PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT
GENERAL COMMITTEES

Public Bill Committee

FINANCE BILL

(Except clauses 5, 15 and 25 and certain new clauses and new schedules)

Second Sitting

Tuesday 17 October 2017

(Afternoon)

CONTENTS

PBC (Bill 102) 2017 - 2019

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not later than

Saturday 21 October 2017

The Committee consisted of the following Members:

Chairs: Mr George Howarth, † Mr Charles Walker

† Afolami, Bim *(Hitchin and Harpenden)* (Con)
† Blackman, Kirsty *(Aberdeen North)* (SNP)
† Burghart, Alex *(Brentwood and Ongar)* (Con)
† Cleverly, James *(Braintree)* (Con)
† Creasy, Stella *(Walthamstow)* (Lab/Co-op)
† Dodds, Anneliese *(Oxford East)* (Lab/Co-op)
† Dowd, Peter *(Bootle)* (Lab)
† Fernandes, Suella *(Fareham)* (Con)
† George, Ruth *(High Peak)* (Lab)
† Ghani, Ms Nusrat *(Wealden)* (Con)
† Hopkins, Kelvin *(Luton North)* (Lab)
† Hughes, Eddie *(Walsall North)* (Con)
† Lee, Ms Karen *(Lincoln)* (Lab)
† Linden, David *(Glasgow East)* (SNP)
† Maclean, Rachel *(Redditch)* (Con)
† O'Brien, Neil *(Harborough)* (Con)
† Smith, Jeff *(Manchester, Withington)* (Lab)
† Stride, Mel *(Financial Secretary to the Treasury)*
† Stuart, Graham *(Beverley and Holderness)* (Con)

Colin Lee, Jyoti Chandola, *Committee Clerks*

† attended the Committee

Public Bill Committee

Tuesday 17 October 2017

(Afternoon)

[Mr Charles Walker *in the Chair*]

Finance Bill

(Except clauses 5, 15 and 25 and certain new clauses and new schedules)

2 pm

The Chair: Mr Howarth made some preliminary announcements this morning regarding Committee proceedings, including permission for Members to remove their jackets if they wish to do so in this October heatwave. Before we come to clause 10, I understand that the Minister wishes to raise a point of order.

The Financial Secretary to the Treasury (Mel Stride): On a point of order, Mr Walker. I believe that in this morning's sitting, in response to a question from the hon. Member for Bootle, I may have inadvertently suggested that the Bill's changes to the money purchase annual allowance regime will result in a £70 million per annum cost to the Exchequer. I should have said that £70 million of revenue will be raised for the Exchequer in each year.

The Chair: I thank the Minister for that clarification, as I am sure does the entire Committee.

Clause 10

Personal portfolio bonds

Question proposed, That the clause stand part of the Bill.

Mel Stride: It is a great pleasure to serve under your chairmanship, Mr Walker. Clause 10 provides the power to amend by way of statutory instrument the property categories that the holder of a life annuity, life insurance policy or capital redemption policy can select without making that policy or contract a personal portfolio bond.

The personal portfolio bond rules introduced in 1999 countered avoidance arrangements where an individual could select personal investments, such as property portfolios, in life insurance policies to defer the tax charge on any resulting income or gains. The legislation treats a policy as a personal portfolio bond if it allows the holder to select the property held in that policy. A policy will not be a personal portfolio bond if it permits only the selection of property specifically listed in the legislation. The categories of property listed in the legislation have features that ensure that the policyholder cannot customise them to allow personal property to be placed within the policy.

The list of permitted property has not materially changed since the rules were introduced in 1999. Since then, various new types of investment vehicle have been developed that similarly cannot be manipulated to include personal property. Up to now, those have not been added to the list. That unnecessarily narrows the range of investment choices for policyholders.

The clause provides the power to make secondary legislation to amend the categories of property listed. The power will ensure that, in future, the rules can be updated more quickly to accommodate new types of investment vehicles. Following Royal Assent, the Government will lay regulations using the power to add three investment vehicles as permitted property: real estate investment trusts, overseas investment trust companies and authorised contractual schemes. Draft statutory instruments have been provided to the Committee. The power will allow the Government to respond quickly as new methods of investment develop, to enable legislation to keep pace with changes in the financial services industry and ensure that tax rules do not needlessly impede innovation and competition in the sector.

Anneliese Dodds (Oxford East) (Lab/Co-op): I am grateful to the Minister for providing clarification. Is there any evidence of the extent of awareness among fund advisers regarding the existing restrictions, and how will they be made aware of the new rules? That is particularly important if new rules are to be adopted through secondary legislation. We have heard about the new categories of property that might be incorporated, but there is likely to be less spotlight on them in future if we do not discuss them in the context of a Finance Bill. At present, it is possible for fund advisers to accidentally acquire non-permitted assets for a client's policy, which rules it out as a PPB and means that the rules on yearly deemed gain do not apply.

Mel Stride: I reassure the hon. Lady that there has been extensive consultation on the measure. The consultation on reviewing the list of properties ran from 9 August to 3 October 2016 and explored adding three types of investment vehicle. The majority of respondents welcomed the proposed addition of the investment vehicles discussed. Many suggested further additions, which will require further review before any recommendation is made.

Question put and agreed to.

Clause 10 accordingly ordered to stand part of the Bill.

Clause 11

EIS and SEIS: the no pre-arranged exits requirement

Question proposed, That the clause stand part of the Bill.

The Chair: With this it will be convenient to discuss clauses 12 and 13 stand part.

Mel Stride: Clauses 11, 12 and 13 make changes to the tax-advantaged venture capital schemes: the enterprise investment scheme, the seed enterprise investment scheme and venture capital trusts. The changes provide small but useful easing of the rules, which I shall explain in more detail. Following the calling of the general election and subsequent negotiations between the Government and the Opposition, these clauses were removed from the Finance Act 2017. As all the clauses are wholly relieving, the Government have introduced retrospective legislation to ensure that taxpayers can still benefit from the changes being made from the original commencement date.

The tax-advantaged venture capital schemes provide a range of generous tax reliefs to encourage individuals to invest directly or indirectly in certain smaller and higher-risk early stage companies. These small companies would otherwise struggle to access the funding they need to grow and develop, because they have little or no track record to attract funding from the market.

Clause 11 makes changes to an anti-abuse rule, the no pre-arranged exits requirement, in the enterprise investment and seed enterprise investment schemes. The rule prevents tax relief from being provided if arrangements under which the shares were issued might lead to a disposal of those or other shares in the company and so potentially put the future continuation of the company at risk.

Many companies include such rights in their standard documents. However, rights allowing for share conversions in the future carry no risk to the integrity of the scheme, as excluding the rights can be administratively burdensome for some companies. The changes will allow companies to qualify for relief if they issue shares that include rights to a future conversion into shares of another class in that company. The changes are wholly relieving and will apply retrospectively, with effect for shares issued on or after 5 December 2016.

Clause 12 makes technical changes to clarify the law and ensures venture capital trusts can provide follow-on funding to certain groups of companies. The changes ensure that the VCT rules work in the same way as those for EIS. The rules for VCTs and EIS were changed in late 2015 to target the schemes more closely on early stage companies. However, the rules do allow older companies to receive tax-advantaged investments in some situations. These include follow-on funding provisions. Broadly speaking, follow-on funding may be provided to an older company as long as the company received its initial tax-advantaged funding at a time when it met the basic age limit. The changes made by clause 12 ensure that, where certain conditions are met, VCTs will be able to provide follow-on funding for companies that have been taken over by a new holding company after the initial funding was received.

Clause 13 makes changes to extend a power for the Treasury to make regulations on the exchange of certain investments held by a VCT. A VCT may hold non-qualifying investments, but only in very limited circumstances. Regulations under the current power ensure that VCTs are not at immediate risk of losing their approved status when they are obliged to exchange a qualifying investment for a non-qualifying investment. However, the power to make regulations applies only where the original investment is a qualifying investment.

The new regulations will provide broadly similar protection to VCTs where the original investment is a non-qualifying investment and the VCT is similarly required to exchange the investment as part of a commercial reorganisation or buy-out. Without the new regulations, VCTs would continue to rely on Her Majesty's Revenue and Customs exercising its discretion to avoid immediate loss of approval when a non-qualifying investment is exchanged. Draft regulations will be published for public consultation later in the year. The regulations will provide certainty to a VCT regarding the treatment of the new shares or securities obtained when it exchanges non-qualifying investments.

Clauses 11, 12 and 13 make technical easements to reduce administrative burdens and smooth certain rules within the tax-advantaged venture capital schemes. I therefore hope that they will stand part of the Bill.

Anneliese Dodds: I have two questions about clauses 11 and 12. First, EIS and SEIS are two of the four tax-advantaged venture capital schemes, alongside venture capital plus and social investment tax relief, which we will discuss under a later clause. In addition to the features mentioned by the Minister, the schemes share in common the fact that advance assurance applications and submissions of statutory compliance statements are often sought by those seeking to reassure potential investors about the tax treatment of their investments. Clearly, the new requirement will widen eligibility for EIS and SEIS, potentially leading to a greater number of requests to HMRC for these kinds of ex-ante assessments. I would be grateful if the Minister could assure us that HMRC will be able to satisfy those requests in a timely manner.

I understand from the Minister's response to my parliamentary question on this matter that there is no time limit on an advance assurance application, and while the target for more complex cases is 40 days, he admitted that more complex cases may take longer. Although I agree with him that the changes will simplify the administrative side for business to an extent, they could complicate qualifying criteria from HMRC's point of view. How will the Minister ensure that that does not lead to greater pressures on an already struggling HMRC?

On clause 12, my second question is perhaps more fundamental. As I understand it, EU state-aid rules generally suggest that the operation of such tax reliefs should focus on genuinely promoting new growth rather than on the acquiring of existing businesses, given that we are talking about the state exempting certain categories of firms from tax that others must pay. Will the Minister provide us with a taste of how he has assured himself that this relief genuinely will focus on the promotion of such new growth?

Mel Stride: I thank the hon. Lady for her questions. On clause 11, she has been in touch with the Treasury about the important matter of advance assurances from HMRC, which always does its utmost to provide advice in as timely a manner as possible. The change proposed by the clause, however, is to remove a requirement on HMRC to opine on the approach that some companies intend to take, which will introduce greater certainty.

Clause 12, which relates to VCTs and the introduction of a parent company, is also likely to ease the investment decision because it will take away the uncertainty that would otherwise accrue by having a parent company inserted into the corporate structure under consideration. These technical amendments therefore make important changes to existing legislation.

Question put and agreed to.

Clause 11 accordingly ordered to stand part of the Bill.

Clauses 12 and 13 ordered to stand part of the Bill.

Clause 14

Social investment tax relief

Question proposed, That the clause stand part of the Bill.

The Chair: With this, it will be convenient to discuss the following:

Amendment 20, in schedule 1, page 103, line 37, at end insert—

"10A After section 257TE (minor definitions etc), insert—

"257TF Review of operation of this Part

(1) Prior to 30 June 2019, the Commissioners for Her Majesty's Revenue and Customs shall complete a review of the operation of social investment tax relief.

(2) The review shall consider in particular—

(a) the effects of changes made to this Part by Schedule 1 to the Finance (No. 2) Act 2017, and

(b) the effectiveness of the anti-abuse provision.

(3) The Chancellor of the Exchequer shall lay a report of the review under this section before the House of Commons as soon as practicable after its completion.""

This amendment would require HMRC to undertake a review of the operation of social investment tax relief, including the changes to it made by Schedule 1.

That schedule 1 be the First Schedule to the Bill.

Mel Stride: Clause 14 and schedule 1 make changes to increase the amount of investment that newer social enterprises can raise through social investment tax relief. These changes will make social investment more attractive to a wider range of enterprises and investors. Excluding lower risk activities will ensure that the scheme is well targeted and delivers value for money.

Would it be in order, Mr Walker, to speak now to amendment 20 and schedule 1?

The Chair: If the Minister sits down, the Opposition can speak to the amendment.

2.15 pm

Anneliese Dodds: As the Minister has indicated, amendment 20 is to the schedule, which is grouped with clause 14. We have a number of concerns about the proposed changes to social investment tax relief, which is why our amendment asks for a review of their effectiveness and impact.

As colleagues will be aware, social investment tax relief is aimed at supporting social enterprises, comprising those businesses that plough their profits—or at least a proportion of them—back into a social and/or environmental mission. With this relief, where investments by individuals are eligible, they can reduce an individual's income for income tax purposes by almost a third. It is clearly a significant relief and one that, while having many positive impacts, has been suggested as leading to abuses, with the social or environmental impacts from investment in some anecdotal cases being cosmetic rather than actual.

There are also underlying issues about whether there is a level playing field between social enterprises and the public sector when it comes to the delivery of some public services, which could be intensified by the development of additional scope or type of tax reliefs when it comes to social enterprises. Indeed, for those reasons, some people have entirely rejected even the principle of social investment tax relief in the first place. I understand Dame Hilary Blume, director of the Charities Advisory Trust, was concerned about the creation of the relief in the first place, saying it would attract those interested in profits rather than social good to the sector.

In my experience as a constituency MP—and others may share this experience—social enterprises that operate in my constituency, such as the charity Aspire Oxford, undertake work that the Government either have never done or which they have abandoned due to a lack of resources, such as the enormous reductions in support provided through probation services. It is important that organisations such as these, which genuinely deliver additionality, are supported. Nonetheless, in that context, we have a variety of concerns about the currently proposed changes and it is for that reason that we ask for a review. I would be grateful—even if our amendment does not pass—if the Minister could provide answers to a number of these concerns, presently or by letter in the future.

The first concern we have is about the process surrounding these measures. As colleagues will know, rather confusingly, not all social enterprises qualify for social enterprise relief. Predominantly, the relief is focused on community interest companies, charities and community benefit societies. For that reason, before receiving investment, many social enterprises ask HMRC for advance assurance—this topic pops up again—that they will qualify for SITR. I am concerned to have learned from the sector that assessors seem to have been taking decisions already about whether social enterprises will qualify for SITR on the basis of the rules we have in front of us today, which have not yet been passed by Parliament, rather than on the basis of the current rules.

I know the rules would have retrospective impacts: in practice they would be for investments dating from 1 April. It seems strange, however, for assessors to be taking decisions already on the basis of the new rules and this is potentially a disadvantage for social enterprises that are negatively affected by the new rules.

I have also heard concerns about the new treatment of leasing within the new provisions. As I understand it, the Government conceive of leasing as an inherently low-risk activity and therefore not worthy of subsidy, but it is not clear to me that all the implications of this position have been thought through. An example is that of a specialist facility, such as a rundown heritage swimming pool. In fact, many of us may have those in our constituencies—as we know, many have closed. It is very difficult for local authorities to redevelop those facilities in current financial circumstances. We could imagine an example where a social enterprise might want to take on that pool, purchase it, attract investors into that project, but not run the swimming pool themselves as they do not have the expertise to do so. They might then want to have a leasing arrangement with a specialist leisure provider to deliver the services from that swimming pool. The problem with the new changes is that, in this context, even though the risk of that new approach would be reduced because the specialist provider would have more experience of running swimming pools than the social enterprise, the latter would be left in an invidious position, because it would lose the tax break if it engaged in that kind of leasing arrangement.

Stella Creasy (Walthamstow) (Lab/Co-op): My hon. Friend is making a powerful case about the importance of trying to make these kind of rules work for the reality of how social investment often happens in our local communities. Does she agree with me that there is also a concern that by excluding asset-leasing, things like community pubs and community land trusts might also be excluded by the Government, probably unintentionally? Many of us know of small community groups that may want to take over pubs in our communities that would be excluded by this measure and unintentionally actioned against. Surely we should be acting on that.

Anneliese Dodds: I am grateful to my hon. Friend for making that point, and I agree that this could apply to a range of different facilities. In many circumstances, this kind of arrangement is the only way to keep those facilities going. We could see them entirely disappear—we all know about the sad disappearance of community pubs in our areas—so I am grateful to her for making that point.

In addition to those potential issues, we are also concerned about the differential treatment of social enterprises by age, with the £1.5 million cap being lifted for social enterprises under seven years old. Will the Minister explain why there is precisely this seven-year limit? It may in practice be that local authorities are relying on well-established, well-run and highly experienced social enterprises to help to provide essential services and facilities in conditions of extreme budget cuts, but it is those older enterprises that are potentially disadvantaged by this scheme. I hope that we are going to learn the exact decision-making process on this seven-year cut-off point. If it is specifically to advantage younger social enterprises, why is that the point? Is it the case that youth is being viewed as a proxy for the ability to take on risky activities? If so, where is the evidence basis for that?

I point again to the example of Aspire in my constituency that operates a range of programmes, including one that supports offenders going into work—people who would not normally necessarily be taken on by different employers. Surely that is a highly risky activity, but it is one at which they—as an established social enterprise—excel. Age does not necessarily appear to be a good proxy for the ability to take on riskier activities. If this seven-year cut-off is not there to encourage younger social enterprises, then why has it been instituted? We need more information on this.

Finally, we feel that additional evidence on the effectiveness of the anti-avoidance clauses within the new provisions is required. Social enterprises in the voluntary sector have a long history in areas such as hospice care, specialist domestic violence and mental health services where they have often genuinely driven innovation. Other social enterprises, such as those I mentioned earlier, have merely donated some of their profits to charity, rather than having a genuinely social or environmental mission. May we have more clarification on how abuse will be identified and dealt with?

Kirsty Blackman (Aberdeen North) (SNP): I do not want to speak for long, but I wanted to say that the hon. Member for Oxford East made a comprehensive, passionate and well-informed case on the amendment. If the Labour party seeks to press the amendment to a vote, we will support it. If the Minister responds to any of the comments by letter, I would be keen to see some of his answers, so I would appreciate being copied into that response.

Mel Stride: Compared with typical companies, social enterprises face greater difficulties in accessing the funding they need to grow and develop. Social investment tax relief provides a number of generous tax reliefs to encourage individuals to invest in social enterprises that deliver social or community benefits. The current limit to the amount of investment that a social enterprise can receive through SITR is around £300,000 over three years. We announced in 2014 that we would look to expand the scheme, and we are now doing so.

The changes made by schedule 1 will increase the investment limit to £1.5 million over the lifetime of all social enterprises using SITR. In order to target the relief more effectively at the social enterprises that most struggle to attract investment, those under seven years old will no longer be bound by the three-year rolling investment limit of £300,000. I think this addresses the issues raised by the hon. Member for Oxford East about why the period is seven years. There is a greater vulnerability when social enterprises start up and they are fresh and young. They have yet to have a track record on which they can build, in order to grow. For those we are removing the roaming £300,000 over three years requirement. Social enterprises older than seven years can still use SITR for investment up to the three-year rolling investment limit of £300,000, subject to the lifetime limit of £1.5 million.

Schedule 1 makes a number of other changes to ensure that the scheme is well targeted at activities that will genuinely achieve socially beneficial aims, and provides value for money. That includes targeting SITR at social enterprises with fewer than 250 employees. Some activities have always been excluded from the relief so that it is not used as a tax-advantage route for low-risk investment. The excluded activities list will be updated to exclude a number of low-risk activities, including leasing assets and raising finance to lend on to others.

I agreed wholeheartedly with the hon. Member for Oxford East's assertion about the importance of these social enterprises. She mentioned Aspire, for example, in her own constituency and many of us can think of similar organisations in our constituencies. On the more detailed process points that she was interested in, particularly around HMRC and advanced assurances, I am happy to write to her.

On the specific issue of leasing, allowing those activities to benefit from SITR would risk diverting finance away from higher risk social enterprises. We must not lose sight of the fact that the whole purpose of this scheme is to encourage those kinds of organisations and all the good works that they do, which might not otherwise come forward for the reason of being high risk. Of course, those organisations struggle the most to raise finance. Leasing assets typically provides a reliable income stream, which makes it a lower risk activity. Allowing social enterprises to raise money to lend on to other enterprises would be complex to administer and would leave the scheme open to misuse.

Stella Creasy: As a Co-op, as well as Labour, MP, I am rather passionate about the idea of social investment. The Minister seems to be a little short-sighted about the

[Stella Creasy]

idea of assets—after all, there are many people looking at running community pubs, for instance, which is a great example of a community asset that we might want to support. I would not see that as an example of a low-risk venture. Surely, if he accepts our amendment, we can look at some of those issues and make sure that he is not missing out on some of the things he would like to see investment in because of a concept of risk that is rather narrow, rather than recognising some of the boundaries of co-operative and social investment.

Mel Stride: I thank the hon. Lady for her intervention. I guess there is a trade-off between getting very detailed and more precise in where we target these kinds of reliefs and, on the other hand, sometimes having complexity and confusion. It can be difficult to winkle out the precise anomalies that she may be alluding to. However, I can reassure her that, under the EIS scheme, many pubs, including community pubs, can qualify. They may be excluded under certain circumstances within the SITR scheme, but under EIS she will find that there are at least possibilities.

On the general issue of anti-avoidance, we are seeking to avoid situations where these schemes—whether they are EIS, SITR or VCTs—are simply being used as places to preserve capital at very little risk and to give a tax return as a consequence of the scheme. It is important that we have tight, sensible and effective avoidance measures in place.

Finally, further provisions to align the rules more closely with the enterprise investment scheme, including anti-abuse provisions, will also be introduced. Amendment 20 would require a review of the effects of the scheme, including the effectiveness of the anti-abuse provision and other changes being made by schedule 1. The Government have already committed to a full review of SITR within two years of its expansion. An early review would make it impossible to adequately gauge the effectiveness of the provisions that we are introducing now. Further, these anti-abuse provisions were introduced in direct response to HMRC becoming aware of the creation of aggressive tax-planning structures designed to exploit this relief. We estimate that around 800 social enterprises will benefit from the relief over the next five years. By 2021-22, SITR is forecast to cost £65 million per year, £30 million more than if the scheme was not enlarged.

We have had an interesting debate on the scheme. As we have already committed to a full review, I ask the hon. Member for Oxford East to withdraw amendment 20. Schedule 1 will increase the amount of investment that social enterprises can raise through SITR making it attractive to a wider range of enterprises and investors. Other changes will ensure that the scheme is well targeted and delivers value for money.

2.30 pm

Anneliese Dodds: I am grateful to the Minister for his clarification, which has been enormously helpful. However, he referred to winkling out particular anomalies and we feel that that is exactly what we need a little more of. On the issue of the seven years of activity as a social enterprise before qualifying for the three-year £1.5 million cap, I am concerned, despite the Minister's helpful comments, that we are not focusing on the exact loci of risk. We seem to be assuming that risk is inherent in the age of the social enterprise concerned and not on the activity that it is engaged in. It is perfectly possible—I mentioned an example earlier—for an older social enterprise to try to attract funding in order to undertake a very risky activity. Dealing with some of those risky activities is what we need social enterprise to be engaged in, particularly as we have many areas where local authority funding is no longer available and there are also market failures. We really need to have community facilities and different services preserved. I therefore wish to press the amendment.

Mel Stride: I think we are in total agreement with the hon. Lady on the issue of focusing these funds and incentives on riskier social enterprises, in other words, the ones that would not naturally happen without this kind of intervention. However, while those that are less than seven years old will be subject to the £1.5 million cap, which is a considerable increase in what we have had before and will not be restricted by the £300,000 maximum investment in any three-year period, those social enterprises that have been trading for longer than seven years, can still have access to £1.5 million in total, albeit in any three-year period they are restricted to £300,000 maximum to be raised. It is not as if there is a terrible cliff edge between the two. We will still be providing a lot of support for older social enterprise.

Anneliese Dodds: I thank the Minister, but I am still concerned about why exactly seven years has been chosen as the cut-off. Listening to his helpful remarks, I imagine that we could see some gaming around this, because there is a significant tax advantage from having a younger social enterprise. Would we see social enterprises being created out of previous ones just to qualify for the different tax treatment when actually they would be focused on the same activity? It seems peculiar to me and I do not understand why the seven-year figure has been chosen. My dad was an accountant; he always said to me, "You've got to keep your bank statements for seven years", so I can understand seven years from that perspective. Why is there no gradation? Why seven and not another figure—three, five, 15 or 20 years? Perhaps some clarification can be provided.

Mel Stride: I suppose we are saying that whatever number of years we chose, the hon. Lady's argument would always be relevant, in the sense that it is an arbitrary figure. It happens to be seven years in this case. In terms of anti-avoidance and gaming at the margins, to which she referred, there are some strong anti-avoidance measures in the Bill that, for example, seek to address directly the specific issues she raised of perhaps one social enterprise taking over another that has a different age profile and in some way gaming the system as a consequence. Those elements are addressed in the anti-avoidance measures.

Question put and agreed to.

Clause 14 accordingly ordered to stand part of the Bill.

Schedule 1

Social investment tax relief

Amendment proposed: 20, in schedule 1, page 103, line 37, at end insert—

"10A After section 257TE (minor definitions etc), insert—

"257TF Review of operation of this Part

(1) Prior to 30 June 2019, the Commissioners for Her Majesty's Revenue and Customs shall complete a review of the operation of social investment tax relief.

(2) The review shall consider in particular—

(a) the effects of changes made to this Part by Schedule 1 to the Finance (No. 2) Act 2017, and

(b) the effectiveness of the anti-abuse provision.

(3) The Chancellor of the Exchequer shall lay a report of the review under this section before the House of Commons as soon as practicable after its completion.""—*(Anneliese Dodds.)*

This amendment would require HMRC to undertake a review of the operation of social investment tax relief, including the changes to it made by Schedule 1.

Question put, That the amendment be made.

The Committee divided: Ayes 9, Noes 10.

Division No. 5]

AYES

Blackman, Kirsty
Creasy, Stella
Dodds, Anneliese
Dowd, Peter
George, Ruth
Hopkins, Kelvin
Lee, Ms Karen
Linden, David
Smith, Jeff

NOES

Afolami, Bim
Burghart, Alex
Cleverly, James
Fernandes, Suella
Ghani, Ms Nusrat
Hughes, Eddie
Maclean, Rachel
O'Brien, Neil
Stride, rh Mel
Stuart, Graham

Question accordingly negatived.

Schedule 1 agreed to.

Clause 16

Calculation of profits of trades and property businesses

Question proposed, That the clause stand part of the Bill.

The Chair: With this it will be convenient to discuss that schedule 2 be the Second schedule to the Bill.

Mel Stride: Clause 16 makes changes to ensure that landlords can use the cash basis to calculate their profits for tax, and simplifies the treatment of capital expenditure within the cash basis.

At Budget 2016, the Government announced that we would explore options to simplify the tax rules for businesses, self-employed people and landlords. Trading businesses have been able to use the cash basis method of calculating their profits for tax since 2013. The method calculates profits on a cash in, cash out basis and minimises the need for complicated accounting adjustments. It has been well received; more than 1 million trading businesses have chosen to use the cash basis since its introduction. Extending and improving the cash basis is a significant step to simplify the tax rules.

Following consultation, the Government announced that from April 2017 they would increase the cash basis threshold for traders to £150,000, extend the cash basis to some landlords, and simplify the treatment of capital expenditure in the cash basis. The increase to the cash basis threshold for traders was implemented by secondary legislation, so does not appear in the Bill.

The changes made by the clause will allow more than 2.3 million property businesses to choose to use the simpler cash basis method of calculating their profits for tax, which will provide administrative savings to approximately 1.8 million of them. The changes to the treatment of capital expenditure in the cash basis will allow capital expenditure to be deducted from income, unless it relates to specific types of assets listed in the legislation. That will mean that, including any additional property businesses, nearly 3 million businesses using the cash basis will have a clearer idea of what they can deduct for tax, and when.

The clause legislates for measures announced at spring Budget 2017 and takes effect from April 2017. It therefore has retrospective effect. The measures will simplify tax on many businesses and landlords, who will benefit from the use of the cash basis and the reform of the capital expenditure rules in the cash basis.

Question put and agreed to.

Clause 16 accordingly ordered to stand part of the Bill.

Schedule 2 agreed to.

Clause 17

Trading and property allowances

Question proposed, That the clause stand part of the Bill.

The Chair: With this it will be convenient to discuss the following:

Amendment 21, in schedule 3, page 155, line 15, at end insert—

"**Chapter 3**

Review of chapters 1 and 2

783BR Review of operation of this Part

(1) Prior to 30 June 2020, the Commissioners for Her Majesty's Revenue and Customs shall complete a review of the operation of the provisions of this Part.

(2) The review shall consider in particular—

(a) the use and effects of full relief,

(b) the use and effects of partial relief,

(c) the use of relief in relation to trading income, and

(d) the use of relief in relation to property income.

(3) The review shall compare the effects on the Exchequer in each of the first two years of its operation with the effects forecast by the Office for Budget Responsibility at the time of—

(a) the 2016 Budget, and

(b) the 2016 Autumn Statement.

(4) The Chancellor of the Exchequer shall lay a report of the review under this section before the House of Commons as soon as practicable after its completion."

This amendment would require HMRC to undertake a review of the operation of the new trading and property allowances in the first two relevant tax years.

That schedule 3 be the Third schedule to the Bill.

Peter Dowd (Bootle) (Lab): It is a pleasure to serve under your chairmanship, Mr Walker.

I appreciate that the strictures of Finance Bill procedure commonly give rise to the overwhelming excitement of review amendments, so I ask the Committee to withhold its lack of surprise that amendment 21 would introduce yet another review. The Government's sensible stated aim in introducing the allowance is to recognise that

[Peter Dowd]

many taxpayers no longer fit within a neat and simple model of PAYE-only income or self-assessment-only income. We all recognise that that is the reality, but we should not get too carried away by the idea that online hobby trading is an entirely new activity triggered by the advent of the online sharing economy; I suspect it is more like old wine in new skins. Spending a weekend repairing a few clocks as a hobby and then selling them on eBay for extra income on the side is not an entirely new phenomenon. People 20 years ago did the same through car boot sales, antique fairs or classified ads; this is just a modern version.

Modernising the tax system to recognise the multiple sources of income that taxpayers may now receive is sensible, but we should not always imagine that the problems that we are trying to solve are entirely new, nor should we make too hasty a stab in the dark for solutions. The Association of Taxation Technicians says that, as drafted, the provisions discriminate against individuals who, in addition to having the type of microbusiness to which the trading allowance is intended to apply, also have a sole trader business which cannot benefit from the trading allowance. In that situation, the provisions prevent the microbusiness from qualifying for the trading allowance. The ATT's concern is that the allowance is potentially discriminatory.

The Government state that the aim of the allowance is to provide

"simplicity and certainty regarding Income Tax obligations on small amounts of income from providing goods, services, property or other assets…and to help the UK become leaders in the digital and sharing economy",

but it could easily end up creating new complications for taxpayers, or lead inadvertently to perverse incentives. The Chartered Institute of Taxation's Low Incomes Tax Reform Group welcomes the aim of the measures, but has said that it is

"very concerned that unrepresented low-earners will struggle to understand some of the more complex rules, especially if they have overlap profits, more than one trade or source of income or have not elected, as often will be the case, to use the cash basis of accounting."

Its concerns stem especially from the fact that this relief's intended group of users is less likely to engage professional accountants or other advisers. As a result of the complications involved in having to choose a particular accounting basis or work out the types of income that apply, the allowance may fail to benefit that group of users. It may instead become yet another strand in the complex web of allowances that professional advisers throw into the mix when helping their clients to avoid tax.

Anneliese Dodds: I appreciate my hon. Friend's comments about the role of personal advisers; the same point came up this morning. Moreover, has not HMRC's online system for calculating the taxes payable on relatively small amounts of income already been found wanting? As a result of the interaction between the four different allowances—personal savings, tax-free dividend income, the savings starting rate and the personal allowance—individuals have become liable for more tax than they should have to pay, because the online system is not calibrated appropriately. In theory, the new provision is meant to obviate the need to declare income for those purposes, but does my hon. Friend not agree that it must be designed carefully to avoid the flaws that affect people with small incomes who qualify for the allowances?

2.45 pm

Peter Dowd: My hon. Friend hits the nail on the head; that is an excellent forensic point that the Minister will have heard, and will, I hope, take up, especially in relation to our amendment.

The potential problems might be still bigger in the case of property income where the new relief interacts with existing schemes such as rent-a-room relief. Taxpayers will need to work out which relief applies before determining whether and how they need to make a self-assessment return. Although I am confident that the Minister is genuine in his desire to help more people get on the right side and make the right declarations for their taxes, I worry that the added complexity could easily put off more people from making the correct declaration. I suspect that none of us wants that, including him, because it is not particularly sensible. In many cases, it will not be due to anyone's desire for dishonesty; it will be because taxpayers used to operating only within pay-as-you-earn will be confronted with a confusion of options in considering how they must declare to HMRC.

The Low Incomes Tax Reform Group has rightly highlighted the complications that might arise for lower-income households. The new reliefs might free taxpayers from the need to declare very small amounts to HMRC, but will not have the same effect of releasing their obligations to account to the Department for Work and Pensions if they are universal credit claimants. Those are the households that would benefit most from simplification, rather than finding themselves subject to the most bewildering requirements to account to the state. I do not wish to waylay the Committee with the ongoing issue of universal credit implementation, as we will undoubtedly have a debate about that tomorrow, but the Low Incomes Tax Reform Group highlights a fair point: so-called simplifications involving tax and social security can sometimes have the opposite effect on those expected to use them. I think that we have all witnessed that to a greater or lesser degree.

Our amendment proposes an HMRC review, to report by 2020, of the use of the reliefs and the resulting effects on the Exchequer. I know that the inclination is to resist all Opposition amendments, but I can see little cause to resist this one. Inevitably, just like other measures discussed earlier, the reliefs will be revisited, unpicked, reworked and recalibrated in future Budgets. Sensible and calm review by HMRC must be in the interests of everybody involved.

Kelvin Hopkins (Luton North) (Lab): It is a pleasure to serve under your chairmanship, Mr Walker. I support my hon. Friend the Member for Bootle. It is said that Britain has more accountants per head of population than any other country, probably because the complexity of our tax system means that we all need to use one. However, in this situation, as he said, the amounts involved might be small, and the cost of an accountant might be quite high. That could deter people from using accountants, getting them into more difficulty.

Is there not a case for a proper review by HMRC, which knows the score because it deals with such things on a daily basis? HMRC could advise the Government on introducing appropriate changes that would simplify the tax system as well as helping those who would benefit from tax reliefs in a more practical and pragmatic way.

Mel Stride: Clause 17 and schedule 3 introduce two new tax allowances so that, from April 2017, individuals with gross trading or property income below £1,000 no longer have to declare or pay tax on that income. Digital platforms are allowing more and more people to supplement their income by sharing property, resources, time and skills. It is perhaps a rather more rapidly growing segment than the hon. Member for Bootle recognised. The UK is a world leader in the sharing economy; a report by PwC shows that the UK sharing economy has grown at the fastest pace in Europe, with transactions worth about £7.4 billion in 2015. This is expected to grow to £140 billion in 2025.

As the economy changes, the tax system should keep pace. For this reason the Government want to support the sharing economy and ensure that the tax system is not burdensome for those making small amounts of income, whether through selling goods, providing services or renting out their property. This could include those advertising their plumbing services through an online platform or those renting out a driveway space, for example. The changes made by clause 17 will introduce two new income tax allowances so that the individuals with gross trading or property income below £1,000 will no longer have to declare or pay tax on that income. Many individuals engaging in these activities on a small scale are not aware of their tax obligations. The new allowances make these obligations clear and straightforward, providing much needed clarity for people making small levels of extra income.

The trading allowance will also include miscellaneous income from providing assets or services, creating certainty for individuals, who will not have to understand tax case law to determine whether their activities should be taxed as a trade. The Government estimate that at least 700,000 individuals could benefit from the allowances. Over three quarters of these are basic rate taxpayers who could save up to £400 in income tax each year.

The Opposition raised a number of points. One was the lack of availability of this allowance to those who are already making self-assessments to HMRC, because they are already sole traders. Part of the reason for that is to ensure that we do not have any diversion of activity from those individuals' general work arrangements into this scheme driven solely by an attempt to lower taxation. The point has been made about the importance of simplicity in the scheme. Certain aspects of the scheme clearly make it simple: people with that kind of income are not required to make a submission to HMRC, and there is a "miscellaneous" category of income that can address the complications around whether this is trading income—"miscellaneous" is quite a wide-ranging term.

The hon. Member for Bootle raised a fair point on rent-a-room tax relief arrangements; that is why HMRC's efforts in detailing its guidance on the gov.uk website are so important. All the allowances will be very carefully explained. The guidance is being prepared alongside representative bodies and will include clear, step-by-step explanations and a number of examples, so it will be very easy for people to follow exactly how the arrangements work. Support will also be available via the HMRC helpline.

Amendment 21 would require HMRC to complete a review of the cost and effectiveness of the allowances by 2020 and the effects on the Exchequer in each of the first two years. Such a review is unnecessary. As I have set out, the two new allowances ensure that the tax system is not burdensome for those making small amounts of income. Their effect will be to support the enormous contribution that the sharing economy is making to the UK economy, while simplifying the tax system to support the job creators of the future. As there is no need for taxpayers to declare this income to HMRC, any review would impose a disproportionate burden on taxpayers and be inconsistent with the core rationale for the reliefs. In addition, the Bill also includes specific clauses designed to prevent abuse, and HMRC will carefully monitor the reliefs to ensure that they work as intended. I therefore urge the Committee to resist this amendment.

The two new tax allowances will help micro-entrepreneurs by removing complexity and uncertainty for those wanting to earn small amounts of extra income. There will be no forms to fill in and no tax to pay. It is a tax break for the digital age, furthering the Government's commitment to simplify the tax system and help the UK become a global leader in the digital and sharing economy. I therefore commend the clause to the Committee.

Peter Dowd: We will not press the amendment to a vote but the Minister acknowledges, de facto, that the economy and the world of work is changing fast. There are so many developments out there—apps, online, the whole kit and caboodle—which is all the more reason for the Government to keep on top of this issue. That is why we want the review, because the world changes so quickly.

Ruth George (High Peak) (Lab): Obviously, universal credit is being rolled out. That will be a particular detriment to people on very low incomes who are self-employed, because they will be deemed to earn the minimum wage on 35 hours a week throughout the year: around £13,600. If their actual income is below that at the moment, they can receive tax credits and are eligible to apply if they have children and a family. Under universal credit, they will not be able to receive such payments, though they may be liable for tax. That is another reason why a review after the roll-out of universal credit would be particularly useful, to see the impact on the self-employed and people with micro-businesses.

Peter Dowd: My hon. Friend makes a valid point. This is not quite as simple as the Minister would like us to believe, although I am not suggesting that he is trying to cajole us into it. The bottom line is that we will not push this to a vote today but we hope that the Minister takes into account the views we have expressed. If he does not wish to take account of our views, I exhort him to consider those of at least the two organisations that sent us documentation on the matter.

Question put and agreed to.

Clause 17 accordingly ordered to stand part of the Bill.

Schedule 3 agreed to.

Clause 18

Carried-forward Losses

Question proposed, That the clause stand part of the Bill.

The Chair: With this it will be convenient to discuss the following:

Amendment 22, in schedule 4, page 230, line 37, at end insert—

"188FAA Review of operation of this Part

(1) Prior to 30 June 2020, the Commissioners for Her Majesty's Revenue and Customs shall complete a review of the operation of the provisions of this Part.

(2) The review shall consider in particular—

(a) the use and effects of reliefs under this Part,

(b) the effects on the Exchequer in each year of operation,

(c) a comparison of the amounts referred to in paragraph (b) and any official forecasts of those amounts prior to the introduction of this Part.

(3) The Chancellor of the Exchequer shall lay a report of the review under this section before the House of Commons as soon as practicable after its completion."

This amendment would require HMRC to undertake a review of the operation of the provisions for group relief for carried-forward losses.

Amendment 23, in schedule 4 page 247, line 2, at end insert—

55A (1) Prior to 30 June 2019, the Commissioners for Her Majesty's Revenue and Customs shall complete a review in accordance with the provisions of this paragraph.

(2) The review shall consider the changes made in—

(a) paragraphs 24 to 26 of this Schedule in relation to insurance companies,

(b) paragraphs 27 to 46 of this Schedule in relation to certain creative industries,

(c) paragraphs 47 to 55 of this Schedule in relation to oil activities.

(3) The review shall consider in particular and in relation to each of the sectors mentioned in sub-paragraph (2)—

(a) the use and effects of the changes made,

(b) the effects on the Exchequer in each year of operation,

(c) a comparison of the amounts referred to in paragraph (b) and any official forecasts of those amounts prior to the introduction of this Part, and

(d) any effects on the economic activities of companies and others in each of the sectors mentioned in sub-paragraph (2).

(4) The Chancellor of the Exchequer shall lay a report of the review under this paragraph before the House of Commons as soon as practicable after its completion."

This amendment would require HMRC to undertake a review of the operation of the provisions for carrying forward trade losses for insurance companies, creative industries and oil activities.

That schedule 4 be the Fourth schedule to the Bill.

Clause 19 stand part.

Peter Dowd: These two clauses and the schedule represent the most complicated measures in the Bill, as I suspect everybody acknowledges. The corporate tax system and its rules on carrying forward losses present a maze of regulations and rules to be navigated by the heads of companies before they can claim relief. There is, therefore, some merit behind the Government's measures to relax the rules around losses.

Under these measures, companies can set losses arising on 1 April this year against the total taxable profits, rather than particular types of income of a company and its group members. The amount of losses they can carry forward will be restricted to 50% and will apply to any losses incurred at any time. Of course, on top of that, each company or group will be entitled to a £5 million annual allowance of unrestricted profit, ensuring that 99% of companies are unaffected by the restriction.

I would like to ask the Minister how the £5 million figure for the annual allowance was reached. In addition, what consideration has the Treasury given to lowering or raising the threshold for unrestricted profit? The reforms being discussed today were first announced at the 2016 Budget. The Government then consulted on the measure in the business tax road map, as it was called, which I understand has led to this package of clauses and schedule.

The changes to the current rules have been encouraged because, under the old system, companies could offset all their eligible taxable profits through losses carried forward. That led to a situation where in some instances a large company pays no tax in a year when it makes a substantial profit. The majority of G7 countries already have restrictions of this kind in place.

I believe it is important to look at international comparisons and examine how other countries deal with this complex issue. From my research, it is clear that the big distinctions on how countries focus on carried-forward losses are: the length of time losses can be carried back; the length of time losses can be carried forward; and when losses can be shared with other companies.

3 pm

First, we can see that the length of time that losses can be carried back to allow a refund of previous tax paid varies in other countries. In Australia, there is no limit, while the length of time is two years in the United States, and three years in Canada. Similarly, the length of time that losses can be carried forward to future years and offset against future profits is wide-ranging. The limit is 10 years in Canada and 20 years in the United States. In the UK and Australia, the length of time is indefinite. The final distinction is on when losses in other countries can be shared with other taxpayers, such as parent and/or sister companies. On that note, will the Minister inform the Committee how much work the Treasury has undertaken in examining and comparing the approaches that other countries take to carried-forward losses? What merit is there in the UK Treasury adopting best practice?

The anti-avoidance measures in clause 19 specifically will extend the loss refresh anti-avoidance rules in the Corporation Tax Act 2010 that prevent arrangements designed to convert carried-forward losses into in-year losses, which can be used more flexibly in terms of carried-forward UK property business losses and carried-forward non-trading losses on intangible fixed assets.

The measures will also change the timeframe within which a major change in the nature or conduct of a trade can occur. That timeframe will be extended from a period within three years of a change to a company's ownership to five years. That extended timeframe applies only where the change in ownership and the major change in the nature and conduct of a trade occur on or after 1 April 2017. The Government state in the explanatory notes:

"This change will ensure that where a company undergoes a change in ownership, and a major change in its business (within the relevant timescale) that involves a major change in a trade or business that has generated carried-forward losses, any losses arising from that trade or business before the change in ownership will be disallowed completely, and cannot be set against future profits or claimed as group relief".

Under the measure, a company may not claim group relief for any losses arising in a company before that company was acquired. The measures apply when a company

"acquires an asset under the intra-group transfer rules such that no gain or loss arises on the transfer, and, within 5 years of the change in ownership, that company makes a gain on the disposal of the asset."

As the explanatory notes state, the Bill

"introduces new timescales within which a major change in the business of a company or a co-transferred company must take place…The rules apply where a major change in a trade takes place within a period of 5 years of the change in ownership…or where a major change in an investment business takes place within a period of 8 years beginning 3 years before the change in ownership…This means that where there is a major change in a trade or business that has generated carried-forward losses, any losses arising from that trade or business before the change in ownership will be disallowed completely, and cannot be carried forward against future profits or claimed as group relief".

The Opposition fully support measures that clamp down on tax avoidance and deter companies from abusing the carried-forward loss mechanism, but the measures need to be tested further, particularly when looking at the number of opt-outs that clause 18 and schedule 4 give, for example, to the oil and gas industry, the creative industries, Northern Ireland and the insurance industry.

With the specific sector-wide opt-outs, there is concern that companies may, but not necessarily will use carried-forward losses as a way to avoid taxation. The creative industries bring more than £84.1 billion to the UK annually. Under the changes, a loss made in the separate film trade may be carried forward from a pre-completion period to a relevant later period. Where that is the case, the amount of that loss not attributable to film tax relief can be treated as a loss in a later period. We can all imagine a scenario where a film company uses those measures to avoid tax—I am not saying they will do that—by repeatedly carrying forward losses from one failed film project to another. Of course, that would be a wholly unique example, and is not reflective of the industry as a whole. I really want to emphasise that: it is not reflective, but it is why the Opposition are keen to push for a review of the effectiveness of the opt-outs given to the creative industries, insurance companies, and oil and gas companies in the Bill.

I want to turn to banking losses covered by the banking sector. In the 2016 Finance Bill, carried-forward losses for the banking sector were reduced from 50% to 25%. We are now 10 years on from the global financial crisis, and can all see the merit and importance of regulating the amounts of losses that banks can keep on their books, given that at the height of the crisis the Office for National Statistics records that the Government had to spend £1.6 trillion bailing out the banks. Although 25% may seem like a stringent figure, it may still be too high given the billions of pounds' worth of risks that banks have on their balance sheets throughout the year.

Durham University finance and economics professor Kevin Dowd—no relation, to the best of my knowledge—recently wrote a report published by the Adam Smith Institute, which said that British banking remains

"an accident waiting to happen."

He criticised the Bank of England's stress tests as being wholly inadequate, masking the fact that banks are more leveraged now than they were 10 years ago. The Governor of the Bank of England himself has said that UK banks are already forgetting the lessons of the global financial crisis, and it is our responsibility to remind them.

Given the renewed concern about the banking system and the added risks that banks may take in the light of Brexit, what consideration has the Minister given to lowering the figure at which banks can carry forward losses, and does he accept that there may be a case for limiting it further? If we continue to have an economy with, let us say, stagnant growth, high inflation, as the figures indicate today, poor productivity—30% below the Germans—and one of the lowest levels of investment in Europe, we are inevitably putting ourselves once more at the mercy of the banks. The Minister may doubt what I say, but I think that is pretty much a fact.

Kelvin Hopkins: There is a lot of evidence that the banks are still engaging in risky gambling on the international exchanges, and compensating for that by squeezing ordinary taxpayers, ordinary bank customers and small businesses in particular to back up their gambling losses. Would my hon. Friend say that we are still facing danger in the future because of the banks' behaviour?

Peter Dowd: We always have to be vigilant—that is the key. Vigilance is crucial. Virtually no one had experienced anything like the banking crisis in living memory. Given that, we have to be on our guard that we do not all breathe such a sigh of relief that it was so long ago that we lose our vigilance.

It seems to me that strong regulations, which will not only protect the taxpayer and their savings, but develop practices at the heart of the industry, are the only bulwark against another financial crisis being created and enacted through reckless banking practice. I hope that the Minister will give some thought to that, particularly given that when we finish the summer-autumn Finance Bill we will immediately start the winter Finance Bill. Given the Government's delayed and, I have to say, sometimes chaotic timetable, it will no doubt end up being called the spring Bill instead. Dare I say it, we have a Minister who is the man for all seasons in that regard. *[Interruption.]* Don't give up the day job, as they say—or perhaps hon. Members would like me to.

Many of the stakeholders to whom the Opposition spoke raised concerns about the complexity of the proposals and the speed with which the Government have attempted to take them through.

Anneliese Dodds: I am grateful to my hon. Friend for running through many of the problems that stakeholders have mentioned to us. One addition to the many ambiguities he mentioned is that, to my mind, a clear rationale does not seem to have been provided for the decision to loosen the rules so that past losses can be offset against

[Anneliese Dodds]

any type of profit, rather than the current position of only being able to offset them against the same type of profit—for example, only offsetting trading losses against trading profits. That is yet another change for which we perhaps require further information and debate.

Peter Dowd: My hon. Friend makes another good point. The Chartered Institute of Taxation has criticised the Government—"criticise" is the word I use, although I am not sure it would say that; it would most probably say it has brought this to the Government's attention—for not balancing

"its desires to raise some modest revenue with its duty to produce legislation that can be followed with predictability and certainty."

Other financial organisations have argued that the measure is likely to create winners and losers. Small groups unlikely to have £5 million of losses, for which this is a high proportion of the total, will benefit from the change. For large groups that wish to access the group relief changes, it is less clear. Deloitte has argued that the slowdown in offset of brought-forward losses for large groups may in fact mean an acceleration in the tax cost for larger companies. Will the Minister offer more clarity on how the group relief will work in practice—particularly the nomination process, whereby a specific company has to be nominated to manage the whole group relief?

The measure seems fraught with potential dangers. For starters, the Bill makes no mention of what happens when a company chooses to join or leave a group that benefits from the group relief. Will the Minister explain whether such a mechanism will be built into the legislation, or whether we will need a further clause in a future Finance Bill that tinkers with carried-forward losses once more? Given the uncertainty felt by many in the business community, the Opposition believe it is only right that the Government submit a review of the operation of the group relief in the carried-forward losses, assessing the cost and impact of the new restrictions and how they will impact on large companies.

Mel Stride: Clauses 18 and 19 and schedule 4 make changes to the rules for corporation tax losses, as we have discussed. They modernise the losses rules by increasing their flexibility, while at the same time ensuring that companies pay tax in years when they earn significant profits. When a company makes a loss, it can carry it forward and use it to offset the tax liability of certain income in future years. Carrying forward losses is an important feature of the tax system and ensures that the tax paid by companies is proportionate with their profits over the long term.

However, these loss relief rules are not reflective of the way businesses operate and are out of step with international practice, which I shall come on to in a moment. First, carried-forward losses can typically only be set against profits from the activities to which they relate, as the hon. Member for Bootle pointed out, rather than the profits of other activities in a company, or the profits of other companies within a group. Secondly, the absence of any restriction on the amount of taxable profit that can be relieved by carried-forward losses means businesses making substantial UK profits may not pay any corporation tax due to losses incurred on historic activities.

The clauses will have effect from 1 April 2017, in line with the commencement date previously announced by the Government. The changes made by clause 18 will mean that rules will be relaxed for losses arising from 1 April 2017 that are carried forward, such that those losses can be set against the profits of different activities within a company and the taxable profits of its group members. As we have said, the amount of annual profit that can be relieved by carried-forward losses will be restricted to 50% from 1 April 2017, subject to an allowance of £5 million per group.

The hon. Member for Bootle asked specifically about that £5 million figure, and about whether the Treasury has looked at international comparisons and factored that into its thinking on this matter. I assure him that it has. This rate is more generous than the rates in a number of other countries. In Germany, for example, the rate is €1 million. As he pointed out, the main rationale for focusing the restriction above £5 million is to bear down on the top 1% of profitable businesses in the country without going further down the spectrum. We believe that we have achieved the right trade-off between the level of the figure and the number of companies that will potentially be affected by the restriction.

3.15 pm

The amount of annual profit that can be relieved by carried-forward losses will be restricted to 50% from 1 April. That restriction will address a public concern by helping to ensure that companies that make substantial profits pay tax. It is worth dwelling on that point for a moment. There is a general feeling among the public that large companies, when they make a lot of profit, should pay to support the public services that we are all in favour of.

The restriction focuses on the largest companies. Due to the £5 million allowance, as the hon. Gentleman recognised, 99% of companies are forecast to be unaffected by the restriction, but all companies will benefit from the more modern and flexible loss-relief regime. The changes in clause 19 will stop companies entering into avoidance schemes to exploit the rules introduced by clause 18. Taken together, the loss-relief reforms will raise more than £1.6 billion over the next five years.

Amendment 22 would require HMRC to undertake a review of the operation of the provisions that introduce group relief for carried-forward losses. The current rules for carried-forward losses do not reflect the way businesses operate in practice and can lead to the unfair outcome of losses being worth more to some companies than to others, depending only on their group structure. The provisions to allow carried-forward losses to be set against the profits of group members are an important step to modernise the regime. The Bill will also introduce robust anti-avoidance provisions, to ensure that the new flexibility does not lead to opportunities for abuse. As with all policies, the Government will monitor the regime closely once it commences to ensure that it operates as intended.

I urge hon. Members to reject amendment 22. A mandated formal review is not an appropriate response to provisions that have been widely consulted upon and carefully designed. On anti-avoidance, the hon. Gentleman rightly raised certain circumstances that the Bill will deal with. For example, it will ensure that companies do not abuse the buying-in of losses by taking over other corporate bodies, or by using losses from trades that are not carried out by the acquiring company, which can be done using various devices.

The hon. Gentleman asked why there is a carve-out for creative industries under these arrangements. That is because they are subject to special rules when it comes to losses. While a creative project—a film, for example—is ongoing, its losses cannot be surrendered to companies in the same group. That means that the company is not able to use losses in the flexible way that other companies can. Those special rules are an anti-avoidance measure, and including creative losses in the relaxation part of the loss reform would risk opening up avoidance opportunities, which we clearly do not wish to happen.

The hon. Gentleman also asked about banks. He suggested that restricting the use of bank losses to 25% might be too generous. I remind him that banks are already subject to an 8% corporation tax surcharge and a levy on their balance sheets, which is not an approach that we have taken to other sectors of the economy. Further restrictions on losses on top of the specifically designed tax regime to reflect the unique position of banks in the economy would be disproportionate.

I turn to amendment 23, which would require HMRC to undertake a review of the operation of the provisions for carried-forward losses for insurance companies, creative industries and oil activities. It may be helpful if I explain why those sectors are being treated differently.

The provisions relating to insurance companies prevent the reforms from reducing the value of individuals' life assurance policies. The loss-relief reform is intended to apply to companies, and the unique structure of the life assurance industry means that it is necessary to make these provisions to prevent individuals from being unfairly impacted. As I said, the reforms have not been applied to creative industries because they already face high restrictions on the use of losses for anti-avoidance reasons, and the oil and gas regime is subject to a bespoke ring-fenced tax regime that prevents taxable profits from oil and gas extraction from being reduced by losses from other activities. It is right to maintain the integrity of that regime by continuing to treat it separately.

These clauses and the schedule introduce new rules that will modernise the UK's loss relief and will help to ensure that businesses cannot use carried-forward losses to pay no tax in each accounting period in which they make substantial profits. I hope that Opposition Members will not press their amendment, and I commend these measures to the Committee.

Peter Dowd: I tried to set to out as comprehensively as I could, without getting too complicated, complex or specific, why we were concerned to keep tabs on this. Trying to keep tabs on the Government's proposals has been today's theme, and that is why we have asked for reviews. In the current climate, when there are so many pressures on public services and a range of challenges for the country, we are all concerned to ensure that organisations that benefit from our fantastic country and from the protection of the rule of law pay their dues. That is not to point the finger at anyone specifically to say they are not paying their dues, but to ensure that we to some extent guard the guards. That is what we are trying to do today: to guard the guards; that is our job and our responsibility. Given the Minister's explanation, we will not press the amendment, but no doubt we will come back to these issues in due course.

Question put and agreed to.

Clause 18 accordingly ordered to stand part of the Bill.

Schedule 4 agreed to.

Clause 19 ordered to stand part of the Bill.

Ordered, That further consideration be now adjourned.—*(Graham Stuart.)*

3.22 pm

Adjourned till Thursday 19 October at half-past Eleven o'clock.

Written evidence reported to the House

FB 01 Mark Coulter, Technical Consultant, Kerr Henderson (Financial Services) Ltd.

FB 02 The Tax Faculty, Institute of Chartered Accountants in England and Wales

FB 03 Association of Taxation Technicians (ATT)

FB 05 Low Incomes Tax Reform Group (clause 7)

FB 06 Low Incomes Tax Reform Group further submission (clause 17 and schedule 3)

FB 07 Chartered Institute of Taxation (clauses 18 and 19 and schedule 4)

FB 08 Chartered Institute of Taxation further submission (clause 20 and schedule 5)

FB 09 Chartered Institute of Taxation further submission (clauses 27 and 28)

FB 10 Chartered Institute of Taxation further submission (clauses 29 to 33 and schedules 8 to 10)

FB 11 Chartered Institute of Taxation further submission

FB 12 Association of Taxation Technicians (ATT) further submission (new schedule A1, paragraph 12)

FB 13 Association of Taxation Technicians (ATT) further submission (new schedule A1, paragraph 14)

FB 14 Chartered Institute of Taxation further submission (clause 9 – life insurance policies)

FB 15 Chartered Institute of Taxation further submission (clause 16 – calculation of profits of trades and property businesses)

FB 16 Enterprise Tax Consultants