level and through letters at official level.

While we are in the EU, both sides continue to be bound by existing rights and obligations, and EU law allows for a reduced rate of not less than 5% to be applied to those products. We apply the lowest reduced rate, but we cannot apply a zero rate until there is an EU legislative change. We continue to push for it and to engage on the issue very actively, but the EU legislation can be initiated only by the Commission, and to date it has not provided the proposal that it was planning to bring forward before the EU membership referendum. We continue to push for the proposal, and we have tried to find ways of accelerating the prospects of a change, but it is likely that it will feature only as part of the VAT rates review that we anticipate will happen towards the end of this year. We will continue to keep the House updated, and no doubt we will return to the issue in the debates on this year's Finance Bill.

**Kate Green:** Irrespective of Brexit, what is the Minister's assessment of the likelihood that the European Union and its component member states will be able to develop and introduce a modernised VAT system, as the Commission hopes? What difficulties does she envisage for the other member states in reaching agreement on doing so?

**Jane Ellison:** As I said, this would be a very major change to the EU VAT system. To give colleagues a sense of perspective, it would affect about €600 billion of member states' VAT revenue, which is a lot of money. We estimate that between 3.2 million and 3.7 million EU firms are involved in cross-border trade. Although this Committee in particular has expressed a degree of frustration at the speed at which events move, it is right that the Commission, member states and business stakeholders work together and take time to assess the impact. Any change has to strike the right balance, in terms of both preventing fraud and of simplicity and ease of operation. Inevitably, there is sometimes an offset between those two ambitions. We probably feel that the Commission's medium-term timeline looks a bit optimistic, but we continue to monitor these events very carefully and influence them.

**The Chair:** If no more Members wish to ask questions, we now proceed to the debate on the motion.

*Motion made, and Question proposed,*

That the Committee takes note of European Union Document No. 7687/16, a Commission Communication on an action plan on VAT: Towards a single EU VAT area—Time to decide; and agrees with the Government that it provides a basis for a way forward on key UK priorities on VAT simplification and on VAT rates.—(*Jane Ellison.*)

9.29 am

**Peter Dowd:** I have nothing further to add to this debate.

9.29 am

**Kirsty Blackman** (Aberdeen North) (SNP): I have a few things to add to our debate. First, I want to talk about the Scottish context, particularly on VAT for police and fire. It has previously been said that there cannot be changes to VAT for police and fire because of European regulations, and that there cannot be a change within what is classed as one member state.

In Scotland, our police and fire services are paying £35 million a year in VAT that we believe we should not be paying. We have made that case on a number of occasions, but the UK Government have refused to make changes to the system, despite allowing both the London Legacy Development Corporation and Highways England a derogation in terms of their VAT, which has not been the case for the Scottish police and fire services. If we are leaving the European Union, which it seems we are, will there be changes in that regard?

The other thing to consider is that if we go forward on the basis of what has been provided today—the document that has been put forward by the EU—there is a suggestion that there will be more flexibility for member states regarding what they can and cannot zero-rate. So if we continue with these regulations, would there be a possibility that the UK Government could more easily zero-rate the police and fire services than they have so far been willing to do? That is a specific point about the Scottish context.

I will also mention sanitary products. Again, this document mentions a couple of options for the future, option 1 and option 2, both of which involve changes around some of the derogations; option 2 in particular involves changes of that kind. We have this historical

situation whereby the derogations were created when we first joined the European Union and they make little sense in today's context. Some things that are luxury products—I consider them to be luxury products—currently have a derogation, and there are some things that I would consider essential products, such as sanitary products, that do not. I am not just talking about products for the absorption of blood but those for the absorption of urine or breast milk, which I have pressed the Minister on previously.

Those products should have a zero rate of VAT, because they are necessary. There are strange contextual issues around products used for the absorption of urine, but a number of people have got to pay VAT on them even though they are absolutely necessary products for them. It is really important that the Government consider this issue as we go forward.

I will put both those things in context. I disagree with the hon. Member for Bootle, who said that this debate is almost irrelevant; the opposite is actually true. What we need to do, as current members of the European Union, is ensure that decisions taken around VAT are as favourable as possible for the UK. We need to go into those negotiations and make our position clear, which is why I am taking the time today to speak about those things that I think are really important, so that the Minister is aware, when he goes into those negotiations, that I think they should be key priorities.

The wider context is that we will be outside the EU and we will have less of a seat at that table than we do currently. The Minister has mentioned the seat that we have around the OECD table, but when it comes to the single EU VAT area the likelihood is that it will take some time to create it and that we will lose our seat at the EU table before it actually comes into force. So we need to make our voice heard as clearly as possible right now, so that future regulations are positive for us.

One of the reasons I think this issue is really important is that if Members look at the top of page 8 of the papers we have been given they will see that the second paragraph says:

“better cooperation with international organisations and non-EU countries over VAT should make it possible to extend the EU system of administrative cooperation to non-EU countries, particularly to ensure effective taxation of e-commerce.”

**Peter Dowd:** I do not understand why people do not get this point, but does the hon. Lady agree that the Commission will not discuss anything in this whole debate about post-Brexit issues with us? It just will not do that. Does she accept that?

**Kirsty Blackman:** In the context of the article 50 negotiations that we will have, I think that the Commission will say to us, “No, we're not very keen to discuss some of the ongoing future framework.” However, we are currently a member state. We have not yet triggered article 50 and while the article 50 negotiation period is happening, we have two years as an EU member state. The Commission does not have the ability to exclude us from negotiations about how things will develop in the future. So if the Government and the UK fail to do what I am suggesting, there will be a huge issue regarding how the UK gains access to things such as the single market in the future.

**Peter Dowd:** I repeat what I said earlier: this action plan—not a future action plan or one we would like—sets out the pathway to the creation of a single EU VAT area. Does the hon. Lady not understand that we are not going to be in a single EU VAT area?

**Kirsty Blackman:** We will not be in a single EU VAT area because we will not be an EU member state. However, the paragraph that I have just read out says that it should be

“possible to extend the EU system of administrative cooperation to non-EU countries, particularly to ensure effective taxation of e-commerce”,

so we will be involved as a third country. Given the way the EU does trade deals, it will look to ensure that there is as much equivalence and commonality as possible in a number of areas. We therefore need to make the case for the industries, sectors and products that we think are important. Ensuring that our voice is as loud as possible in these negotiations will benefit us as a country.

The likelihood is that the EU will look to include some commonality or equivalence in relation to VAT systems in a post-Brexit deal with the UK. The EU is a much bigger entity than the UK, so we need to think carefully about how the EU is currently structured and what it is currently doing to ensure that it is as favourable as possible for us when we become a third country and try to make a trade deal with it.

**Mr Baker:** I have been listening carefully to what the hon. Lady has said, which has been interesting. What consideration has she given to the need to co-operate on issues such as VAT in a world of global e-commerce that necessarily extends to many nations and millions of people outside the European Union?

**Kirsty Blackman:** That is a really interesting point, which highlights how much sovereignty has to be given away when agreeing a trade deal with another country. As the EU is a major player and a major consumer of our services exports—that is particularly relevant for e-commerce—we probably need to concentrate on agreeing a trade deal with it before thinking about deals with other countries. It is likely that the EU will want to talk about VAT when it makes trade deals with other third countries, too, so having a common relationship with the EU will probably be positive for us when we make deals with third countries.

I very much appreciate the chance to talk in this debate and make our priorities clear. If there is more flexibility over VAT and its devolution once the UK leaves the EU, I will call for the entirety of VAT to be devolved to Scotland. We have mentioned that before. Under the Scotland Act 2016, the top share of VAT is devolved to the Scottish Parliament. Although that is nice, it does not give us flexibility over policy levers, so I would call for further devolution in that situation.

9.38 am

**Jane Ellison:** I thank hon. Members for their contributions. I particularly thank the hon. Member for Aberdeen North, who spoke for the Scottish National party, for her wide-ranging contribution. I note that she made a bid with regard to police and fire services to add to the Treasury's £30 billion and counting of VAT bids. We have explored the issue of the VAT incurred as a result of the changed arrangements, so she will be

[Jane Ellison]

familiar with the point that I am going to make. That issue was in the business case for the changed arrangements. The Scottish Government were warned repeatedly that that would be the result of the way that they restructured emergency services, so it is surprising that the SNP keeps raising the issue as if the change was somehow imposed from the outside. The Scottish Government were alerted at the time. Our position on that remains unchanged, but as I said, I will add it to the list of things for which people want to see relief, along with the others that she mentioned.

I agree with the hon. Lady more—I think we both perhaps disagree slightly with the shadow spokesman for the Labour party—on her point that it remains very much in our interests to continue to engage with this debate. I will not speculate or second-guess the outcome of our Government's negotiations or where the EU Commission is going on this, but there is a mutual interest in smooth and competitive trading arrangements. European markets account for around half the UK's overall trade and foreign investments; around 3.5 million jobs. We will therefore continue to engage extremely actively and constructively while we are in the EU. However, it remains the case that even once we are outside it, the EU VAT system is influential. It is in our interests to ensure, to the extent that we can, that it is aligned with OECD and other international work, to take up the point made by my hon. Friend the Member for Wycombe that this debate is wider than the EU.

We will remain engaged and there is mutual benefit, not just because of businesses that have EU subsidiaries. Because of the cross-border nature of trade, there is mutual advantage in making sure that arrangements make sense, both within and without the EU. I reject the counsel of despair from the Opposition Front Bench that there is no point in doing this—there is every point.

**Peter Dowd:** I am surprised the Minister has taken that view. It is a complete distortion. We are talking in the context of the document before us. This debate is

specifically in relation to the document before us. It has taken years to get to this position. We are only two years from leaving the EU, and the idea that this has to do with post-Brexit negotiations is complete and utter tosh. Does the Minister agree that there is a difference between trying to saddle us, in relation to post-negotiation deals, with this and trying to deal with this specific issue? The two are completely different and the Minister should know that.

**Jane Ellison:** The Minister does know that, but the point I am making is that we are obviously in the EU until we are not. It continues to be in our interest to influence debate. I think I have engaged very directly with the shadow Minister's point. The point I have been trying to make is that this is a broader challenge than just within the EU. The international direction of travel on VAT remains important. The extent to which, for example, better co-operation is enshrined within new systems will provide better information on which we can help to shape policies around supplies across borders.

The OECD is already looking at ways to improve international co-operation, so there is every reason to continue to engage with this agenda. It is nonsense to say that it is irrelevant, even though we will be outside the EU in due course. The extent to which we have a degree of alignment in objectives and that direction of travel between the EU and other major trading blocs, and international trading and economic organisations such as the OECD remains fundamentally important because they have at their heart the desire to find some key principles around which we can all agree that will facilitate trade, less fraud and lower burdens on business across the piece.

I end where I began by saying that this is an important issue on which we will continue to engage while we are in the EU, and continue to influence in a number of different ways once we are outside it.

*Question put and agreed to.*

9.44 am

*Committee rose.*