PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT
GENERAL COMMITTEES

Public Bill Committee

FINANCE BILL

(Except clauses 7 to 18, 41 to 44, 65 to 81, 129, 132 to 136 and 144 to 154 and schedules 2, 3, 11 to 14 and 18 to 22)

Third Sitting

Tuesday 5 July 2016

(Morning)

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PBC (Bill 001) 2016 - 2017

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Saturday 9 July 2016

The Committee consisted of the following Members:

Chairs: Sir Roger Gale, † Mr George Howarth

† Argar, Edward *(Charnwood)* (Con)
† Atkins, Victoria *(Louth and Horncastle)* (Con)
Blackman, Kirsty *(Aberdeen North)* (SNP)
† Boswell, Philip *(Coatbridge, Chryston and Bellshill)* (SNP)
† Burns, Conor *(Bournemouth West)* (Con)
† Cadbury, Ruth *(Brentford and Isleworth)* (Lab)
† Cooper, Julie *(Burnley)* (Lab)
Donelan, Michelle *(Chippenham)* (Con)
† Dowd, Peter *(Bootle)* (Lab)
† Frazer, Lucy *(South East Cambridgeshire)* (Con)
† Gauke, Mr David *(Financial Secretary to the Treasury)*
† Hall, Luke *(Thornbury and Yate)* (Con)
† Hinds, Damian *(Exchequer Secretary to the Treasury)*
† Long Bailey, Rebecca *(Salford and Eccles)* (Lab)
† McGinn, Conor *(St Helens North)* (Lab)
† Mak, Mr Alan *(Havant)* (Con)
Marris, Rob *(Wolverhampton South West)* (Lab)
† Matheson, Christian *(City of Chester)* (Lab)
Merriman, Huw *(Bexhill and Battle)* (Con)
† Mullin, Roger *(Kirkcaldy and Cowdenbeath)* (SNP)
† Quin, Jeremy *(Horsham)* (Con)
Streeting, Wes *(Ilford North)* (Lab)
† Stride, Mel *(Lord Commissioner of Her Majesty's Treasury)*
Tolhurst, Kelly *(Rochester and Strood)* (Con)

Simon Patrick, Marek Kubala, *Committee Clerks*

† attended the Committee

Public Bill Committee

Tuesday 5 July 2016

(Morning)

[Mr George Howarth *in the Chair*]

Finance Bill

(Except clauses 7 to 18, 41 to 44, 65 to 81, 129, 132 to 136 and 144 to 154 and schedules 2, 3, 11 to 14 and 18 to 22)

Clause 50

Tax relief for production of orchestral concerts

9.25 am

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

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

That schedule 8 be the Eighth schedule to the Bill.

Clause 51 stand part.

Rebecca Long Bailey (Salford and Eccles) (Lab): Who knows what adventures the Finance Bill will take us on today? Hopefully the sittings will be a little more sedate than last week's.

I will first address clause 50 and schedule 8, and then move on to clause 51 relating to television and video games tax relief. Clause 50 brings in schedule 8, which introduces a new relief for orchestral concerts, provides for consequential amendments to other parts of taxes Acts as a result, and arranges for the commencement of the relief. First announced in the autumn of 2014, the new tax relief for orchestral production will allow qualifying companies engaged in the production of concerts to claim an additional deduction in computing their taxable profits and, where that additional deduction results in a loss, to surrender the losses for a payable tax credit. The additional deduction and the payable credit are calculated on the basis of European Economic Area core expenditure, up to a maximum of 80% of the total core expenditure by the qualifying company. The additional deduction is 100% of qualifying core expenditure, and the payable tax credit is 25% of losses surrendered.

The credit is based on the company's qualifying expenditure on the production of a qualifying orchestral concert. The expenditure must be on activities directly involved in producing a concert, such as rehearsal costs. Qualifying expenditure will not include indirect costs, such as financing, marketing and accountancy and legal fees, and at least 25% of the qualifying expenditure must be on goods or services that are provided from within the EEA. Concerts that have among their main purposes the advertising of goods and services or the making of a recording, or that include a competition, will not qualify for relief.

The stated objective of the measure is to support the creative sector and sustainably promote British culture. I certainly back that approach, not least because the BBC Philharmonic orchestra is based in my constituency and continues to attract many like-minded orchestral organisations to my city. On the machinery of the calculations, however, as the deduction of credit is calculated on the basis of EEA core expenditure, what assessment has the Minister made of amendments that might need to be made to the clause as a result of Britain's exit from the EU?

I am pleased that the Government took the time to consult on the measure, and I note that the summary of responses published in March 2015 indicates that the industry welcomed the introduction of the relief. I am also pleased that the Government took heed of the Opposition's concerns about the initial proposal exempting brass bands from the relief, effectively introducing a brass band tax, and that the Government subsequently included brass bands in the relevant definition in March 2015. The draft Bill and a policy paper were published in December 2015, and the Government did not make any substantive changes after the technical consultation exercise, so I am confident that the legislation will do what it says on the tin.

The measure is expected to cost the Exchequer £5 million in the financial year 2016-17 and £10 million every financial year thereafter until 2019-20. The Opposition agree with the principle of supporting the UK's creative industries and therefore support clause 50 and schedule 8, but we are concerned that we keep creating relief after relief. Why does this targeted measure take the form of a tax relief, rather than a grant? Also, the industry is concerned that the relief does not support commercial music production, which is supported in other countries. Will the Minister clarify today, or indeed in a written response after today, what support is in place for this important industry?

Finally, what modelling have the Government done to ensure that the legislation is rigorous enough to prevent use of the relief for avoidance purposes? I understand that there were some issues about film tax relief and avoidance, and I am also concerned that the wording in proposed new section 1217RL to the Corporation Tax Act 2009 may not be very robust, especially with reference to those tax avoidance arrangements that fall within the ambiguous term, "understanding"; I am sure that the Minister will agree that by their very nature those will not be contractual. Will he confirm whether he has given thought to additional resources that Her Majesty's Revenue and Customs might need if it is adequately to investigate such scenarios?

Clause 51 simply makes minor, consequential amendments to the Taxation of Chargeable Gains Act 1992 and the Corporation Tax Act 2010, substituting the words "section 1218B" for "section 1218". The Opposition support television and video games tax relief, as we introduced it. We see no issue with this technical clause.

The Financial Secretary to the Treasury (Mr David Gauke): It is a great pleasure to serve under your chairmanship again this morning, Mr Howarth. I welcome the hon. Member for Salford and Eccles to the Committee. She has taken on a substantial workload in the past few days. Having had experience of performing her role of holding the Government to account in the Finance Bill, I recognise how challenging it can be. I wish her luck in that; if I may say so, she has made an excellent start, raising important points about this group of clauses.

I will start with a few words about clauses 50 and 51 and schedule 8, and then I will respond to the hon. Lady's questions. The Government have supported our world-leading creative and cultural sectors, which have entertained millions worldwide while attracting significant investment into the United Kingdom. Clause 50 and schedule 8 provide further support by introducing a new corporation tax relief for the production of orchestral concerts. The Government recognise the cultural value and artistic importance of Britain's orchestras. The relief is intended to support them in continuing to perform for a range of audiences, and in contributing to British culture.

Clause 51 makes minor consequential amendments to the Taxation of Chargeable Gains Act 1992 and the Corporation Tax Act 2010 as a result of the introduction of video games tax relief in the Finance Bill 2013. The change is not expected to have an impact on businesses that claim the relief.

The UK is home to some exciting, world-famous orchestras. The relief introduced by clause 50 recognises their artistic importance and cultural value. Its objective is to support orchestras so that they can continue to perform for a wide range of audiences. To deliver that support, the Government are building on the success of existing creative sector tax reliefs available for the production of film, high-end television and children's television, video games, animation and theatre. Those reliefs have shown how targeted support can make a real difference, not only by promoting economic activity, but by promoting British culture and the way that the UK is viewed internationally.

Clause 50 will introduce a new corporation tax relief and payable tax credit for the qualifying costs of producing an orchestral performance. It will support a wide variety of ensembles and performances, from chamber orchestras to large brass bands playing music ranging from jazz to blues. It will allow production companies to claim a payable tax credit worth up to 25% of the cost of developing an orchestral concert, with effect from 1 April this year.

In 2013, minor consequential amendments were made to the Corporation Tax Act 2010, as some sections were renumbered following the introduction of video games tax relief in the Finance Bill 2013. Clause 51 makes a further consequential amendment to the Act and the Taxation of Chargeable Gains Act 1992; it is not expected to have an impact on any business claiming that relief.

The Government are grateful for the constructive and positive engagement with the industry since the policy was announced, and during consultation in 2015. That has enabled us to understand better how the orchestra industry operates, and to design a relief that will work across the sector. The director of the Association of British Orchestras, Mark Pemberton, has commented that the relief

"will make a big difference to our members' resilience in these challenging times, helping them to continue to offer the very best in British music-making to audiences both here in the UK and abroad."

The hon. Lady asked whether there was a risk of the relief being abused. Effective anti-avoidance rules are critical to the long-term success and stability of orchestra tax relief. Rules similar to those applied to the creative industry reliefs aim to prevent artificial inflation of claims. In addition, there will be a general anti-avoidance rule based on the GAAR denying relief where there are any tax-avoidance arrangements relating to the production—and, of course, HMRC will monitor for abuse once the regime has been introduced. On HMRC resourcing, I point the Committee in the direction of the £800 million announced in last year's summer Budget, which provided further investment in HMRC to deal with avoidance and evasion measures more generally.

I come back to the point the hon. Lady raised about film tax relief and how that was abused. It is true that an earlier design of film tax relief was brought in by the previous Labour Government and was abused. That relief was abandoned by that Government, and the replacement model has been much more successful. It has provided the support that the film industry needs and benefits from, and that has helped to ensure that we have a thriving film industry without anything like the risks of abuse we saw formerly. In the measures that we have taken, we have learned from the previous approach.

The hon. Lady referred to making use of an EEA definition, and understandably asked what the implications are of the vote to leave the European Union. It is too early to say exactly how that will work. We are not sure what relationship we will have with the European Union, other than that we will be leaving it. It is quite possible that EEA definitions and so on will remain relevant, but we currently remain members of the EU and are considering legislation that takes effect in April, so it is necessary to comply with the rules as they stand. If it is necessary to review definitions, that is something we will have to look at, but that will depend on the future renegotiation.

The hon. Lady expressed the concern that perhaps we have too many tax reliefs. As the Chancellor made clear in the House of Commons yesterday, there is a place for reliefs, but our general and main focus has been on lowering corporation tax rates, and that continues to be the case. There is scope for using tax reliefs to support investment in growth through the tax system, and that is why we provide a range of tax reliefs and allowances. The Government have restricted a number of tax reliefs and allowances; for example, we have introduced a cap on income tax reliefs, restricted relief for buy-to-let landlords and capped the amount of losses through which banks can reduce their tax, so we have taken action on reliefs where we feel that their use is disproportionate to the benefits for the wider economy.

On orchestras, the Government are committed to supporting the arts through both spending programmes and tax reliefs. The orchestra tax relief is intended to complement current funding. It is specifically aimed at supporting orchestras in continuing to produce high-quality music that is enjoyed by a range of audiences. In those circumstances, we think it is justifiable. I hope that the clause has the support of Members in all parts of the Committee.

Question put and agreed to.

Clause 50 accordingly ordered to stand part of the Bill.

Schedule 8 agreed to.

Clause 51 ordered to stand part of the Bill.

Clause 52

BANKING COMPANIES: EXCLUDED ENTITIES

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

The Chair: With this it will be convenient to discuss clause 53 stand part.

Rebecca Long Bailey: Clauses 52 and 53 relate to the taxation of banking companies. Clause 52 amends the excluded entity test that forms part of the definition of a bank for tax purposes, and clause 53 makes provisions to restrict corporation tax loss relief.

Following the financial crash in 2008, specific taxes were imposed on the banking sector, and a definition of "banking companies" was required. The excluded entity test forms part of this definition. Clause 52 revises the legislation so that undertaking a second activity is possible, provided that the entity undertakes one of the specified regulated activities in the excluded entities test, and that the other activity, when considered by itself—that is, without taking into account the regulated activity that is specified in the excluded entities test—would not require the firm to be both an IFPRU 730K investment firm and a full-scope IFPRU firm as defined by reference to the Financial Conduct Authority handbook.

As the British Bankers Association has explained in far more articulate layman's terms,

> "Effectively there is a list of permitted activities which do not cause you to be treated as a bank and brought into the various bank-specific taxes, even if you meet all the other conditions. The change to the rules allows you to carry on more than one of those activities and still be excluded."

This measure clarifies the rules and has been welcomed by industry. We therefore have no issue with agreeing the clause today. We also welcome clause 53, which, to quote the explanatory notes to the Bill,

> "further restricts the proportion of a banking company's annual taxable profit that can be offset by brought forward losses to 25%. The further restriction will apply to accounting periods beginning on or after 1 April 2016."

At autumn statement 2014, it was announced that the amount of taxable profit that could be offset by banks' historical carried-forward losses would be restricted to 50% from April 2015. However, this clause further restricts the proportion of a banking company's annual taxable profit that can be offset by brought-forward losses from 50% to 25%. The restriction will remain subject to a £25 million allowance for building societies, and an exemption for losses incurred by new entrant banks. The Government estimate that this will generate over £2 billion in extra revenue between the current financial year and 2020-21. They also state that the measure should be revenue-neutral in the long run for any one bank, but the timing of the measure may well have negative implications for cash flow.

The British Bankers Association has indicated that further restricting bank losses from the financial crisis to 25% of profits rather than 50% primarily brings about a timing difference; it effectively accelerates payment of £2 billion in tax into this Parliament and out of the next one. Combined with the previous changes, it means £5 billion is being brought forward to this Parliament.

Can the Minister say why the Chancellor needed to accelerate this windfall in tax revenues? Was it part of his desperate attempts to ensure a budget surplus by 2020? I suspect it might have been. However, that argument is now redundant, given the recent suspension of that aim, and I am really glad that the Chancellor is finally listening to the experts and my hon. Friend the shadow Chancellor. Nevertheless, we welcome this new requirement on banking companies to increase their contribution to the Exchequer in the light of their role in causing the current economic situation.

I am glad that the Government are taking steps to address the casino banking sector. However, the policy should be seen in the wider context of the Government's new settlement with financial services, as announced by the Chancellor, which includes the shift in emphasis from the bank levy to the banks' tax surcharge as a result of lobbying by the sector, and watering down promised regulatory provisions in the Bank of England Act 2016.

In the 2016 Budget, the introduction of a general restriction on carried-forward losses was announced. That will come into effect on 1 April 2017, and the Opposition support it. In the meantime, we are more than happy to agree to the further restriction set out in clause 53.

9.45 am

Mr Gauke: I am grateful to the hon. Lady for her support for clauses 52 and 53, which will ensure that the exceptional tax treatment of banks' crisis-related losses is maintained in the light of the wider changes to the UK loss relief regime announced in the Budget. They will also amend the definition of a bank used in tax legislation to ensure that bank-specific tax measures are targeted as intended.

Clause 52 will change the definition of an investment bank to ensure that legislation is appropriately targeted. We have been clear that banks should make a fair contribution to reflect the risks they pose to the UK economy, and we have taken several steps to ensure that they do make that contribution. The Chancellor introduced the bank levy—a tax on banks' balance sheets—in 2011 and removed tax relief for banks' compensation in relation to misconduct and mis-selling from July 2015. We restricted the amount of profit that banks can offset with historical corporation tax losses, and we introduced a new supplementary tax of 8% on banking sector profit from 1 January 2016.

Those policies, which are forecast to raise more than £28 billion between 2015 and 2021, rely on there being an appropriate definition in tax legislation of a bank. That definition is based broadly on the extent to which a company is regulated and the nature of the activities that it undertakes. Concerns have been raised that the existing definition has the potential to go further than intended and bring into scope companies that are not undertaking retail or investment banking activities. We seek to address that through clause 52, which will make a minor technical change that is expected to have a negligible cost to the Exchequer and will ensure that legislation is fair and appropriately targeted. The clause will ensure that banking taxes are targeted appropriately at banks and that legislation remains simple, certain and effective.

Clause 53 will reduce from 50% to 25% the amount of profit that banks can offset with historical losses for corporation tax purposes from 1 April 2016. When a company makes a loss for corporation tax purposes, it is able to offset that loss against the profit of a group member in the same year. If that is not possible, companies are able to carry forward their losses and offset them against future profits. Companies' ability to carry forward losses is an important feature of the corporation tax system. It means that companies with volatile income streams are not subject to higher effective rates of tax on their long-term profits. In the 2014 autumn statement, the Chancellor announced that the proportion of taxable profit that could be offset by banks' pre-April 2015 losses would be limited to 50% from 1 April 2015. That exceptional treatment recognised the significant losses that banks had carried forward from the financial crisis and the subsequent misconduct scandals, and the impact that those losses were having on banks' corporation tax payments. It was forecast to increase corporation tax receipts by £2 billion between 2015 and 2020.

In the March 2016 Budget, fundamental reforms were announced to the treatment of carried-forward losses across all industry groups, to take effect from April 2017. First, there will be greater flexibility regarding the profits against which carried-forward losses can be offset. Secondly, the amount of profit that can be offset by carried-forward losses will be restricted to 50% from April 2017, subject to a £5 million allowance. Those reforms will create a more modern loss relief regime in the UK that is competitive with those in other G7 countries and better aligned with how businesses operate.

The changes made by clause 53 will maintain the exceptional treatment of banks' historical losses by reducing from 50% to 25% the amount of profit that banks can offset with historical carried-forward losses from 1 April 2016. That will increase banks' corporation tax payments by around £2 billion over the next five years. The existing reliefs for losses incurred by new entrant banks and building societies will be maintained; those will continue to be treated in the same way as losses in other industry groups.

On the hon. Lady's question about timing, these measures, taken together, will raise about £5 billion in 2016-17 alone. It is important that the banking sector's tax contribution is made when it is most needed during this period of fiscal consolidation. I take the point about the changed circumstances in the light of the vote to leave the European Union. It is also important that we make progress in reducing the deficit, and that we demonstrate that the Government are fiscally responsible. That is what we are doing. This measure is part of a plan to make progress to reduce our deficit further. Having given the Committee those points of information, I hope that these clauses can stand part of the Bill.

Question put and agreed to.

Clause 52 accordingly ordered to stand part of the Bill.

Clause 53 ordered to stand part of the Bill.

Clause 54

Reduction in rate of supplementary charge

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

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

Clauses 55 to 59 stand part.

Clause 128 stand part.

New clause 3—*Corporation tax treatment of the oil and gas industry*—

'The Chancellor of the Exchequer shall, within six months of the passing of this Act, commission a comprehensive review of the corporation tax rates and investment allowances applicable to companies producing oil and gas in the UK or on the UK continental shelf, and publish the report of the review.'

New clause 6—*Oil and gas: decommissioning contracts*—

'(1) The Chancellor of the Exchequer shall commission a review of the ways in which the tax regime could be changed to increase the competitiveness of UK-registered companies in bidding for supply chain contracts associated with the decommissioning of oil and gas infrastructure.

(2) In undertaking the review, the Chancellor shall consult the Department for Business, Innovation and Skills, the Oil and Gas Authority; Scottish Ministers; and any other stakeholders that the Chancellor thinks appropriate.

(3) The Chancellor shall report to Parliament on the results of his review within six months of the passing of this Act.'

The Exchequer Secretary to the Treasury (Damian Hinds): It is a pleasure to serve under your chairmanship once again, Mr Howarth. These measures bring into statute a £1 billion package of fiscal reforms for the UK's oil and gas sector. These changes will deliver the next stage of the Government's reform plan for the oil and gas fiscal regime, and they will give much-needed support to an industry facing exceptionally challenging conditions. They will provide the right conditions in which to maximise the economic recovery of the UK's oil and gas resources by lowering sector-specific tax rates, updating the current system of allowances and expanding the types of activity that can generate financial relief. The Government are making these changes to protect jobs, encourage investment in new projects and infrastructure, and safeguard the future of one of our most vital national assets.

I will provide hon. Members with some background to the changes. Almost 200 companies are currently in production in the UK oil and gas industry. They support 30,000 jobs directly and 250,000 in the wider supply chain. As hon. Members know, since 2014 the industry has experienced highly challenging conditions. Oil prices have fallen to less than half their 2014 value, putting thousands of jobs at risk. In the 2014 autumn statement, the Government set out our plan to reform the oil and gas fiscal regime in the publication "Driving investment". That document recognised the need to reduce the future oil and gas tax burden in order to maximise economic recovery and keep the UK basin attractive to investors as it further matures. We delivered on that plan by reducing the rate of the supplementary charge and the petroleum revenue tax in 2015. As announced in the March 2016 Budget, we will lower both those rates further.

Between 2013 and 2015 the Government introduced the investment, onshore and cluster area allowances, which replaced the old suite of field allowances with a simplified and expanded relief system to generate greater investor certainty in the sector. The Government intend to include tariff income—income from third-party access to oil and gas infrastructure—in the scope of the investment and cluster area allowances. We will introduce secondary legislation later this year to facilitate that. Clauses 55 to 59 update the investment, onshore and cluster area allowances to align them with that piece of future legislation and ensure that the allowances are not generated twice.

The changes made by clause 54 will halve the rate of the supplementary charge from 20% to 10%. That will make the sector more attractive to future investors,

[Damian Hinds]

thereby providing much-needed support for jobs and supply chain opportunities across the industry. As I said, clauses 55, 57 and 58 update the disqualifying conditions of the investment, onshore and cluster area allowances to prevent allowances being generated twice and to limit opportunities for avoidance. Clause 55 amends the investment allowance to update the conditions that disqualify expenditure incurred before a field is determined. This will protect the Exchequer and ensure the legislation works as intended.

Similarly, clause 57 updates the onshore allowance to introduce certain disqualifying conditions. This will provide parity with the other allowances available to the sector. Clauses 55 and 58 insert leasing into the disqualifying conditions for the investment and cluster area allowances. Together these three clauses will align the investment, cluster area and onshore allowances with future legislation while ensuring the allowance is not open to avoidance opportunities.

Clauses 56 and 59 amend the investment and cluster area allowances and introduce a power to expand the meaning of "relevant income". The Government intend to enable tariff income to activate the investment in cluster area allowances and incentivise owners to maintain investment in the sector's infrastructure, including key pipelines. These measures will encourage further investment in exploration and appraisal projects, which are the lifeblood of the industry.

Finally, clause 128 changes the petroleum revenue tax by reducing its rate from 35% to zero. Our commitment is effectively to abolish this tax by zero-rating it on a permanent basis. This change will simplify the tax regime for investors and level the playing field between investment opportunities in older oil fields and infrastructure and new developments across the North sea. Furthermore, clause 128 will update the Oil Taxation Act 1975 to reflect the new zero-rated nature of the petroleum revenue tax and amend the cap on interest carried on its repayments. The clause will work in tandem with clauses 54 to 59 to deliver the next stage of fiscal reforms to support the oil and gas sector.

New clause 3, tabled by the hon. Member for Kirkcaldy and Cowdenbeath, calls for the Government to review the taxes and allowances that apply to oil and gas-producing companies in the UK within six months of the Bill receiving Royal Assent. However, a further review into oil and gas taxes is not required because the Government already carried out a broad review of the fiscal regime in 2014. The outcome of that review, as I mentioned, was the publication "Driving investment", which sets out our long-term plan to ensure that the fiscal regime continues to support the objective of maximising economic recovery while ensuring a fair return on those resources for the nation.

The principles in "Driving investment" recognise the need for the oil and gas tax burden to fall as the basin matures, and the need to factor wider commercial opportunities when making judgments about future fiscal policy. The March 2015 Budget delivered on many of the reforms set out in that plan by reducing the rate of both the supplementary charge and the petroleum revenue tax. The package announced in the March 2016 Budget delivers the next stage of our plan for reform.

The Government understand now, as we did in 2014, that certainty and stability are crucial to providing the right conditions for companies to continue investing in this vital industry. Another review could create further uncertainty for the industry and delay investment, particularly in the current environment. Therefore, given the volume and range of work that has been done in this area recently, an additional review is unnecessary, so I urge the hon. Gentleman not to press his new clause or, failing that, I urge Members to reject it.

New clause 6, which was also tabled by the hon. Member for Kirkcaldy and Cowdenbeath, calls for a review into how the tax regime could increase the competitiveness of UK-registered companies in bidding for supply chain contracts associated with decommissioning. Decommissioning in the UK continental shelf brings significant opportunities for UK business and we want to maximise those. The Government fully support the vision of Sir Ian Wood to establish the north-east of Scotland as

"a global centre of knowledge and excellence in offshore mature basin technology and decommissioning".

That is why the Government support the creation of an oil and gas technology centre in Aberdeen as part of the Aberdeen city deal. It is also why the Oil and Gas Authority will soon be publishing a decommissioning plan for the continental shelf. This will be focused on enabling the £15 billion service sector in Aberdeen to become the centre of a new global market for decommissioning and will help UK firms to capitalise on the huge opportunities that will become available. It is of course important that we have a tax regime that supports that ambition, and the package being delivered in the Bill will ensure that the UK has one of the most competitive tax regimes in the world for oil and gas. In addition, the Government have cut the rate of corporation tax to 20%—the lowest in the G20—and we are committed to going further.

With a competitive tax system in place and the OGA's focus on realising the opportunities of decommissioning, I firmly believe that UK businesses are in a strong position to benefit. Certainty and stability are vital, and I do not believe that these would be supported by a further review. I therefore urge the hon. Gentleman not to press new clause 6.

The changes brought about by these clauses will deliver the £1 billion package of fiscal reforms announced in the March 2016 Budget by cutting tax rates, encouraging investment in infrastructure and updating the oil and gas allowances. These measures will send a strong signal to the global investment community that the UK's oil and gas sector is open for business and ready for investment.

10 am

Philip Boswell (Coatbridge, Chryston and Bellshill) (SNP): It is a pleasure to serve under your chairmanship once again, Mr Howarth. As the Minister has spoken to both new clause 3 and new clause 6, I seek clarification that I may attend to both at the same time.

The Chair: Yes.

Philip Boswell: Thank you. In relation to new clause 3, the cut to the supplementary charge set out in clause 54 is of course welcome. It will assist in encouraging business investment, and I commend this initiative. However, the UK Government's support for the oil and gas industry, as it pertains to the cut in the supplementary charge and in a more general sense, does not go far enough. The alterations made to the financing of the oil and gas sector fall significantly short of the fiscal and regulatory reforms necessary to ensuring a steady recovery in the ongoing North sea crisis. Despite the oil price continuing to rise—it is currently around $50 for Brent crude—instead of the extensive regulatory changes experienced over the past 15 years, stability and certainty are required to increase and retain investment as well as some incentivisation. I must admit to being further encouraged by the Minister's statements in this respect.

However, the UK Government must consider all possibilities that could facilitate fresh investment in the oil and gas sector. These possibilities need not be restricted to fiscal support. For example, schemes such as Government guarantees ought to be explored. I would welcome such initiatives from the Minister. Has he considered further the following suggestions, made by the Scottish Government to the Chancellor in February 2016: removing fiscal barriers, specifically for exploration and enhanced oil recovery; implementing fiscal reforms to improve access to decommissioning tax relief and encourage late-life asset transfers—that would reduce costs and help prevent premature cessation of production, which is critical if marginal fields are to be garnered in future—and implementing additional non-fiscal support, such as Government loan guarantees, to sustain investment in the sector? I welcome his commitment to future legislation, especially in relation to cluster allowances, and look forward to its introduction. The industry has called for a comprehensive strategic review of tax rates and investment allowances. Based upon my own experience of working in the sector, I believe that this review would be beneficial, hence my support for new clause 3.

In relation to new clause 6, the UK continental shelf is one of the first large fields in the world to reach super-mature status. This poses both a challenge and an enormous amount of opportunity. While no reservoir on the planet has harvested more than 50% of its reserves, and most of the "sweet oil"—the high-quality, easy-to-reach oil found to date, which requires minimum processing—has gone from the sector, we need to look at improving recovery and the technology required to maximise output through enhanced oil recovery, in order to maximise profits from these fields, marginal or otherwise.

Decommissioning is a key part of the life cycle of UKCS assets. Some have now lasted for over three decades, which in many cases considerably exceeds their original design life. It is advances in technology and additional tie-backs—additional nearby fields that can be tied into the existing infrastructure—which would otherwise be unprofitable if they required a bespoke pipeline, that have made our oil and gas industry so successful.

Oil & Gas UK has estimated that between now and 2040 the total decommissioning spend in the North sea on offshore assets is set to rise by £46 billion. That represents a huge opportunity for domestic supply chains, not to mention extensive finds further west of Shetland and off the west coast of Scotland, which as yet have hardly been touched. The companies that operate on the UK continental shelf are respected all over the world, as it is there, in rough seas with heavy swells, that technology has advanced in conjunction with safety measures to ensure that the North sea, and Scotland in particular, are at the forefront of offshore construction and sub-sea technology, which is something I specialised in at BP, Shell and Premier Oil.

Given our well-deserved status in sub-sea technology and the maturity of some of our fields, there is a real opportunity to become world leaders in well plugging and decommissioning. The UK Government need to incentivise and support the oil and gas industry so that UKCS expertise can be further developed in the North sea and exported around the globe. That begins with ensuring that the oil and gas industry is working in a fiscal regime that is appropriate to the maturity of the field, which is what new clause 6 seeks to do. Although there are always new fields being discovered and technological advances rendering previously unprofitable reservoirs profitable, it is in the management of mature assets, via enhanced oil recovery and further tie-backs, that optimise power output and profitability, a strategy adopted by Statoil, our near neighbours, the Norwegian national oil and gas company, where every barrel counts. That has proved very successful and is a strategy we should copy.

The removal of fiscal and regulatory barriers is imperative to the advancement of an internationally competitive tax regime in the North sea, such as Norway's incentive to remove taxation on exploration where the contractor or operator drills a duster. The Minister of State, Department of Energy and Climate Change, the hon. Member for South Northamptonshire (Andrea Leadsom), in response to a question from my hon. Friend the Member for Aberdeen South (Callum McCaig) in September 2015, committed to a proactive policy to encourage the development of a capable and competitive UK supply chain. That proactive approach needs to start sooner rather than later.

I welcome the Minister's announcement on the oil and gas technology centre in Aberdeen, and on the decommissioning focus in Aberdeen and the offshore construction centre in the UK, but what steps have the Government taken to compensate oil and gas companies for exploration in the UKCS where a duster is drilled? For example, in Norway no tax is applied to such exploration. What tax incentives are in place, or are being considered, to encourage or subsidise decommissioning projects by UK companies, where new technologies, techniques or even tried and tested decommissioning methods are utilised on various types of assets?

In September 2015 Wood Mackenzie reported that low oil prices could render marginal fields economically unviable and lead to potential decommissioning of up to 140 fields within the next five years. I reiterate that Brent crude remains at around $50 a barrel. If prices continue to rise to the forecast $70 to $75 dollars a barrel after the summer, what tax incentives has the Minister put in place to identify and retain critical infrastructure across the UKCS?

With that in mind, new clause 6 calls for a review of the ways in which the tax regime could be changed to increase the competitiveness of UK-registered companies in bidding for supply chain contracts associated with

[Philip Boswell]

the decommissioning of oil and gas infrastructure, with the aim of ensuring that we take advantage of this momentous opportunity.

Rebecca Long Bailey: With permission, I will speak to clauses 54 and 128 together before moving on to the remaining clauses and new clauses.

As we have heard, clauses 54 and 128 reduce the rates of the supplementary charge levied on the ring-fenced profits of companies involved in oil and gas production and petroleum revenue tax respectively. Companies involved in the exploration for and production of oil and gas in the UK are charged ring fence corporation tax and a supplementary charge. RFCT is calculated in the same way as corporation tax but with the addition of a ring fence so that losses on the mainland cannot be offset against profits from continental shelf fields. It is important to note that the rates of RFCT differ from those of corporation tax, and that the main rate of RFCT is 30%. The supplementary charge is an additional charge on a company's ring-fenced profits. Clause 54 would reduce the supplementary charge from 20% to 10% from 1 January 2016.

Petroleum revenue tax, which was introduced in 1975, is a tax on the profits from oil and gas production from fields approved before 16 March 1993. The Finance Act 1993 reduced the rate from 75% to 50%, and it was then reduced to 35% from 1 January 2016. Clause 128 reduces the rate to zero, effectively abolishing the tax, as the Chancellor explained in his Budget speech. These two measures, taken together, are expected to cost the Treasury just over £1 billion between this financial year and 2021. The Government expect the reduction in rates to increase the post-tax profits of affected companies. This will make investment in oil and gas projects on the UK continental shelf more attractive, which will lead to additional production of oil and gas.

According to the tax information and impact note, and as the Minister confirmed today, there are around 200 companies extracting oil and gas in the UK. The industry directly supports 30,000 jobs, with another 250,000 in the supply chain. The decrease in the supplementary charge and the petroleum revenue tax will have a positive impact on company post-tax profits and result in lower instalment payments being made. We have already welcomed this support for the UK's oil and gas industry. The industry trade body, Oil & Gas UK, has broadly welcomed this reduction in the headline rate of tax paid on UK oil and gas production, from a rate of 50% to 67.5% to a rate of 40% across all fields.

However, it is important to note that Oil & Gas UK has stated that the reduction in tax will help only those companies that are actually making a profit. It estimates that fewer than half a dozen companies are paying corporation tax this year. Indeed, the 2016 Budget stated that the tax receipts for these companies in 2015-16 were zero. A reduction in those tax rates is therefore welcome, but it is a long-term benefit.

Frankly, I think that more needs to be done in the short term. Stakeholders have said that they are more concerned about the lack of exploration activity. Only one well was drilled in the first quarter of 2016, so more has to be done to stimulate exploration. Can the Minister confirm whether any plans are in the pipeline—excuse the pun, but we have to get our fun somewhere in the Finance Bill—to stimulate exploration on the UK continental shelf in the short term?

I have also heard concerns from the industry about the late-life asset market. As we have heard today from Scottish Members, decommissioning is a normal part of a production cycle, but it is very expensive. I am aware that a tax relief is available, but it depends on a company's tax history. If new companies buy older fields, they cannot access the relief, thus blocking late-life asset trade. Essentially, assets are not being sold on as they should be. The policy paper on the 2016 Budget states that the Government are open to exploring

"whether decommissioning tax relief could better encourage transfers of late-life assets",

if "significant progress" on reducing the cost of decommissioning has been made. I worry that that is rather vague. I would therefore welcome clarification from the Minister on exactly what "significant progress" means.

Clauses 55 to 59 make minor changes to the investment allowance, cluster area allowance and onshore allowance. These three allowances provide relief by reducing the amount of ring-fenced profits on which the supplementary charge is due. Investment and cluster area allowances are given at a rate of 62.5%, and onshore allowance at 75%. Clauses 55 and 58 update the conditions that disqualify expenditure from generating investment allowance and cluster area allowance respectively. They expand the conditions following the extension of the allowance to include some leasing expenditure by secondary legislation not yet enacted. As we have heard from the Minister, this is to ensure that there are no gaps in the legislation that would permit these allowances to be generated twice. This will have effect for expenditure incurred on or after 16 March 2016.

The clauses are technical measures with which I have no issue whatever. However, stakeholders have expressed frustration that it has taken so long to lay before Parliament the regulations extending the allowances. According to Oil & Gas UK, the consultation on the draft statutory instrument concluded in January, and since then things have gone quiet. Could the Minister take this opportunity to confirm exactly when the draft SI will be laid before Parliament?

10.15 am

Clauses 56 and 59 give the Government power to extend the meaning of "relevant income" in relation to both investment allowance and cluster area allowance. The Government intend to allow tariff income to activate the allowances. When these allowances were introduced, they could be activated only by production of income from an oilfield. The allowance did not work well if the investment was in a pipeline that the company owned, but that transported another company's oil and gas, which generated tariff income. In that case, no production income was generated, so the allowance was not activated.

The Government originally intended to include tariff income, but it was not included in the original legislation because of the complexities of identifying and apportioning capital expenditure to infrastructure owners and users. Having taken steps, the Government now intend to allow tariff income to activate the allowance, in order to encourage investment in infrastructure. The clauses give the Government power, through secondary legislation, to expand the meaning of "relevant income" to include tariff income. We are wholly supportive of that extension. Will the Minister assure me that the introduction of secondary legislation to expand the allowances to include leasing expenditure will not be delayed while the Government draft the SI to include tariff income in "relevant income"? Time is of the essence when it comes to supporting investment in the UK continental shelf. The industry simply cannot wait for the legislation to be published while the Government get their act together.

Clause 57 relates to onshore allowances, which reduce the amount of ring-fenced profits subject to the supplementary charge to the equivalent of 75% of capital expenditure on onshore oil and gas fields. When it was introduced, there were no disqualifying conditions and a few loopholes were identified, including the ability to generate the allowance twice on an asset. The clause amends the onshore allowance to mirror disqualifying conditions for the cluster area allowance, essentially tightening up the legislation.

The Opposition had some concerns about the onshore allowance when it was introduced in the Finance Act 2014, and we pressed our amendment to a vote. That amendment called for a review examining the impact on onshore oil and gas exploration and field developments in the next 10 years, and the differential impact on individual shale fields, among other things. We are pleased that the Government are introducing disqualifying conditions to provide parity with other allowances, but are still concerned that the allowance provides an incentive for fracking. Why is this allowance more generous than those for investment in cluster areas? Will the Minister also confirm when the advice from the Committee on Climate Change on how fracking will affect the UK's ability to meet our climate change targets will be published? We will support clause 57, but I hope the Minister will address my concerns.

New clauses 3 and 6 were tabled by the hon. Member for Kirkcaldy and Cowdenbeath. New clause 3, as we have heard, calls for a comprehensive review of the corporation tax rate and the investment allowances applicable to oil and gas companies. New clause 6 calls for a review of how the tax regime could be changed to increase the competitiveness of UK-registered companies bidding for supply chain contracts associated with the decommissioning of oil and gas infrastructure. As I mentioned earlier, the sector has identified significant issues with the late-life asset market. We support the Scottish National party in its calls for a review of decommissioning contracts. Legislation surrounding the UK oil and gas tax regime has been remarkably piecemeal, and a review of the whole regime would not be unhelpful. We support all the clauses in this group. I look forward to the Minister's response.

Damian Hinds: It is a pleasure to respond to the pertinent questions put by the Opposition and SNP Front Benchers. They both asked about exploration, which is the lifeblood of the industry's future. We had a choice: introduce a complex system of reliefs and incentives relating to exploration, or have a simple, straightforward tax cut across the board. We chose the latter. Reducing the tax payable on the economic activity lowers the hurdle point for investments, improves the net present value of projects, and means that more will take place. It is cutting the headline rates of tax, rather than anything else, that provides a clear incentive to invest in the continental shelf. The Government have also twice provided £20 million for seismic surveying to help kick-start those processes.

Allowances came up a number of times. Over the past few years, the Government have been simplifying that system. Allowances mean that projects that are economic, but not commercial at the higher rates of tax, can go ahead. That is good for the Exchequer, as it brings in more income, and good for the companies concerned. The hon. Member for Salford and Eccles, who speaks for the Opposition, asked when the Government would finalise the secondary legislation expanding the definition of qualifying expenditure for the investment cluster area allowances. Draft legislation was published at the end of last year and the technical consultation ended in January. HMRC has been analysing the responses to that and liaising with the Treasury and the OGA to ensure that the legislation works as intended. We plan to lay the new regulation before the House after the summer recess. It will apply to all qualifying expenditure incurred after 8 October 2015.

The hon. Lady also asked about the power to extend the definition of relevant income and the timing. The Treasury will consult with industry shortly, and will ask it to provide information and evidence to inform the design of the inclusion of tariff income in the investment cluster area allowances. It is a complex area, with a range of commercial arrangements that we need to understand if we are to ensure that infrastructure owners and users can benefit from the allowances. The power has been drafted in such a way as to ensure that the inclusion of tariff income can have a retrospective effect. That measure will not delay the introduction of the extension to qualifying expenditure.

The hon. Member for Coatbridge, Chryston and Bellshill rightly asked about the crucial opportunity area of decommissioning. Decommissioning across the shelf is expected to become a multibillion-pound industry, and there are significant export opportunities as other basins around the world become more mature. Decommissioning costs here could be more than £40 billion. As I said earlier, the Government support Sir Ian Wood's vision of establishing north-east Scotland as a real centre of excellence. That is why we support the creation of an oil and gas technology centre in Aberdeen as part of its city deal. As the hon. Gentleman will know, the OGA will soon publish its United Kingdom continental shelf decommissioning plan.

The hon. Gentleman and the hon. Member for Salford and Eccles asked about late-life assets and asset transfers. We are in constant discussion with the OGA and industry to understand what impediments there may be to value-creating deals going ahead, and we retain an absolutely open mind on that. The hon. Gentleman also asked about Government guarantees. Again, that is something on which the Government have an open mind, in recognition of the importance of the sector. The Government are willing to consider proposals for using the UK guarantee scheme for infrastructure where that could help to secure new investment in assets of strategic importance to maximise economic recovery. Any proposals would need to meet the scheme's criteria, including those relating to commerciality and financial credibility.

[Damian Hinds]

The Government have recognised the exceptionally challenging conditions that the industry faces, and in response announced a £1 billion package of fiscal reforms in the March 2016 Budget, which built on the extensive package from the previous year. The package includes halving the rate of the supplementary charge, permanently zero-rating the petroleum revenue tax, and extending the scope of key allowances to incorporate leasing and to encourage investment across the North sea. The Government have also committed £20 million of funding to a second round of seismic surveys to encourage development in under-explored areas.

Despite the extremely challenging conditions, this remains a sector of opportunity for Scotland and the UK; it is estimated that somewhere between 11 billion and 21 billion barrels of oil and oil equivalents are still to be had. More than £11 billion was invested in the sector last year. I am constantly encouraged by the positive attitude of the industry, and all the work that it is doing to get its cost base down and continue to look for new opportunities. I assure you, Mr Howarth, and all hon. Members, of the Government's absolute commitment to the very positive tripartite approach between the industry, the Oil and Gas Authority, which is really more than a regulator, and the Government, who include the Scotland Office, the Department of Energy and Climate Change and the Treasury.

Christian Matheson (City of Chester) (Lab): There is no doubt that the UK offshore oil and gas sector has a world lead, provides huge revenue and technical expertise to the UK, and needs to be protected, but my hon. Friend the Member for Salford and Eccles raised the spectre of onshore fracking. Can the Minister give reassurance that our efforts to support the offshore oil and gas industry will not be used as a back-door way of giving tax breaks to onshore fracking?

Damian Hinds: Mr Howarth, you would not want me to stray on to topics that are not strictly in the scope of the Finance Bill. The Government believe that there is significant potential for unconventional oil and gas—for fracking—and I think that we owe it to future generations, to ourselves and to British industry to make sure that we discover what opportunities are there. Exactly how the regime develops, in fiscal terms, is to be determined, but we know that there will be an absolutely robust safety regime. In the initial phase, the important thing is to find out on how big a scale that opportunity may be.

I had reached the conclusion of my remarks, having reiterated the very firm commitment across Government to supporting this industry. This is a bold package of support in the Budget. We know of no other country in the world that has responded on quite such a scale to the extremely challenging conditions presented by the world oil price. I commend the clause to the Committee.

Question put and agreed to.

Clause 54 accordingly ordered to stand part of the Bill.

Clauses 55 to 59 ordered to stand part of the Bill.

The Chair: I remind the Committee that I will put the question on clause 128—and new clauses 3 and 6, if required—without further debate when we reach them.

Clause 60

Profits from the exploitation of patents etc

Mr Gauke: I beg to move amendment 50, in clause 60, page 94, line 16, at end insert

", or

'(b) the company elects to be treated as a new entrant for the purposes of this Part.'"

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

Government amendments 51 to 115 and 136.

Clause stand part.

Government amendments 116 to 121.

That schedule 9 be the Ninth schedule to the Bill.

Mr Gauke: Clause 60 and schedule 9 make changes to ensure that the UK's patent box operates in line with a newly agreed international framework resulting from the base erosion and profit shifting action plan. The Forum on Harmful Tax Practices—the international group leading work on action 5—focused on harmonising the level of substantive activity required for access to preferential intellectual property regimes such as the patent box. This was linked to the BEPS action plan's overall aim of aligning taxation with economic substance. The framework applies to all patent and innovation box-type regimes that apply preferential tax treatment to IP income in OECD, G20 and EU countries. It ensures that preferential tax treatment cannot be offered for as little as simply registering ownership of IP in a jurisdiction offering such a regime. While the UK's patent box includes adequate safeguards to address these concerns, this framework will ensure that robust standards apply internationally.

The new framework also takes a slightly different approach from the UK patent box, so amendments to the current regime are required. In particular, the international framework links the availability of a lower tax rate offered by a preferential IP regime to the proportion of the development expenditure on the IP that the claimant taxpayer incurred, directly or through a third-party subcontractor. This means that if, for example, a claimant taxpayer directly incurred only half of the expenditure on a patent, with the other half of the expenditure being on acquisition, IP, or outsourcing to a related party, only half the profit derived from that patent will benefit from a lower tax rate.

10.30 am

The patent box was introduced in the Finance Act 2012 following extensive consultation. Once fully phased in, it gives an effective corporation tax rate of 10% on trading profits earned from patents and other similar types of intellectual property. To qualify under current rules, the claimant taxpayer needs either to have had significant involvement in the development of the IP or to actively manage the IP in the UK. That will not change. The patent box provides an incentive for companies to develop, retain and commercialise new and existing patents in the UK. That in turn incentivises companies to bring to the UK high-value jobs and investment associated with the development, manufacturer and exploitation of patents.

The changes made by clause 60 will bring the UK patent box in line with the new international framework. The main change is the introduction of the research and development fraction, which provides the link between the IP profit and the R and D undertaken on that IP, implementing the key principle of the international framework. The fraction is defined as the ratio of the company's direct R and D spend on the IP plus any third-party subcontracting to total spend, which adds in the cost of acquiring the IP and related party subcontracting.

The figures in the ratio are cumulative, building up over time to reflect the development history of the IP asset. The result can be increased by up to 30% when the ratio is less than 1, although the final value cannot exceed 1. The final value is then applied to the relevant IP profits to give the amount of profit that can benefit from the lower patent box tax rate. The qualifying profit will be the same or less than the amount under the current patent box rules. If in exceptional circumstances the ratio is not a true reflection of the claimant's value-creating activities, the company may be able to increase it accordingly to take such circumstances into account. The new rules apply from July 2016.

As the UK already has a patent box, transitional provisions are needed for companies already claiming for existing IP. To allow claimant taxpayers to ensure that they can comply with the requirements of the new patent box, a five-year transitional period begins on 30 June 2016, after which only those taxpayers who would qualify to elect into the patent box for periods prior to that date will be allowed to claim under the current rules. A claimant taxpayer will be able to continue to apply the current patent box rules for existing IP if it qualifies for the transitional period and there are no major changes to its position during that period. An existing IP broadly means patents applied for before 1 July 2016.

If a company has income from a product that relies on existing IP and patents applied for on or after that date, it will continue to be treated according to the current patent box rules, as long as the core technology of that product is protected by patents applied for before 1 July 2016. If that is not the case, the profit from the product will transition to the new rules linked to the proportion of patents that do not qualify as existing IP over total patents. The transitional period will end five years later on 30 June 2021, after which only the new form of the patent box will be available.

The transitional arrangements will not be available where IP has been acquired directly or indirectly from a country without a preferential IP regime after 1 January 2016, and that acquisition was undertaken with a tax avoidance motive. That safeguards the transitional provisions from an abuse whereby a company would aim to acquire IP simply to access the five-year period. That safeguard is part of the international framework and so applies to all preferential IP regimes, including the UK patent box.

Those affected by the changes are UK companies that hold and exploit patents or patent-like rights and that claim relief under the current patent box. We expect that these changes will restrict the overall amount that can be claimed through the patent box, reducing cost to the Exchequer. That reduction is expected to be £120 million over the next five years.

The Government amendments to clause 60 introduce features that ensure that the benefit of the patent box is protected for claimant taxpayers and respond to specific issues raised by interested parties during formal consultation. If some of these amendments were not introduced, a number of interested parties would see their claims significantly reduced under the new patent box rules. The new rules could also potentially be open to manipulation and abuse. These amendments do not cover provisions addressing the issue of how the revised rules will apply in the context of more complex, collaborative R and D arrangements, such as cost share agreements. It is the Government's intention to include such provisions in Finance Bill 2017, to provide an opportunity for consultation with interested parties.

Amendment 50 allows taxpayers to forgo the right to use the transitional provisions, should they prefer to opt straight into the new patent box. Amendments 51 to 56, 60 to 63, 69 to 70, 78 to 79 and 88 to 112 give companies greater flexibility to track IP income and R and D expenditure at product or product family level, by removing the requirement that a product must contain more than one IP asset. We have created rules to account for the implementation of the international framework, which, incidentally, has a double impact on a taxpayer's patent box claims where an acquisition of IP involves staged payments made to the seller, allowing for sharing in the success of further development. We are also extending the definition of an acquisition of IP to cover expenditure on such an acquisition from which the relevant qualifying IP is derived, evolved or enhanced. These features are introduced by amendments 57, 66, 77, 80 and 81, and 121.

Amendments 58 and 59, 64, 67, 82 to 84 and 116 to 120 introduce simplification rules for taxpayers with smaller claims, so that they are not discouraged from claiming the patent box. Amendment 65 addresses the fact that legislation does not currently exclude finance income from the overall income that can benefit from the patent box; the measures would otherwise result in unintentional widening of the patent box.

Amendments 68, 73 and 74 ensure that any relevant R and D expenditure incurred by a foreign branch of a UK claimant company that has opted out of UK taxation under foreign branch exemption rules is treated as related party subcontract expenditure of the UK company for the purposes of calculating the R and D fraction. Under the Bill, only 65% of subcontracted R and D costs are used in the R and D fraction. Amendments 71, 72, 75 and 76 remove the treatment on subcontracted R and D costs, so that the entire amount is counted towards qualifying expenditure amounts.

The safeguard in the transitional provisions requires a determination as to whether an IP asset has been acquired from a country with or without a preferential IP regime in place. Amendments 85 to 87 clarify that the power to designate foreign tax regimes operates properly when it is used after Royal Assent. Amendment 113 widens the existing anti-avoidance provisions to take into account potential abuses of the changing rules. Finally, amendments 114 and 115 ensure that where one company takes over a trade from another, the transferee will be able to step into the shoes of the transferrer, inheriting both the IP and the expenditure history on that IP.

Let me briefly anticipate and respond to amendment 136, which would require the Chancellor of the Exchequer to publish

"within six months of the passing of this Act"

a report on the patent box, giving an

"assessment of the value for money…and…efficacy of, the Patent Box."

This amendment is not needed and would fall short of the plans the Government already have in place. Due to the time periods allowed for electing into the patent box and the impact of the transitional provisions, a one-time publication would not give a substantive picture of how the patent box is operating, or take into account the revisions to the regime. That is why we are proposing to publish annual statistics on the patent box, rather than a one-time publication. The Government intend to make the first publication in September this year and annually thereafter.

To conclude, the changes made by clause 60 will ensure that the patent box complies with the new internationally agreed framework, while the amendments ensure that the benefit of the patent box is protected for claimant taxpayers. I therefore commend clause 60, schedule 9 and amendments 50 to121.

Rebecca Long Bailey: Clause 60 and schedule 9 make substantial changes to the patent box, which provides for a reduced rate of corporation tax on profits from patents and similar intellectual property. The changes in this clause ensure compliance with the new international framework developed by the OECD for preferential IP regimes as part of the base erosion and profit shifting project.

The changes mean that the amount of profit for an IP asset that qualifies for the reduced 10% rate of corporation tax available through the UK patent box will depend on the proportion of the asset's development expenditure incurred by the company. According to the explanatory notes to the Bill, the amended rules will require profit for the purpose of the patent box to be calculated at the level of an IP asset—for example, the patent, product, or product family relying on an IP asset or assets. The profit will be adjusted to reflect the proportion of the development activity on the asset, product, or product category undertaken by the company.

As the Minister confirmed, the measure will have effect for new entrant companies to the patent box on or after 1 July 2016, and also for some IP assets acquired on or after 2 January 2016. The new rules are being phased in, which is welcome; the current patent box rules will apply to some companies and IP throughout a transitional period lasting until 2021. The new rules will apply to all companies and IP after 2021.

By way of background, in December 2009 the Labour Government announced that they would consult on introducing a patent box—a reduced rate of corporation tax applied to income from patents—from April 2013 at a possible annual cost of £1.3 billion. The coalition Government took up our proposals for a patent box in a wider review of corporate taxation launched in November 2010. The consultation document argued that a tax relief would be most effective if it focused on patents, and that it would be proportionate to charge corporation tax at just 10% on profits made from them.

The coalition Government confirmed their plans in the 2011 Budget, and published a further consultation document in June. Draft legislation for the Finance Bill 2012 was published in December, including provisions for the patent box. In Budget 2012, the Government confirmed the introduction of the patent box, which would be phased in over five years from 1 April 2013. They estimated that its cost would rise from £350 million in 2013-14 to £910 million by 2016-17.

The Opposition welcomed the introduction of the relief, while moving an amendment to require the Government to report on

"other opportunities to introduce targeted support for business".

This tax reform was clearly strongly supported by business at the time, but was not uncontroversial. Concerns were raised by several European countries, as well as the European Commission, that reform might represent harmful tax competition, encouraging companies to shift the ownership of patents created in other countries to the UK.

In late 2013, the EU code of conduct group raised concerns about the UK patent box, leading to press speculation that the Government might have to substantively amend the new relief. In November 2014, the Government announced that the UK had agreed with Germany that preferential intellectual property regimes—of which the UK patent box is one—should not encourage harmful tax competition and, as a result, certain changes would be made to the UK regime from June 2016. Subsequently, in October 2015, HMRC launched a consultation on amending the patent box regime to take account of these concerns. In December 2015, draft legislation to give effect to this change was published along with an impact note on the measure.

The 2016 Budget specifically confirmed that

> "The government will modify the operation of the Patent Box to comply with a new set of international rules created by the OECD, making the lower tax rate dependent on, and proportional to, the extent of research and development expenditure incurred by the company claiming the relief. This will come into effect on 1 July 2016."

10.45 am

According to the commentary in the *Tax Journal*,

> "Whilst the majority of the provisions are consistent with the draft clauses released in December 2015, there were a number of important changes and previously omitted items included in the Bill."

Those include flexibility for the grandfathering of products that contain both pre-1 July IP qualifying rights and post-30 June IP qualifying rights, and a provision allowing for an increase in the R and D fraction in exceptional circumstances. Perhaps the Minister could take this opportunity to confirm what would constitute exceptional circumstances.

The *Tax Journal* goes on to say:

> "The default length of the 'relevant period' for tracking and tracing R&D expenditure to the IP has been extended from 15 years to 20 years. In addition, a new provision has been introduced within the relevant period rules to provide clarification on the timing of expenditure for tracking and tracing purposes. Whilst this rule looks to align the timing of expenditure with the time at which it becomes deductible for corporation tax purposes, it should also act as an anti-forestalling measure. Unfortunately, despite representations, it seems that a company is only able to track and trace R&D expenditure at product family level (rather than as individual IP rights) where the product contains more than one item of IP. This remains a significant issue for some taxpayers."

Could the Minister confirm why that is the case?

My hon. Friends and I have tabled amendment 136 because we have heard from stakeholders that the efficacy of the patent box may be somewhat undermined as a result of the changes to ensure that we comply with the OECD recommendations. We support the principle of the patent box—indeed, we brought it in—but we also think that it needs to be reviewed in the light of these changes to make sure that it is the best mechanism to achieve its desired aim of incentivising patents based in the UK. Furthermore, the necessity for clause 60 and schedule 9 is somewhat in question, given the country's decision to leave the EU; I made a similar point about earlier clauses. Has the Minister considered the implications of the vote on the patent box? We are happy to accept Government amendments 50 to 121, which were tabled after consultation with stakeholders.

To conclude, we are very supportive of the patent box, but we have concerns about its efficacy, given all these changes. I hope that the Minister can address some of the concerns I have raised, but I will not push amendment 136 to a vote.

Mr Gauke: I thank the hon. Lady for her broad support for the patent box. What we sought to do with the patent box—both when it was introduced and now—is ensure that we have incentives in our tax system to encourage internationally mobile activity. This is about bringing jobs and investment to the United Kingdom. It is not about artificial profit shifting. On the Government's wider approach to the international tax system, we believe that there should be close alignment between economic activity, the profits that relate to that, and where those profits are taxed. That is why the UK has taken a leading role in the OECD's base erosion and profit shifting process. Of course, any process like BEPS requires compromise, but the direction in which we believe the international tax system should go—towards closer alignment—is the one that BEPS has pursued, and we are pleased with the outcomes.

The changes to the patent box reflect a degree of compromise, but in essence, thanks to the patent box, the UK continues to offer an attractive place in which intellectual property may be developed. That is something that we wish to continue. I have to pick up on three of the points made by the hon. Member for Salford and Eccles. In the context of the EU, I will make a similar point to one I made earlier: we are still in the EU and a negotiation has yet to be undertaken to know where we stand exactly. There is also a wider point: when addressing the challenges of the international tax system, much of the legislation would apply whether we were in the EU or not, because the OECD BEPS process applies to all OECD countries. I do not think that anyone is proposing a referendum on whether we should leave the OECD—it is not one that I would welcome. In these circumstances, we expect to comply with the OECD standard, and that is very much our approach.

The hon. Lady also made a couple of technical points, the first of which was about what constitutes exceptional circumstances. For example, IP might have been purchased but turned out to be worth less, so that its contribution to the fraction is out of line with the cost. Obviously I cannot be exhaustive, but I hope that example is helpful in illustrating the types of things we are talking about. She also asked about tracking and tracing at an individual product level, and why that is not the approach we have taken. Companies will be able to track and trace at IP product level, so I hope that she is reassured, but I will write to her with further information.

Amendment 50 agreed to.

Amendments made: 51, in clause 60, page 94, line 38, leave out "either".

Amendment 52, in clause 60, page 94, line 43, leave out "multi-IP" and insert "IP".

Amendment 53, in clause 60, page 94, line 43, at end insert

", or

(c) a sub-stream consisting of income properly attributable to a particular kind of IP process (a "process sub-stream")".

Amendment 54, in clause 60, page 95, line 1, leave out from "See" to second "and" and insert

"subsection (5) for the meaning of "IP item" and "IP process"".

Amendment 55, in clause 60, page 95, line 2, before "further" insert

"see subsections (5A) and (6) for".

Amendment 56, in clause 60, page 95, line 2, at end insert "and process sub-streams".

Amendment 57, in clause 60, page 95, line 12, at end insert—

"But see section 357BIA (which provides that certain amounts allocated to a relevant IP income sub-stream at Step 3 are not to be deducted from the sub-stream at this Step)."

Amendment 58, in clause 60, page 95, leave out lines 13 to 17.

Amendment 59, in clause 60, page 95, line 19, leave out from beginning to "deduct" in line 20.

Amendment 60, in clause 60, page 95, leave out lines 40 to 47 and insert—

"(5) In this section—

"IP item" means—

(a) an item in respect of which a qualifying IP right held by the company has been granted, or

(b) an item which incorporates one or more items within paragraph (a);

"IP process" means—

(a) a process in respect of which a qualifying IP right held by the company has been granted, or

(b) a process which incorporates one or more processes within paragraph (a).

(5A) For the purposes of this section two or more IP items, or two or more IP processes, may be treated as being of a particular kind if they are intended to be, or are capable of being, used for the same or substantially the same purposes."

Amendment 61, in clause 60, page 95, line 48, leave out

"which is properly attributable to a multi-IP item".

Amendment 62, in clause 60, page 95, line 49, after "sub-stream" insert "or process sub-stream".

Amendment 63, in clause 60, page 96, line 5, at end insert—

'( ) Any reference in this section to a qualifying IP right held by the company includes a reference to a qualifying IP right in respect of which the company holds an exclusive licence."

Amendment 64, in clause 60, page 98, line 2, leave out "357A" and insert "357A(1)".

Amendment 65, in clause 60, page 98, line 21, after first "income" insert ", finance income".

Amendment 66, in clause 60, page 100, line 41, at end insert—

"357BIA Certain amounts not to be deducted from sub-streams at Step 4 of section 357BF

(1) This section applies where a company enters into an arrangement with a person under which—

(a) the person assigns to the company a qualifying IP right or grants or transfers to the company an exclusive licence in respect of a qualifying IP right, and

(b) the company makes to the person an income-related payment.

(2) A payment is an "income-related payment" for the purposes of subsection (1) if—

(a) the obligation to make the payment arises under the arrangement by reason of the amount of income the company has accrued which is properly attributable to the right or licence, or

(b) the amount of the payment is determined under the arrangement by reference to the amount of income the company has accrued which is so attributable.

(3) If the amount of the income-related payment is allocated to a relevant IP income sub-stream at Step 3 of section 357BF(2), the amount is not to be deducted from the sub-stream at Step 4 of section 357BF(2) unless the payment will not affect the R&D fraction for the sub-stream."

Amendment 67, in clause 60, page 104, line 6, leave out from beginning to end of line 31 on page 105.

Amendment 68, in clause 60, page 108, line 13, at end insert—

"(3A) If an election made by the company under section 18A of CTA 2009 (election for exemption for profits or losses of company's foreign permanent establishments) applies to the relevant period, expenditure incurred by the company during the period which meets conditions A and B—

(a) is not "qualifying expenditure on relevant R&D undertaken in-house", but

(b) is "qualifying expenditure on relevant R&D sub-contracted to connected persons",

so far as it is expenditure brought into account in calculating a relevant profits amount, or a relevant losses amount, aggregated at section 18A(4)(a) or (b) of CTA 2009 in calculating the company's foreign permanent establishments amount for the period."

Amendment 69, in clause 60, page 108, line 22, leave out

"incorporated in a multi-IP item"

and insert

"—

(i) to which income in the sub-stream is attributable, or

(ii) which is incorporated in an item".

Amendment 70, in clause 60, page 108, line 23, at end insert

", or

(c) in a case where the sub-stream is a process sub-stream, relates to a qualifying IP right granted in respect of any process—

(i) to which income in the sub-stream is attributable, or

(ii) which is incorporated in a process to which income in the sub-stream is attributable."

Amendment 71, in clause 60, page 109, line 8, leave out "65% of any" and insert "the".

Amendment 72, in clause 60, page 109, leave out lines 10 to 15 and insert

"in making payments within subsection (2).

(2) A payment is within this subsection if—

(a) it is made to a person in respect of relevant research and development contracted out by the company to the person, and

(b) the company and the person are not connected (within the meaning given by section 1122)."

Amendment 73, in clause 60, page 109, line 15, at end insert—

"(3) If an election made by the company under section 18A of CTA 2009 (election for exemption for profits or losses of company's foreign permanent establishments) applies to the relevant period, expenditure incurred by the company during the period in making payments within subsection (2)—

(a) is not "qualifying expenditure on relevant R&D sub-contracted to unconnected persons", but

(b) is "qualifying expenditure on relevant R&D sub-contracted to connected persons",

so far as it is expenditure brought into account in calculating a relevant profits amount, or a relevant losses amount, aggregated at section 18A(4)(a) or (b) of CTA 2009 in calculating the company's foreign permanent establishments amount for the period."

Amendment 74, in clause 60, page 109, line 23, after "means" insert "the total of—

(a) any expenditure which is "qualifying expenditure on relevant R&D sub-contracted to connected persons" as a result of section 357BMB(3A) or 357BMC(3) (certain expenditure attributed to company's foreign permanent establishments), and

(b) ".

Amendment 75, in clause 60, page 109, line 23, leave out "65% of any" and insert "the".

Amendment 76, in clause 60, page 109, leave out lines 25 to 30 and insert

"in making payments within subsection (2).

'(2) A payment is within this subsection if—

(a) it is made to a person in respect of relevant research and development contracted out by the company to the person, and

(b) the company and the person are connected (within the meaning given by section 1122)."

Amendment 77, in clause 60, page 109, line 39, leave out from "company" to end of line 41 and insert

"in making during the relevant period payments within any of subsections (1A), (1B) and (1C).

(1A) A payment is within this subsection if it is made to a person in respect of the assignment by that person to the company of a relevant qualifying IP right.

(1B) A payment is within this subsection if it is made to a person in respect of the grant or transfer by that person to the company of an exclusive licence in respect of a relevant qualifying IP right.

(1C) A payment is within this subsection if—

(a) it is made to a person in respect of the disclosure by that person to the company of any item or process, and

(b) the company applies for and is granted a relevant qualifying IP right in respect of that item or process (or any item or process derived from it).

(1D) Where the company has incurred expenditure in making a series of payments to a person in respect of a single assignment, grant, transfer or disclosure, each of the payments in the series is to be treated for the purposes of this section as having been made on the date on which the first payment in the series was made."

Amendment 78, in clause 60, page 110, line 2, leave out

"incorporated in a multi-IP item" and insert "—

(i) to which income in the sub-stream is attributable, or

(ii) which is incorporated in an item".

Amendment 79, in clause 60, page 110, line 4, at end insert

", or

(c) in a case where the sub-stream is a process sub-stream, a qualifying IP right granted in respect of a process—

(i) to which income in the sub-stream is attributable, or

(ii) which is incorporated in a process to which income in the sub-stream is attributable."

Amendment 80, in clause 60, page 110, line 22, leave out "357BME" and insert "357BMD".

Amendment 81, in clause 60, page 111, leave out from beginning of line 8 to ", and" in line 11 and insert

"in each of subsections (1A), (1B) and (1C) the word "relevant" were omitted".

Amendment 82, in clause 60, page 112, line 25, leave out "357A" and insert "357A(1)".

Amendment 83, in clause 60, page 112, line 46, at end insert—

"Small claims treatment

357BNA Small claims treatment

(1) This section applies where—

(a) a company carries on only one trade during an accounting period,

(b) section 357BF applies for the purposes of determining the relevant IP profits of the trade for the accounting period, and

(c) the qualifying residual profit of the trade for the accounting period does not exceed whichever is the greater of—

(i) £1,000,000, and

(ii) the relevant maximum for the accounting period.

(2) The company may make any of the following elections for the accounting period—

(a) a notional royalty election (see section 357BNB),

(b) a small claims figure election (see section 357BNC), and

(c) a global streaming election (see section 357BND).

This is subject to subsections (3) and (4).

(3) The company may not make a notional royalty election, a small claims figure election or a global streaming election for the accounting period if—

(a) the qualifying residual profit of the trade for the accounting period exceeds £1,000,000,

(b) section 357BF applied for the purposes of determining the relevant IP profits of the trade for any previous accounting period beginning within the relevant 4-year period, and

(c) the company did not make a notional royalty election, a small claims figure election or (as the case may be) a global streaming election for that previous accounting period.

(4) The company may not make a small claims figure election for the accounting period if—

(a) the qualifying residual profit of the trade for the accounting period exceeds £1,000,000,

(b) section 357C or 357DA applied for the purposes of determining the relevant IP profits of the trade for any previous accounting period beginning within the relevant 4-year period, and

(c) the company did not make an election under section 357CL for small claims treatment for that previous accounting period.

(5) In subsections (3) and (4) "the relevant 4-year period" means the period of 4 years ending with the beginning of the accounting period mentioned in subsection (1)(a).

(6) For the purposes of this section, the "qualifying residual profit" of a trade of a company for an accounting period is the amount which (assuming the company did not make an election under this section) would be equal to the aggregate of the relevant IP income sub-streams established at Step 2 in section 357BF(2) in determining the relevant IP profits of the trade for the accounting period, following the deductions from those sub-streams required by Step 4 in section 357BF(2) (ignoring the amount of any sub-stream which is not greater than nil following those deductions).

(7) For the purposes of this section, the "relevant maximum" for an accounting period of a company is—

(a) in a case where no company is a related 51% group company of the company in the accounting period, £3,000,000;

(b) in a case where one or more companies are related 51% group companies of the company in the accounting period, the amount given by the formula—

$$\frac{£3{,}000{,}000}{1+N}$$

where N is the number of those related 51% group companies in relation to which an election under section 357A(1) has effect for the accounting period.

(8) For an accounting period of less than 12 months, the relevant maximum is proportionally reduced.

357BNB Notional royalty election

(1) Subsection (2) applies where a company has made a notional royalty election for an accounting period under section 357BNA(2)(a).

(2) In its application for the purposes of determining the relevant IP profits of the trade of the company for the accounting period, section 357BHA (notional royalty) has effect as if—

(a) in subsection (2) for "the appropriate percentage" there were substituted "75%", and

(b) subsections (3) to (6) were omitted."

357BNC Small claims figure election

(1) Subsection (2) applies where a company has made a small claims figure election for an accounting period under section 357BNA(2)(b).

(2) In its application for the purposes of determining the relevant IP profits of the trade of the company for the accounting period, section 357BF(2) (steps for calculating relevant IP profits) has effect as if in Step 6—

(a) for "marketing assets return figure" there was substituted "small claims figure", and

(b) for "(see section 357BL)" there was substituted "(see section 357BNC(3))".

(3) Subsections (4) to (9) apply for the purpose of calculating the small claims figure for a relevant IP income sub-stream established at Step 2 in section 357BF(2) in determining the relevant IP profits of a trade of a company for an accounting period.

(4) If 75% of the qualifying residual profit of the trade for the accounting period is lower than the small claims threshold, the small claims figure for the sub-stream is 25% of the amount of the sub-stream following Step 4 in section 357BF(2).

(5) If 75% of the qualifying residual profit of the trade for the accounting period is higher than the small claims threshold, the small claims figure for the sub-stream is the amount given by—

$$A - \left(\frac{A}{QRP} \times SCT\right)$$

where—

A is the amount of the sub-stream following the deductions required by Step 4 in section 357BF(2),

QRP is the qualifying residual profit of the trade of the company for the accounting period, and

SCT is the small claims threshold.

(6) If no company is a related 51% group company of the company in the accounting period, the small claims threshold is £1,000,000.

(7) If one or more companies are related 51% group companies of the company in the accounting period, the small claims threshold is—

$$\frac{£1,000,000}{1+N}$$

where N is the number of those related 51% group companies in relation to which an election under section 357A(1) has effect for the accounting period.

(8) For an accounting period of less than 12 months, the small claims threshold is proportionately reduced.

(9) Subsection (6) of section 357BNA (meaning of "qualifying residual profit") applies for the purposes of subsection (4) and (5) of this section.

357BND Global streaming election

(1) Subsection (2) applies where a company has made a global streaming election for an accounting period under section 357BNA(2)(c).

(2) In its application for the purpose of determining the relevant IP profits of the trade of the company for the accounting period, this Chapter has effect with the following modifications.

(3) In subsection (2) of section 357BF (relevant IP profits)—

(a) omit Step 2,

(b) in Step 3 for "each of the relevant IP income sub-streams" substitute "the relevant IP income stream",

(c) in Step 4—

(i) in the words before paragraph (a), for "each" substitute "the",

(ii) for "sub-stream", in each place it occurs, substitute "stream",

(d) in Step 6—

(i) at the beginning insert "If the relevant IP income stream is greater than nil following Step 4,",

(ii) for the words from "each" to "Step 4" substitute "the stream",

(iii) for "sub-stream", in the second place it occurs, substitute "stream",

(e) in Step 7—

(i) for "each relevant IP income sub-stream" substitute "the relevant IP income stream",

(ii) for "sub-stream", in the second place it occurs, substitute "stream",

(f) omit Step 8, and

(g) in Step 9 for "given by Step 8" substitute "of the relevant IP income stream following Step 7".

(4) In subsection (3) of that section for "given by" substitute "of the relevant IP income stream following the Steps in".

(5) In subsection (4) of that section for "given by" substitute "of the relevant IP income stream following the Steps in".

(6) Omit subsections (5), (5A) and (6) of that section.

(7) In section 357BIA(3) (certain amounts not to be deducted from sub-streams at Step 4 of section 357BF)—

(a) for "a relevant IP income sub-stream" substitute "the relevant IP income stream";

(b) for "sub-stream", in the second and third places it occurs, substitute "stream".

(8) In section 357BJ (routine return figure)—

(a) for "sub-stream", in each place it occurs, substitute "stream", and

(b) in subsection (1) for "Step 2" substitute "Step 1".

(9) In section 357BL (marketing asset return figure) for "sub-stream", in each place it occurs, substitute "stream".

(10) In section 357BLA (notional marketing royalty)—

(a) for "sub-stream", in each place it occurs, substitute "stream", and

(b) in subsection (1) for "Step 2" substitute "Step 1".

(11) In section 357BLB (actual marketing royalty) for "sub-stream", in each place it occurs, substitute "stream".

(12) In section 357BM (R&D fraction: introduction)—

(a) for "sub-stream" (in each place it occurs) substitute "stream", and

(b) in subsection (1) for "Step 2" substitute "Step 1".

(13) In section 357BMA(1) (R&D fraction) for "sub-stream" substitute "stream".

(14) In section 357BMB(4) (qualifying expenditure on relevant R&D undertaken in-house) for the words after "1138)" substitute "which relates to a qualifying IP right to which income in the stream is attributable".

(15) In section 357BME(2) (qualifying expenditure on acquisition of relevant qualifying IP rights) for the words from "means" to the end substitute "means a qualifying IP right to which income in the stream is attributable".

(16) In section 357BMG (cases where the company is a new entrant with insufficient information about pre-enactment expenditure) for "sub-stream", in each place it occurs, substitute "stream".

(17) In section 357BMH (R&D fraction: increase for exceptional circumstances) for "sub-stream", in each place it occurs, substitute "stream".

(18) In section 357BNC (small claims figure election)—

(a) for "sub-stream", in each place it occurs, substitute "stream";

(b) in subsection (3) for "Step 2" substitute "Step 1"."

Amendment 84, in clause 60, page 113, line 17, at end insert—

"( ) Where section 357BF applies by reason of this section for the purposes of determining the relevant IP profits of a trade of a company for an accounting period, the company may not make a global streaming election for the accounting period under section 357BNA(2)(c)."

Amendment 85, in clause 60, page 113, leave out lines 34 to 44 and insert—

"(a) the company and the person who assigned the right or granted the licence were connected at the time of the assignment or grant,

(b) the main purpose, or one of the main purposes, of the assignment of the right or the grant of the licence was the avoidance of a foreign tax,

(c) the person who assigned the right or granted the licence was not within the charge to corporation tax at the time of the assignment or grant, and

(d) the person who assigned the right or granted the licence was not liable at the time of the assignment or grant to a foreign tax which is designated for the purposes of this section by regulations made by the Treasury."

Amendment 86, in clause 60, page 114, line 1, leave out "(9)(b)" and insert "(8)(d)".

Amendment 87, in clause 60, page 114, line 4, at end insert—

"( ) Regulations may not be made under subsection (8)(d) after 31 December 2016."

Amendment 88, in clause 60, page 114, line 21, leave out "(b)" and insert "(c)".

Amendment 89, in clause 60, page 114, line 24, leave out

"and each product sub-stream"

and insert

", each product sub-stream and each process sub-stream".

Amendment 90, in clause 60, page 114, line 32, leave out

"and product sub-streams"

and insert

", each of the product sub-streams and each of the process sub-streams".

Amendment 91, in clause 60, page 114, line 42, leave out "a multi-IP item" and insert

"an IP item or IP process".

Amendment 92, in clause 60, page 114, line 44, after "sub-stream" insert "or process sub-stream".

Amendment 93, in clause 60, page 114, line 45, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 94, in clause 60, page 115, line 1, after "item" insert "or process".

Amendment 95, in clause 60, page 115, line 4, after "item" insert "or process".

Amendment 96, in clause 60, page 115, line 8, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 97, in clause 60, page 115, line 9, leave out "item or items" and insert "items or processes".

Amendment 98, in clause 60, page 115, line 11, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 99, in clause 60, page 115, line 13, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 100, in clause 60, page 115, line 17, after "sub-stream" insert "or process sub-stream".

Amendment 101, in clause 60, page 115, line 18, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 102, in clause 60, page 115, line 20, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 103, in clause 60, page 115, line 24, after "sub-stream" insert "or process sub-stream".

Amendment 104, in clause 60, page 115, line 26, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 105, in clause 60, page 115, line 27, after "sub-stream" insert "or process sub-stream".

Amendment 106, in clause 60, page 115, line 27, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 107, in clause 60, page 115, line 29, after "items" insert "or processes".

Amendment 108, in clause 60, page 115, line 31, leave out "a multi-IP" and insert

"an IP item or IP process".

Amendment 109, in clause 60, page 115, line 35, after "items" insert "or processes"

Amendment 110, in clause 60, page 115, line 35, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 111, in clause 60, page 115, line 38, after "items" insert "or processes".

Amendment 112, in clause 60, page 115, line 38, leave out "multi-IP item" and insert

"IP item or IP process".

Amendment 113, in clause 60, page 115, line 40, at end insert—

"( ) In section 357FB (tax advantage schemes)—

(a) in subsection (2)(b) (list of ways by which deductions can be inflated)—

(i) omit "or" at the end of sub-paragraph (ii), and

(ii) after sub-paragraph (iii) insert ", or

(iv) an R&D fraction (see subsection (4A)) being greater than it would be but for the scheme.", and

(b) after subsection (4) insert—

"(4A) The reference in subsection (2)(b)(iv) to an R&D fraction is a reference to such a fraction as is mentioned at Step 7 of section 357BF(2).""

Amendment 114, in clause 60, page 115, line 40, at end insert—

"( ) After section 357GC insert—

"Transferred trades

357GCA Application of this Part in relation to transferred trades

(1) Where—

(a) a company ("the transferor") ceases to carry on a trade which involves the exploitation of a qualifying IP right ("the relevant qualifying IP right"),

(b) the transferor assigns the relevant qualifying IP right, or grants or transfers an exclusive licence in respect of it, to another company ("the transferee"), and

(c) the transferee begins to carry on the trade,

the following provisions apply in determining under this Part the relevant IP profits of the trade carried on by the transferee.

(2) The transferee is to be treated as not being a new entrant if—

(a) an election under section 357A(1) has effect in relation to the transferor on the date of the assignment, grant or transfer mentioned in subsection (1)(b) ("the transfer date"), and

(b) the first accounting period of the transferor for which that election had effect began before 1 July 2016.

(3) The relevant qualifying IP right is to be treated as being an old qualifying IP right in relation to the transferee if by reason of section 357BP it is an old qualifying IP right in relation to the transferor.

(4) Expenditure incurred prior to the transfer date by the transferor which is attributable to relevant research and development undertaken by the transferor is to be treated for the purposes of section 357BMB as if it is expenditure incurred by the transferee which is attributable to relevant research and development undertaken by the transferee.

(5) Expenditure incurred prior to the transfer date by the transferor in making a payment to a person in respect of relevant research and development contracted out by the transferor to that person is to be treated for the purposes of sections 357BMC and 357BMD as if it is expenditure incurred by the transferee in making a payment to that person in respect of relevant research and development contracted out by the transferee to that person.

(6) Expenditure incurred prior to the transfer date by the transferor in making a payment in connection with the relevant qualifying IP right which is within subsection (1A), (1B) or (1C) of section 357BME is to be treated for the purposes of that section as if it is expenditure incurred by the transferee in making a payment in connection with that right which is within one of those subsections.

(7) Expenditure incurred by the transferee in making a payment to the transferor in respect of the assignment, grant or transfer mentioned in subsection (1)(b) is to be ignored for the purposes of section 357BME.

(8) In this section—

"trade" includes part of a trade, and

"relevant research and development" means research and development which relates to the relevant qualifying IP right.

(9) For the purposes of this section research and development "relates" to the relevant qualifying IP right if—

(a) it creates, or contributes to the creation of the invention,

(b) it is undertaken for the purpose of developing the invention,

(c) it is undertaken for the purpose of developing ways in which the invention may be used or applied, or

(d) it is undertaken for the purpose of developing any item or process incorporating the invention.""

Amendment 115, in clause 60, page 116, line 9, for "357A" substitute "357A(1)".—*(Mr Gauke.)*

Clause 60, as amended, ordered to stand part of the Bill.

Schedule 9

PROFITS FROM THE EXPLOITATION OF PATENTS ETC: CONSEQUENTIAL

Amendments made: 116, in schedule 9, page 330, line 30, at end insert—

"1A In section 357B (meaning of "qualifying company"), in subsection (3)(b)(ii), for "section 357A" substitute "section 357A(1)"."

Amendment 117, in schedule 9, page 331, line 20, at end insert—

"( ) In subsection (6), in paragraph (a)(ii) of the definition of "relevant accounting period", for "section 357A" substitute "section 357A(1)"."

Amendment 118, in schedule 9, page 331, line 24, leave out paragraph 9 and insert—

"9 (1) Section 357CL (companies eligible to elect for small claims treatment) is amended as follows.

(2) In subsection (1) for "elect" substitute "make an election under this section".

(3) In subsection (6) for "section 357A" substitute "section 357A(1)"."

Amendment 119, in schedule 9, page 332, line 16, at end insert—

"13A In section 357EB (allocation of set-off amount within a group) in subsection (3)(a) for "section 357A" substitute "section 357A(1)".

13B In section 357ED (company ceasing to carry on trade etc) in subsection (2)(c) for "section 357A" substitute "section 357A(1)"."

Amendment 120, in schedule 9, page 332, line 18, at end insert—

"14A In section 357FB (tax advantage schemes) in subsection (4)(b) for "section 357A" substitute "section 357A(1)".

14B (1) Section 357G (making an election under section 357A) is amended as follows.

(2) In the heading, for "section 357A" substitute "section 357A(1) or (11)(b)".

(3) In subsection (1) for "section 357A" substitute "section 357A(1) or (11)(b)".

14C (1) Section 357GA (revocation of election made under section 357A) is amended as follows.

(2) In the heading, for "section 357A" substitute "section 357A(1)".

(3) In subsection (1) for "section 357A" substitute "section 357A(1)".

(4) In subsection (5) for "section 357A" substitute "section 357A(1)"."

Amendment 121, in schedule 9, page 332, line 28, at end insert—

"16A In section 357GE (other interpretation), in subsection (1), at the appropriate place insert—

"payment" includes payment in money's worth,"."— *(Mr Gauke.)*

Schedule 9, as amended, agreed to.

Clause 61

POWER TO MAKE REGULATIONS ABOUT THE TAXATION OF SECURITISATION COMPANIES

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

Rebecca Long Bailey: I want to say a few words about the clause; although it might not seem exciting at first glance, it really is, so listen carefully to what I am about to say.

Three principal themes underpin the Labour party's approach to the provisions in clauses 61 and 64, which we will come to later—in particular, those relating to the taxation of financial products. First, we need to ensure that, when the UK leaves the EU, its arrangements for regulating taxation and financial activity serve the country best and protect it from abusive practices such as tax avoidance and financial crime. Those arrangements must demonstrate the highest levels of transparency and probity.

Secondly, we need to ensure that the infrastructure supporting the UK economy accords with international standards on taxation and regulation, including the relevant OECD and International Accounting Standards Board models, which are applicable to this Bill. Finally, we need to secure Britain's place in the world by ensuring that it maintains the highest international standards.

The Bill's proposals on the taxation of financial instruments may appear on the surface to be merely technical, but they raise a number of significant questions about the organisation of our economy and infrastructure in the near future. Clause 61 appears to be a simple extension of the corporation tax treatment of securitisation companies to the taxes Acts generally. However, in 2008 the non-existent regulation of securitisation structures amplified a medium-sized storm in the US real estate market, and it became a fully-fledged banking crisis. I would like to ask the Minister how closely HMRC and the Treasury have considered the risks that the provision will be used for tax avoidance purposes.

Experience suggests that, if we alter the basis on which tax is levied, financial institutions will attempt to create derivative products that generate losses for tax purposes on, before and after the transition between the two tax codes, as we saw in the case of Inland Revenue Commissioners *v.* Scottish Provident Institution 2003 and many other cases in Hudson's "The Law on Financial Derivatives".

Just in the reported cases, there are several examples of financial institutions using slippery derivative products, for want of a better phrase, to avoid tax liability, such as Prudential plc *v.* Revenue and Customs Commissioners

2008. In that case, Chancellor Morritt held that banks should not be entitled to dictate the tax consequences of their transactions by attributing particular descriptions to them. That sort of tax avoidance, using changes in the tax treatment of products, has been criticised by Professor Alastair Hudson as

"a veritable industry in off-the-peg tax avoidance schemes"

in his book "The Law on Financial Derivatives". Has the Minister considered the misdescriptions that might be possible under this provision?

To return to the particulars of clause 61, securitisation structures operate by transferring assets—whether subprime mortgages, credit card receivables or similar cash flows—into off balance sheet special purpose vehicles. Ordinarily, the profits, or cash flows, received from those assets pass through the special purpose vehicle to the investors who have acquired bonds in the special purpose vehicle. Usually, the residual amounts—the focus of clause 61—that are left in the special purpose vehicle are small, compared with the sums paid to the investors. However, as with all such artificial financial structures, it is possible to manipulate those amounts.

If the residual amounts held by special purpose vehicles are to be saved from withholding tax, as clause 61 proposes, and are to be treated in a different manner for tax purposes—although the provision does not make plain exactly what the different tax treatment will be—that makes it possible for the payment flows through a special purpose vehicle to be raised artificially so that larger sums could benefit from this different tax treatment.

Will the Minister confirm what is stopping an unscrupulous financial institution involved in the off-the-peg industry of tax avoidance derivatives from passing large sums—otherwise subject to withholding tax as payments of interest, for example—through special purpose vehicles? Have the Government considered in detail how such cash flows should be treated to prevent artificial or abusive tax avoidance?

Furthermore, securitisation products, in the form of collateralised debt obligations, use complex derivatives as part of their structure—namely, credit default swaps. The purpose of credit default swaps has always been to permit two things: first, speculation on the creditworthiness of companies and Governments issuing bonds; and secondly, a form of artificial insurance. A feature of credit default swaps and all other credit derivatives is that they are flexible tools—so flexible, in fact, that they are ideal for manipulating tax statutes for tax avoidance purposes.

Professor Alastair Hudson has described the inherent flexibility of financial derivatives in his book "The Law on Financial Derivatives", which I recommend to the Minister for his summer holidays. Professor Hudson states that

"different legal structures and different pricing structures can generate different commercial and structural results out of substantially similar subject matter".

As he shows, it is possible for options contracts to be reorganised as swaps, and vice versa, so the possibilities for tax avoidance are endless. Consequently, it would be simple for financial institutions to repackage their payment obligations to achieve whatever characteristics are most helpful for tax purposes. I fear that clause 61 is really only the tip of the iceberg. There is a serious general point behind the specificity of my concerns about the clause.

11 am

As we debate the Bill, the country finds itself in new territory. In theory, without the strictures of EU legislation, it will be open to us to create our own regulations to govern derivatives as well as the rest of the financial markets. There are many critics of the way in which the EU has chosen to regulate derivatives for the first time. For example, the use of private businesses as central clearing counterparties and trade repositories, which gather information about transactions that have been conducted, has created a new set of risks concerned with the solvency and performance of those private businesses. What if they go insolvent themselves during a future financial crisis? As private businesses, they will necessarily invest their own money, and it is perfectly possible that in the midst of a crisis they will fail to liquidate their investments in time to meet their obligations to their members. In such a situation, it will be the taxpayer—again—who will have to bail out the markets.

Moves are being made in the US Congress to dismantle many of the Dodd-Frank Act protections surrounding derivatives. The UK finds itself at a crossroads. We either ensure that our financial markets are properly regulated, for the protection of the financial institutions themselves as well as the country at large, or we run the risk of the City of London—alongside the first-class business currently conducted there—becoming the drain through which the world launders its dirty transactions.

Although clause 61 appears to be mainly technical, it conceals some important issues. In that spirit, I ask what work the Treasury and HMRC have done in proposing this change. The proper regulation of securitisation products and all derivatives will be an important issue in the establishment of the new British economy. In a paper published on 16 March 2016, HMRC makes explicit reference to the international accounting standards that were created in 2005 in relation to securitisation companies and suggests that this change in the taxation of securitisation

"is not expected to have any significant macroeconomic impacts."

Those accounting standards were created by the International Accounting Standards Board after careful consultation with experts around the world, but all those minds together failed to anticipate the financial crisis that we experienced in 2008. That is a clear lesson for us all about the unintended consequences that can flow from too little care being expended on such reforms. I hope that the Minister can alleviate the concerns that I have raised in relation to clause 61.

The Chair: It may help all Committee members if I point out that if you want to take part in the debate—and everyone is encouraged to take part in the debate—it is usually a good idea to signify that by some means: a nod, a smile or even, more obviously, by rising to your feet. Otherwise, I am as much in the dark as everyone else.

Mr Gauke: Clause 61 will make a simple technical change to widen the scope of the power to make regulations about the taxation of securitisation companies included in the Corporation Tax Act 2010. It will enable the Government to make changes in regulations to remove uncertainty over the tax treatment of what are referred to as residual payments in the securitisation sector. That

[Mr Gauke]

uncertainty generates a large number of requests to HMRC for clearances, which creates an administrative burden on both businesses and HMRC. Making the tax position clear will improve the customer experience. It has been welcomed by the securitisation sector and will improve the UK's competitiveness as a financial centre.

Securitisation companies are a particular type of financial entity in which financial assets such as loans are transferred to a special purpose vehicle as security for debt issued to investors in the capital markets. Securitisation is an important way of getting more credit or liquidity flowing into the economy and of keeping down the costs of UK businesses' borrowing and finance. The securitisation regime has worked well since its introduction, but the current rules have been in place since 2006. They need updating, to reflect recent changes to accounting standards and market developments.

One area of uncertainty that has grown as the securitisation sector has developed over recent years involves residual payments. Residual payments arise because securitisation companies typically contain more financial assets than are likely to be required in order to repay investors, meet transactions costs and retain a small profit. That excess protects against possible poor performance of the assets and allows the securitisation company to obtain an attractive credit rating. The uncertainty that arises is that residual payments may, in limited circumstances, be treated as annual payments for tax purposes and therefore be subject to withholding tax under the Income Tax Act 2007. Whether or not residual payments are treated as annual payments will depend on the facts of each case.

Uncertainty over the withholding tax rules affects the ability of law firms to issue a legal opinion on which ratings agencies can base the credit rating of the securitisation. That has a negative impact on the competitiveness of the UK securitisation sector. Currently, the uncertainty is addressed by companies writing to HMRC to seek clearance that residual payments will not be annual payments and so can be paid without withholding tax. That is an administrative burden for businesses. We would like to clarify the position by removing the potential withholding obligation in regulations, but the existing power is not wide enough to do so.

The changes made by the clause will amend the existing power to make regulations concerning the application of the Corporation Tax Acts to securitisation companies. The clause will extend the power to cover the wider taxes Acts, including the income tax Acts. That will permit changes to be made in regulations to ensure that the requirement to deduct income tax from annual payments will, as intended, not apply to residual payments made by securitisation companies. It will have a negligible cost to the Exchequer. Updated regulations under the amended power will be developed in consultation with interested parties.

The hon. Member for Salford and Eccles raised the role of securitisation in the financial crisis, which we could have spent plenty of time debating. However, while there were significant problems and faults in the US securitisation market, the UK and EU securitisation markets remained relatively robust. The global regulatory framework for securitisation has been completely overhauled since the crisis, including through increased capital requirements, reform of the oversight of credit ratings agencies and improved transparency rules.

The clause will not mean that securitisation companies pay less tax or face less scrutiny from HMRC. There is no statutory definition determining whether a payment is an annual payment. That must be decided based on characteristics established in case law. HMRC's view is that the overwhelming majority of residual payments will never be annual payments. The change will clarify the position by placing the tax treatment on a statutory footing, removing uncertainty for taxpayers. There is no policy change here.

In terms of what is to stop large sums from being artificially passed through these vehicles, the notes have to be issued wholly or mainly to external investors. The SPVs are conduits and do not retain the profits. On how we treat such cash flows to prevent avoidance, under the payment rules an SPV is taxed on a small retained profit that has to be paid out to investors within 18 months.

This simple change to primary legislation has been welcomed by the industry. It will allow changes to be made in regulations to make the tax rules applying to securitisation companies work as intended. It will also make it easier for UK businesses to raise finance through securitisations, making those businesses and the UK securitisation sector more competitive. It will remove uncertainty over the appropriate tax treatment and need for businesses to consult HMRC on this issue before entering into securitisation transactions and it will ensure that the tax treatment of residual payments will be treated consistently. I therefore hope that the clause will stand part of the Bill.

Question put and agreed to.

Clause 61 accordingly ordered to stand part of the Bill.

Clause 62

Hybrid and other mismatches

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

The Chair: With this it will be convenient to discuss that schedule 10 be the Tenth schedule to the Bill.

Rebecca Long Bailey: The same general points that I made about clause 61 broadly apply to this clause. The United Kingdom finds itself occupying a new place in the world and the provisions in the clause relate to the difficult business of double tax treaties. Such treaties currently need to be negotiated on a bilateral basis with countries that are outside large trading blocs such as the EU. They are therefore a model for the sort of issues that will be vital for the UK outside the EU.

There are model double tax treaties created by the OECD, which will guide our work. A future Labour Government would be outward looking in forging alliances of the sort possible under the OECD umbrella to create viable tax regulation and financial regulation internationally. However, there are some contexts in which the provisions in schedule 10, which the clause introduces, appear to be a little vague. For example, proposed new section 259BD(8) prevents a company from being "under taxed", by identifying the highest rate at which tax is charged and asking whether that is lower than the company's full marginal rate of tax should have been.

That is to be done by taking into account, on a "just and reasonable basis", any credit for underlying tax. The reference to just and reasonable appears somewhat vague when contrasted with, for example, provisions governing international accounting standards in earlier clauses. As a survivor of the legal world, will the Minister confirm what "just and reasonable" is intended to mean and how HMRC will use that broad measuring stick in practice? Does he think that is a sufficiently clear mechanism for identifying whether sufficient tax has been paid, or do the Government simply seek to grant HMRC as much slack as they can?

Mr Gauke: Clause 62 and schedule 10 make changes to tackle multinationals that avoid UK corporation tax through cross-border business structures known as hybrid mismatch arrangements. We are building on the new rules announced at autumn statement 2014 and extending them, not least so that they also cover overseas branches, leading the way on implementing international best practice in this area.

The changes will neutralise the tax effect of hybrid mismatch arrangements and effect the recommendations of action 2 of the G20-OECD base erosion and profit-shifting project. In addition, they will neutralise the tax effect of hybrid mismatch arrangements involving permanent establishments. That means that the measure will tackle aggressive tax planning where, within a multinational group, either one party gets a tax deduction for a payment while the other party does not have a taxable receipt or there is more than one tax deduction for the same expense. The aim is to eliminate the unfair tax advantages that arise from the use of hybrid entities, hybrid instruments, dual resident companies and permanent establishments. That will encourage businesses to adopt less complicated cross-border investment structures.

In 2013 the OECD and the G20 countries adopted a 15-point action plan to address base erosion and profit shifting. BEPS refers to tax-planning strategies that exploit gaps and mismatches in the tax rules of different countries to make profits disappear for tax purposes or to shift profits to locations where there is little or no real activity but where the tax rates are low, resulting in little or no overall corporate tax being paid. The BEPS action plan is aimed at ensuring that profits are taxed where the economic activities generating the profits are performed, and where value is created.

11.15 am

Clause 62 and schedule 10 implement the recommendations on neutralising the effects of hybrid mismatch arrangements. The rules are designed to ensure that multinationals can no longer derive tax benefit from mismatch arrangements using hybrid entities, hybrid financial instruments or dual resident companies.

Clause 62 and schedule 10 also include rules to tackle hybrid mismatch arrangements that involve permanent establishments. Permanent establishments of companies are often used as an alternative to hybrid entities in tax planning arrangements, as they provide for similar mismatch opportunities. The clause covers such arrangements to ensure that groups cannot simply sidestep the OECD recommendations by using permanent establishments. Failing to tackle such permanent establishment arrangements would present an obvious opportunity for further avoidance, which would undermine the measure's policy objective.

The Government announced their intention to introduce domestic legislation in October 2014. They consulted at autumn statement 2014 and later published draft legislation for technical consultation in December 2015. As a result, clause 62 and schedule 10 have been informed by consideration of responses to the consultation, by further engagement with interested parties, and by publication of the final OECD report.

The changes made by clause 62 and schedule 10 will address hybrid mismatch arrangements by changing the tax treatment of either the payment or the receipt, depending on circumstances. The rules are designed to work whether both countries affected by a cross-border arrangement, or just one of them, have introduced the OECD rules. The changes will affect large multinational groups with UK parent or subsidiary companies that are involved in transactions that result in a mismatch in tax treatment in the UK, or between the UK and another jurisdiction. The rules will take effect from 1 January 2017. In taking the action, and particularly in providing for the rules to cover permanent establishments, the UK will not only fully implement the agreed OECD recommendations; it will go beyond them. That will bring in more than £900 million over the next five years.

The hon. Member for Salford and Eccles raised a point about the definition of the expression "just and reasonable". There is no definition; it takes account of the facts and circumstances of specific cases and does not give advantage to the tax Administration. It is a well used expression, which is understandably used in the circumstances in question.

The Government are stopping multinationals avoiding paying their fair share of UK tax through the use of cross-border business structures. We are building on the rules that we announced at autumn statement 2014 and extending them so that they also cover overseas branches, leading the way on implementing international best practice in the area.

Question put and agreed to.

Clause 62 accordingly ordered to stand part of the Bill.

Schedule 10 agreed to.

Clause 63

INSURANCE COMPANIES CARRYING ON LONG-TERM BUSINESS

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

Rebecca Long Bailey: I will be brief. The provision raises some seemingly technical questions on the taxation of loan relationships and derivatives—concepts that are closely linked in tax law. As with the other clauses, it requires deeper thought as the UK prepares to leave the EU. What precise changes, which HMRC has presumably observed in the financial markets, have prompted the reforms proposed in clause 63?

The role of insurance companies, particularly naive participants such as AIG before 2008, in derivatives markets must give us all pause for thought when considering how to regulate and tax them in the future. Those

[Rebecca Long Bailey]

enormous insurance companies are involved in vital financial services for our citizens as well as extraordinarily complex financial instruments, such as credit default swaps. We must therefore be concerned that the reforms to the treatment of insurance companies are considered necessary. Will the Minister confirm what work the Treasury has done on assessing the future treatment of derivatives and similar markets and their impact on the UK economy? It is important for the future health of the UK economy that careful analysis of those markets is conducted as we prepare to leave the EU.

Mr Gauke: Clause 63 makes changes to ensure that corporation tax rules applying to insurance companies carrying on long-term business produce the appropriate policy results. A new regime for the taxation of life insurance companies was introduced in the Finance Act 2012 and was widely welcomed. However, putting that into practice has uncovered some specific issues that must be resolved for the regime to operate smoothly and effectively. HMRC has worked with industry to identify those issues, which relate to three main areas: intangible fixed assets, deemed income and trading losses.

Clause 63 will make minor technical changes to that legislation to ensure that it operates as intended. The cost to the Exchequer is negligible. For intangible fixed assets, clause 63 will allow debits to be set against the income for the accounting period in which they are incurred. That will bring the rules into line with those for companies that are not life insurers. For deemed income, clause 63 will prevent unused interest expenses from being set against the minimum profits charge in any circumstances. That will mean that any such charge is always fully taxed. For trading losses, clause 63 will mean that their use is no longer restricted to a company's net position on its derivative contracts in the same period, which will bring stability into that calculation. The changes are relatively minor in nature and will have a small impact on insurers' profits. However, they are important as they will ensure that the legislation delivers the intended policy objectives.

As I said, the Finance Act 2012 introduced a fundamental rewrite of life insurance company taxation. Such major reforms are always likely to necessitate some minor adjustments when put into practice and HMRC has worked with the industry to identify a handful of issues where the legislation does not work as intended. The changes will simply ensure the legislation operates as initially intended, which is why we are making them. Of course, all these matters are kept under review. Again, the hon. Lady raises the point about EU membership and so on. I am not sure I have much to add to what I previously said on that matter. I hope that the clause stands part of the Bill.

Question put and agreed to.

Clause 63 accordingly ordered to stand part of the Bill.

Ordered, That further consideration be now adjourned.—*(Mel Stride.)*

11.23 am

Adjourned till this day at Two o'clock.