PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT
GENERAL COMMITTEES

Public Bill Committee

FINANCE (NO. 3) BILL

(Except clauses 5, 6, 8, 9 and 10; clause 15 and schedule 3; clause 16 and schedule 4; clause 19; clause 20; clause 22 and schedule 7; clause 23 and schedule 8; clause 38 and schedule 15; clauses 39 and 40; clauses 41 and 42; clauses 46 and 47; clauses 61 and 62 and schedule 18; clauses 68 to 78; clause 83; clause 89; clause 90; any new clauses or new schedules relating to tax thresholds or reliefs, the subject matter of any of clauses 68 to 78, 89 and 90, gaming duty or remote gaming duty, or tax avoidance or evasion)

Fourth Sitting

Thursday 29 November 2018

(Afternoon)

CONTENTS

Clause 18 agreed to.
Schedule 6 agreed to.
Clauses 21 and 24 to 26 agreed to.
Schedule 9 agreed to.
Clause 27 agreed to.
Schedule 10 agreed to.
Clause 28 agreed to.
Schedule 11 agreed to.
Clauses 29 to 31 agreed to.
Schedule 12 agreed to.
Adjourned till Tuesday 4 December at twenty-five minutes past Nine o'clock.
Written evidence reported to the House.

PBC (Bill 282) 2017 - 2019

No proofs can be supplied. Corrections that Members suggest for the final version of the report should be clearly marked in a copy of the report—not telephoned—and must be received in the Editor's Room, House of Commons,

not later than

Monday 3 December 2018

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The Committee consisted of the following Members:

Chairs: Ms Nadine Dorries, †Mr George Howarth

† Afolami, Bim *(Hitchin and Harpenden)* (Con)
† Badenoch, Mrs Kemi *(Saffron Walden)* (Con)
† Black, Mhairi *(Paisley and Renfrewshire South)* (SNP)
† Blackman, Kirsty *(Aberdeen North)* (SNP)
Charalambous, Bambos *(Enfield, Southgate)* (Lab)
† Dodds, Anneliese *(Oxford East)* (Lab/Co-op)
† Dowd, Peter *(Bootle)* (Lab)
† Ford, Vicky *(Chelmsford)* (Con)
† Jenrick, Robert *(Exchequer Secretary to the Treasury)*
† Keegan, Gillian *(Chichester)* (Con)
† Lamont, John *(Berwickshire, Roxburgh and Selkirk)* (Con)
† Lewis, Clive *(Norwich South)* (Lab)
† Reynolds, Jonathan *(Stalybridge and Hyde)* (Lab/Co-op)
† Smith, Jeff *(Manchester, Withington)* (Lab)
† Sobel, Alex *(Leeds North West)* (Lab/Co-op)
† Stride, Mel *(Financial Secretary to the Treasury)*
† Syms, Sir Robert *(Poole)* (Con)
Whately, Helen *(Faversham and Mid Kent)* (Con)
† Whittaker, Craig *(Lord Commissioner of Her Majesty's Treasury)*

Colin Lee, Gail Poulton, Joanna Dodd, *Committee Clerks*

† attended the Committee

Public Bill Committee

Thursday 29 November 2018

(Afternoon)

[Mr George Howarth *in the Chair*]

Finance (No. 3) Bill

(Except clauses 5, 6, 8, 9 and 10; clause 15 and schedule 3; clause 16 and schedule 4; clause 19; clause 20; clause 22 and schedule 7; clause 23 and schedule 8; clause 38 and schedule 15; clauses 39 and 40; clauses 41 and 42; clauses 46 and 47; clauses 61 and 62 and schedule 18; clauses 68 to 78; clause 83; clause 89; clause 90; any new clauses or new schedules relating to tax thresholds or reliefs, the subject matter of any of clauses 68 to 78, 89 and 90, gaming duty or remote gaming duty, or tax avoidance or evasion)

Clause 18

Diverted profits tax

2 pm

Question (this day) again proposed, That the clause stand part of the Bill.

The Chair: I remind the Committee that with this we are discussing the following:

Amendment 46, in schedule 6, page 220, line 2, leave out paragraph 11.

This amendment removes the proposed extension of the review period to 15 months.

Amendment 37, in schedule 6, page 220, line 26, at end insert—

"13 The Chancellor of the Exchequer must review the expected change to payments of diverted profits tax and any associated changes to overall payments made to the Commissioners arising from the provisions of this Schedule, and lay a report of that review before the House of Commons within 6 months of the passing of this Act."

This amendment would require the Chancellor of the Exchequer to review the effect on public finances of the diverted profits tax provisions in this Bill.

Amendment 40, in schedule 6, page 220, line 26, at end insert—

"13 The Chancellor of the Exchequer must review the expected revenue effects of the changes made to diverted profits tax in this Schedule and lay a report of that review before the House of Commons within six months of the passing of this Act."

This amendment would require the Chancellor of the Exchequer to review the effect on public finances on the provisions in Schedule 6.

Amendment 41, in schedule 6, page 220, line 26, at end insert—

"13 The Chancellor of the Exchequer must review diverted profits tax against its policy objectives and lay a report of that review before the House of Commons within six months of the passing of this Act."

This amendment would require the Chancellor of the Exchequer to review DPT against its policy objectives.

Amendment 42, in schedule 6, page 220, line 26, at end insert—

"13 The Chancellor of the Exchequer must commission a review comparing diverted profits tax against a Digital Services Tax and lay a report of that review before the House of Commons within six months of the passing of this Act."

This amendment would require the Chancellor of the Exchequer to review DPT against the Government's proposed Digital Services tax.

Amendment 43, in schedule 6, page 220, line 26, at end insert—

"13 (1) The Chancellor of the Exchequer must commission a review on the matter specified in subsection (2).

(2) That matter is the effects on the public finances of the the provisions in this Schedule coming into effect in the tax year 2019-20 compared to previous or subsequent tax years.

(3) The Chancellor of the Exchequer must lay a report of the review under subsection (1) before the House of Commons within six months of the passing of this Act."

This amendment would require the Chancellor of the Exchequer to review the impact of introducing this measure in 2019-20.

Amendment 45, in schedule 6, page 220, line 26, at end insert—

"13 After section 105 insert—

105A Public register of diverted profits tax payments

(1) The Commissioners must provide information to the Treasury listing those companies that have made payments pursuant to a charge of diverted profits tax, and the amounts of those payments.

(2) The Treasury shall publish a register of companies paying diverted profits tax based on the information provided by the Commissioners under subsection (1), and shall make that register available to the general public."

This amendment requires the publication of a public register of those companies that pay diverted profits tax.

That schedule 6 be the Sixth schedule to the Bill.

Kirsty Blackman (Aberdeen North) (SNP) *rose—*

The Chair: We have all waited through our lunch break for this with eager anticipation.

Kirsty Blackman: And a very enjoyable lunch break it was—not that the Committee is not enjoyable, too. *[Laughter.]* I dug myself out of that one. I want to speak both to Labour's amendments and to our own, but I will not speak for long.

I find Labour's amendment 46, which would remove the proposed extension of the review period to 15 months, particularly interesting because I agree with Labour Front-Bench Members that the Government have not adequately explained the effect of changing the review period. More could have been done to provide the Committee with information about the reason for the extension and the decision-making process behind it. On that basis, I would be happy to support the Labour party, but that is not to say that the Government could not come back in future years with reasonable information to justify the extension and set out the impact on the tax take.

Labour's amendment 43 would require the Chancellor of the Exchequer to review the impact of introducing the diverted profits tax in 2019-20—something else that the Government have not adequately explained. We would like a little more information on matters such as the difficulties for organisations resulting from the tax's

implementation and its impact on the Exchequer, because we need to balance those things when we make decisions on tax changes.

The Scottish National party's amendment 37, which would require the Chancellor to review the effect on public finances of the diverted profits tax provisions in the Bill, is broader than some of the specific requests that have been made for individual pieces of information. I understand the Minister's point that Her Majesty's Revenue and Customs regularly provides information to the general public about the diverted profits tax, but I think we could have been given a little more information about the proposals' expected effect on revenue and on the tax gap.

Finally, I know that explanatory notes do not form part of a Bill, but the "Background note" sections are usually quite useful. However, I did not find the background note on clause 18 useful in the slightest, because it does not give a huge amount of information about the rationale behind the Government's decision or behind the individual changes being made to the diverted profits tax. It simply says:

"This measure supports that aim"—

the aim behind the diverted profits tax—

"through amendments to close tax planning opportunities."

If it had given a little more information about what those amendments are and what they mean, the Minister would have avoided facing quite so many questions from the Committee.

The Chair: We also eagerly await the words of Sir Robert Syms.

Sir Robert Syms (Poole) (Con): I would have intervened, Mr Howarth, but you have provoked me into making a brief speech instead.

Corporate tax structures are very complex. Even things like the movement of exchange rates or where products are produced can make a substantial difference to a company's profit and loss account. As I understand it, the diverted profits tax is a backstop—I use the word lightly—in the tax system. The reality is that the Government are trying to protect corporation tax revenue.

Periodically, HMRC will challenge corporation tax computations to see whether companies are paying the right amount of tax. DPT gives the Revenue a little more ammunition to get answers out of those companies and to ensure that the tax paid is correct. I suppose that HMRC would randomly pick several companies, or more, and simply challenge some of the computations. Where they found that an accurate tax statement had not been put in, perhaps they would go back a number of months and issue a notice for payment.

As the Minister pointed out, the companies could still elect to pay via the corporation tax structure rather than this tax. I do not think that having a report on this specific tax would draw very much information, because it will vary widely. There will be some years where quite a lot of back tax will be caught and captured, and a back payment might be picked up from a big company. In other years, all the tax computations will be fairly accurate and it will not pick up very much. My guess is that, instead of a straight line going up, as there is for most taxes, such as VAT, there will be variation each year depending on which companies are challenged, and whether HMRC hits the jackpot or finds that the companies' accountants know what they are doing.

When looking at this backstop, we really have to look at overall corporation tax revenue, which, notwithstanding the fact that the rate has been cut, has actually gone up. I therefore hope that the Government reject these reports—the Government have been far too reasonable in this Committee anyway—stick to their guns, and reject whatever the Opposition want.

The Financial Secretary to the Treasury (Mel Stride): I will be brief, as I am conscious that the Committee is moving fairly slowly through the clauses, and we have quite a lot of the Bill still to cover.

The hon. Member for Oxford East mentioned the diverted profits tax and the digital services tax. Earlier on in her speech, in a different context, she used the expression "comparing apples with pears". I think that is what we are doing here, and that lies at the heart of the objection to her amendment.

Anneliese Dodds (Oxford East) (Lab/Co-op): The Minister knows that I have a lot of respect for him. However, that was exactly my point: the two taxes are based on a fundamentally different view of what should be taxed. Obviously, a digital services tax would be revenue based, whereas DPT is still profit based, and based on the arm's length principle. Surely one should therefore compare them in terms of their efficacy at generating tax revenue, preventing avoidance, and so on. The fact that they are different does not mean that it is not legitimate to compare them.

Mel Stride: I understand what the hon. Lady says, but the expression "preventing avoidance", which she has just used, lies at the heart of the meaningful distinction. DPT is about avoidance, as eloquently expressed by my hon. Friend the Member for Poole, whereas the digital services tax is not about avoidance at all; it is about reflecting the fact that the international tax regime is no longer fit for purpose when it comes to taxing certain types of digital businesses—those that operate through digital platforms, and that have a relationship with UK users and generate value as a consequence. She mentioned Google specifically, but it covers search engines in general, certain online marketplaces and social media platforms.

The two taxes are so distinct. It is important to place on the record that the digital services tax is not an anti-avoidance measure; it is about redefining the way in which those businesses pay their fair share of tax.

Kirsty Blackman: To probe further the point made by the hon. Member for Oxford East, does the Minister not agree that it would be valuable for the Committee to consider the two different types of taxation, and their efficacy, so that in future when decisions are made on tax matters we can work out which would be the best type of tax measure in any given situation?

Mel Stride: It is important to review or consider all taxes in relation to other taxes as a matter of course, because they all have their own positive aspects, distortionary effects, negative aspects, impacts on the economy that might not be desirable, and so forth. It is important that we do that for all taxes. I say to the hon. Lady that, in the case of the digital services tax, we are now consulting on the detail of how that might operate should we introduce it in 2020, in the event that there is

[Mel Stride]

not a multilateral movement across the OECD or the European Union that allows us to work in conjunction with other tax jurisdictions. In the case of the specific tax that we are considering in Committee, there will be ample opportunity to look at it in the kind of detail that I know she will be keen on.

The hon. Member for Oxford East raised the issue of the split, as I understood it, between the impact of DPT as directly revenue raising through the additional corporation tax that is paid, and the deterrent effect that protects revenues that otherwise would have been avoided. We publish annual statistics that show how much tax DPT raises directly and how much it raises indirectly through corporation tax. This year, we published a detailed note setting out the methodology that was used to calculate the revenue raised by DPT, and I am happy to provide the hon. Lady with either that information or a signpost to where it can be found.

The hon. Lady raised the specific issue of the three-month extension that we have been considering in Committee. She made the point well: rather than extending the period by three months, why do we not stick to 12 months and expect the corporation in question to speed up their process? I think we would still be left with the problem that there would have to be a moment in time when that company could still provide information—HMRC would be required to take it into account—which might be of a very complex nature. It would be very difficult for HMRC to make an immediate and reasonable judgment at the last minute. I think that is what drives the importance of separating the time available to the corporation in those circumstances from the additional time that is available solely to HMRC to conduct its final review without additional information suddenly appearing at extremely short notice. I should also point out that the 12-month process is already an accelerated process, and typically we are—in circumstances where the additional three-month time period becomes pertinent—looking at very complex situations, which take time to consider fully.

On the basis of the extract that the hon. Member for Aberdeen North presented to the Committee, it seems to me that more information could have been given in the explanatory notes to make it absolutely clear what it refers to. I will have a closer look at that outside the Committee.

Anneliese Dodds: I am grateful to the Minister for his clarifications. I would like to accept his kind offer to share with me and the Committee—I am sure other Members will be interested as well—the information that he referred to, which sets out the different components of DPT. I think that would be enormously helpful.

The hon. Member for Poole seemed to suggest that there would be two reasons for fluctuation across years. I think he used the word "random" to describe HMRC's choice of which companies to investigate—they could be large or small. I would hope that it would not be a random process, although I am not suggesting he was intimating that. I would hope that it was based on intelligence and that HMRC—I would like it to undertake more of this than it does at the moment—used some of the data sources available to it to drive the process of determining which companies to look at. Hopefully that would not be a source of too much variation.

The hon. Gentleman also suggested that there might be variation because it would be, in some way, a reflection of the compliance-mindedness of tax practitioners in different corporations at any one point. Surely that should improve over time, rather than fluctuate. There may be other reasons for the variation, but I feel we still need to have a clear understanding of it.

Sir Robert Syms: My central point is that if HMRC challenges a corporation tax computation, it does not have to do it every single year with the same company, because essentially it will come to an arrangement about what is acceptable—for at least a period of years. Then it can go and look for the next company. I see it as a rolling process in which essentially there is a dialogue between HMRC and the accountants of the companies. Therefore, everybody knows quite where they stand, and perhaps the companies will benefit as well.

2.15 pm

Anneliese Dodds: I am grateful for that clarification of the hon. Gentleman's comments. I suppose on that basis one would assume that the take would go down, if there was truly a deterrent action. It is not clear to me that that has occurred, but it would be interesting to have the analysis and review, so that we could see whether it is so. That is what our amendments aim to do.

I took on board what the Minister said about the review period, but I am a little confused. As I understand it, the additional time provided for the review period in the Bill is not of a different character from the rest of the review period. It is not a question of the additional three months being just for HMRC to deliberate. It is also a period during which the company can provide additional information—so, potentially, they can now do that right up to the end of 15 rather than 12 months. Therefore it is unclear to me that HMRC will necessarily be helped—unless I am missing something, which I may well be.

Mel Stride: To clarify, briefly, it is not as the hon. Lady views it: the additional three months would be solely for HMRC to carry out its deliberations, albeit that up to the 11th hour within the 12-month period further information could be provided by the company.

Anneliese Dodds: I am grateful to the Minister for clarifying that. It was not completely clear to me from the material provided to us. I underline the points that have been made by the SNP in that regard: it would have helped us to understand the impact of some of the measures if the explanatory notes had included a bit more of the thinking behind them.

In view of what the Minister has said, we are willing to drop some of our amendments. However, we shall want to vote on amendment 40, which is quite similar to the SNP's amendment 37, and amendments 43 and 46.

Question put and agreed to.

Clause 18 accordingly ordered to stand part of the Bill.

Schedule 6

DIVERTED PROFITS TAX

Amendment proposed: 46, in schedule 6, page 220, line 2, leave out paragraph 11.—*(Anneliese Dodds.)*

This amendment removes the proposed extension of the review period to 15 months.

Question put, That the amendment be made.

The Committee divided: Ayes 8, Noes 9.

Division No. 13]

AYES

Black, Mhairi
Blackman, Kirsty
Dodds, Anneliese
Dowd, Peter
Lewis, Clive
Reynolds, Jonathan
Smith, Jeff
Sobel, Alex

NOES

Afolami, Bim
Badenoch, Mrs Kemi
Ford, Vicky
Jenrick, Robert
Keegan, Gillian
Lamont, John
Stride, rh Mel
Syms, Sir Robert
Whittaker, Craig

Question accordingly negatived.

Amendment proposed: 40, in schedule 6, page 220, line 26, at end insert—

"13 The Chancellor of the Exchequer must review the expected revenue effects of the changes made to diverted profits tax in this Schedule and lay a report of that review before the House of Commons within six months of the passing of this Act."—*(Anneliese Dodds.)*

This amendment would require the Chancellor of the Exchequer to review the effect on public finances on the provisions in Schedule 6.

Question put, That the amendment be made.

The Committee divided: Ayes 8, Noes 9.

Division No. 14]

AYES

Black, Mhairi
Blackman, Kirsty
Dodds, Anneliese
Dowd, Peter
Lewis, Clive
Reynolds, Jonathan
Smith, Jeff
Sobel, Alex

NOES

Afolami, Bim
Badenoch, Mrs Kemi
Ford, Vicky
Jenrick, Robert
Keegan, Gillian
Lamont, John
Stride, rh Mel
Syms, Sir Robert
Whittaker, Craig

Question accordingly negatived.

Amendment proposed: 43, in schedule 6, page 220, line 26, at end insert—

"13 (1) The Chancellor of the Exchequer must commission a review on the matter specified in subsection (2).

(2) That matter is the effects on the public finances of the the provisions in this Schedule coming into effect in the tax year 2019-20 compared to previous or subsequent tax years.

(3) The Chancellor of the Exchequer must lay a report of the review under subsection (1) before the House of Commons within six months of the passing of this Act."—*(Anneliese Dodds.)*

This amendment would require the Chancellor of the Exchequer to review the impact of introducing this measure in 2019-20.

Question put, That the amendment be made.

The Committee divided: Ayes 8, Noes 9.

Division No. 15]

AYES

Black, Mhairi
Blackman, Kirsty
Dodds, Anneliese
Dowd, Peter
Lewis, Clive
Reynolds, Jonathan
Smith, Jeff
Sobel, Alex

NOES

Afolami, Bim
Badenoch, Mrs Kemi
Ford, Vicky
Jenrick, Robert
Keegan, Gillian
Lamont, John
Stride, rh Mel
Syms, Sir Robert
Whittaker, Craig

Question accordingly negatived.

Schedule 6 agreed to.

Clause 21

Permanent establishments: preparatory or auxiliary activities

Anneliese Dodds: I beg to move amendment 47, in clause 21, page 13, line 35, at end insert—

"(7) The Chancellor of the Exchequer must review the revenue effects of the preceding provisions of this section and lay a report of that review before the House of Commons within six months of the passing of this Act."

This amendment would require the Chancellor of the Exchequer to review the revenue effects of the changes made by Clause 21.

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

Amendment 48, in clause 21, page 13, line 35, at end insert—

"(7) The Chancellor of the Exchequer must, within 3 months of the passing of this Act, publish a list of additional non-UK resident companies that are classified as having permanent establishments as a result of restricting the application of section 1143 of the CTA 2010.

(8) The list in subsection (7) must be updated annually."

This amendment would require the Chancellor of the Exchequer to publish a list of all additional permanent establishments created as a result of the changes made by Clause 21 three months after the passing of the Act and annually thereafter.

Clause stand part.

Anneliese Dodds: The clause focuses on attempts to wriggle out of triggering permanent establishment status by maintaining that economic activity is preparatory or auxiliary. Currently, certain so-called preparatory or auxiliary activities are understandably exempt from being classified as indicating a permanent establishment. They tend to be of low value and include storing products for the company involved, purchasing goods for it and collecting information for it.

Action 7 in the OECD's BEPS—base erosion and profit shifting—process included a range of measures to tighten up in the OECD's model tax treaty section 5, including in this area. The model tax treaty includes a far-reaching anti-fragmentation rule to prevent activities in a jurisdiction from being intentionally, artificially fragmented between different companies in a group merely so that those activities will not trigger permanent establishment status because they can be classified as preparatory or auxiliary.

The OECD rules prevent the preparatory and auxiliary exemption from applying in situations where there is already a permanent establishment in the country, and where the overall activity carried out both by the company concerned and by companies that are closely related to it are not preparatory or auxiliary. In both cases, however,

[Anneliese Dodds]

the activities must constitute part of a so-called "cohesive business operation". In practice, the measure puts into UK law what the UK has already signed up to via its ratification of the OECD's multilateral instrument for the amendment and updating of tax treaties, which is now sequentially being applied to our existing tax treaties, as we have discussed on a number of occasions just along the Committee corridor.

We seek to amend the clause in a number of ways. First, amendment 48 requires the Chancellor to publish a list of all additional permanent establishments created by the clause, and to do so annually. There is a serious problem of accountability in our tax system. Those who have engaged in tax avoidance are not publicly held responsible. In response to the debate on Second Reading, it looks very clear what tax avoidance is and what it is not. It is behaviour that is legal, but although it may follow the letter of tax law, it does not follow its spirit.

Contrary to what was argued in the previous debate in the Chamber, individual savings accounts do not constitute tax avoidance because their creation was intended and promoted by legislators. On the contrary, artificial arrangements are tax avoidance, because policy makers, whether in the UK or elsewhere—such as for the Dutch and Irish sandwiches—did not indicate that they wished their tax law to be used by those schemes to exploit loopholes.

Relying purely on the spirit of the law or treaties, rather than their letter, leaves our system open to tax avoidance, which is one of the many reasons the Opposition support the introduction of a general anti-avoidance rule—not just anti-abuse. We have talked about that in this Committee. In any case, we must understand which firms profited from these forms of artificial fragmentation. Our amendment asks for that.

It is particularly important to have that analysis at a time when the US approach to corporate taxation and determining where permanent establishment lies is in flux. The corporate tax rate in the US is going down, but that problem is compounded by tightening up in a range of areas, including the adoption of many elements of the BEPS process relating to permanent establishments. It is important to assess the efficacy of measures put forward here in relation to what is occurring in the US, where claims have been made that the situation will lead to onshoring of activity. That remains to be seen, but it will be useful to have an analysis so that we can perform that assessment.

Amendment 47 would require a review of the revenue effect of clause 21. It is not possible to judge its likely efficacy without understanding the extent to which it will promote the correct payment of corporation tax. I note that some jurisdictions, such as Argentina, have included what appear to be more stringent requirements in their permanent establishment roles, going beyond the OECD requirements.

It is important that we properly understand the likely impact of the proposed rules. There has been a debate about this issue at OECD level for quite a long period—since about 2013. There are very different views about whether the OECD approach is sufficiently stringent. It is important to listen to some alternative views that were referenced when this particular action in the BEPS process was investigated, particularly from the BEPS monitoring group in 2015. That group is composed of a variety of experts looking at international tax law and a number of civil society organisations—I will not try to pronounce their names because some are in Spanish and I would get it humiliatingly wrong.

In response to a call for evidence in relation to changes in the OECD tax treaty chapter 5, the group maintained that although an anti-fragmentation rule was proposed by the OECD, it was

"only in relation to pre-sales related activities, such as storage, display or delivery",

as delivered by this clause. The group suggested that was problematic and did not go far enough because:

"These proposed changes would therefore not affect other types of structures which fragment functions such as manufacturing, purchasing, design, marketing and customer support."

It continued:

"Moreover, the current proposals would have limited application to services."

It felt that there was a particular problem for developing countries—I appreciate that we are not in that situation. It said that for the countries it works with often there was also a particular problem from "stripped-risk contract manufacturers". It argued that, as an alternative to the BEPS anti-fragmentation proposals,

"One way to deal with this would be for the Commentary to make clear that where decisions are made locally in a country by personnel of any group member or agent that affect the commercial risks borne by any group member, then that group member will be considered to maintain a 'place of management' within that country within the meaning of Paragraph 2 of Article 5."

That is quite a different approach from assessing whether fragmentation is occurring, and it would be helpful to understand why the Government believe their approach is sufficiently stringent in the light of critiques such as that one. That is another reason why I think our amendment is necessary.

2.30 pm

Mel Stride: The clause makes changes to ensure that foreign businesses operating in the UK cannot avoid creating a taxable presence by splitting up their activities between different locations and companies. A non-resident company is liable to UK corporation tax only if it has a permanent establishment here—I shall use the abbreviation PE for permanent establishment. A PE may be a fixed place of business, also referred to as a branch, or the activity of an agent. We are mostly concerned here with branches.

As the hon. Member for Oxford East has outlined, certain preparatory or auxiliary activities, which are normally low value, such as storing the company's own products, purchasing goods or collecting information for the non-resident company, are classed as exempt activities and do not create a permanent establishment. Some foreign businesses could artificially split their operations among different group companies or between different locations to take advantage of those exemptions and so avoid being liable to corporation tax.

To counter that, the OECD and G20 recommended modifying the definition of permanent establishment. The UK has adopted that change in its tax treaties, the bilateral tax arrangements that divide up taxing rights between countries, with which the hon. Lady and I are most familiar, having taken a series of pieces of secondary legislation through this House on those matters. It has

given effect to that change through the BEPS multilateral instrument, as she pointed out, which entered into force for the UK on 1 October 2018.

Clause 21 replicates that treaty change in UK domestic law to make the change to tax treaties effective. It is most likely to affect non-resident manufacturing and distribution businesses that might try to structure their UK operations in order to minimise their UK tax footprint. The measure sends a signal that the UK Government are determined to tackle tax avoidance by foreign multinationals.

Turning to the two amendments tabled by the Opposition, amendment 47 would require the Chancellor of the Exchequer to review the revenue effects of the changes made by this clause within six months of the Bill becoming law. I cannot support this amendment. Information on revenue effects will not be available six months after the passing of the Act, given that the first accounting periods likely to be affected are those ending on 31 March 2019, for which the filing date of company tax returns will be 31 March 2020.

The Government also cannot support amendment 48, which would require publication three months after the passing of the Act of a list of all additional PEs created as a result of this measure. HMRC would not know, as a company is not required to disclose, whether a declared PE has occurred as a result of this measure or for some other reason. The information would be available to HMRC only if it opened an inquiry into every non-resident company that newly declared a permanent establishment. That, as I hope the Committee would agree, is impractical. It would not be an appropriate use of inquiry powers and it would impose a significant burden on HMRC and the taxpayer for little revenue benefit. The Exchequer impact assessment has scored this measure as likely to have negligible yield. I therefore commend the clause to the Committee and invite Members to reject the amendments.

Anneliese Dodds: I am grateful to the Minister for his clarifications and comments. I think we would be willing to withdraw the amendment, but I note that he did not refer to the critique that I mentioned by the BEPS monitoring group on whether the definition of fragmentation coming within the OECD process was sufficient. I do not want to detain the Committee on that point any longer, but I ask him to bear that critique in mind as we go through any additional tax treaties; I am sure we will come to some in the future with developing countries, because arguably this is a significant problem for them. It can be difficult for them to apply even the conventions in the model tax treaty to capture economic activity within their boundaries when they need to build up their tax base. Of course, we give many of those countries development aid.

As I said, I am willing to withdraw the amendment, but I would be grateful if the Minister kept those points in mind. I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 21 ordered to stand part of the Bill.

Clause 24

Group relief etc: meaning of "UK related" company

Anneliese Dodds: I beg to move amendment 51, in clause 24, page 14, line 4, at end insert—

"(1A) At the end of section 134 of CTA 2010, insert—

'(2) The Chancellor of the Exchequer must review any change, attributable to the amendments made to this section by section 24 of the Finance Act 2019, to payments of corporation tax.

(3) A report of the review under subsection (2) must be laid before the House of Commons by 5 April 2020.'"

This amendment would require the Chancellor of the Exchequer to review the revenue effects of this Clause, as far as they relate to section 134 of the Corporation Tax Act 2010 and report on those changes by the end of the tax year 2019-20.

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

Amendment 52, in clause 24, page 14, line 4, at end insert—

"(1B) At the end of section 134 of CTA 2010, insert—

'(4) The Chancellor of the Exchequer must review the effects on the property market attributable to the amendments made to this section by section 24 of the Finance Act 2019.

(5) A report of the review under subsection (4) must be laid before the House of Commons by 5 April 2020.'"

This amendment would require the Chancellor of the Exchequer to review the effects of this Clause, as far as they relate to section 134 of the Corporation Tax Act 2010, on the property market and report on those changes by the end of the tax year 2019-20.

Amendment 53, in clause 24, page 14, line 7, at end insert—

"(2A) At the end of section 188CJ of CTA 2010, insert—

'(2) The Chancellor of the Exchequer must review any change, attributable to the amendments made to this section by section 24 of the Finance Act 2019, to payments of corporation tax.

(3) A report of the review under subsection (2) must be laid before the House of Commons by 5 April 2020.'"

This amendment would require the Chancellor of the Exchequer to review the revenue effects of this Clause, as far as they relate to section 188CJ of the Corporation Tax Act 2010 and report on those changes by the end of the tax year 2019-20.

Amendment 54, in clause 24, page 14, line 7, at end insert—

"(2B) At the end of section 188CJ of CTA 2010, insert—

'(4) The Chancellor of the Exchequer must review the effects on the property market attributable to the amendments made to this section by section 24 of the Finance Act 2019.

(5) A report of the review under subsection (4) must be laid before the House of Commons by 5 April 2020.'"

This amendment would require the Chancellor of the Exchequer to review the effects of this Clause, as far as they relate to section 188CJ of the Corporation Tax Act 2010, on the property market and report on those changes by the end of the tax year 2019-20.

Clause stand part.

Anneliese Dodds: The clause extends the definition of "UK-related company" for the purposes of group relief to include non-UK resident companies that are within the charge to corporation tax. That change follows previous announcements concerning the tax treatment of non-resident companies carrying out property-related business.

I think it will be helpful to indicate exactly what group relief relates to and why it is relevant. As I am sure the Committee is aware, group relief relates to the process whereby a so-called surrendering company that makes a corporate tax loss can pass certain kinds of

[Anneliese Dodds]

losses to another company in its group. The benefiting company—the "claimant company"—can use the loss passed on to it to reduce its corporation tax liability. Apparently, the claimant company often then pays the surrendering company for the loss it received, up to the value of the tax that was saved. That payment is not counted for tax purposes. The surrendering company benefits from that arrangement, as it has access to those funds from the claimant company rather than having to hang on to the loss for subsequent years. There is no change to the circumstances of the claimant company—it cancels out some of its corporation tax and just passes that saving on to its fellow group member.

That regime was partially liberalised in 2016, albeit that it was then counteracted by the introduction for large companies of a limit, which means that only 50% of profits can be offset against losses carried forward. That ceiling applies across the group, not to individual firms. There are a number of stipulations concerning the extent of common share ownership, which are intended to prevent the false creation of groups in relation to group relief. It is necessary for one company to be the owner of three quarters or more of the other company's share capital, or for a third company to own three quarters or more of the share capital of both companies involved, in order for them to be counted as part of a group for this purpose.

Other tests attempt to ensure that a genuine rather than a spurious group is involved. In addition, only certain types of income loss qualify, including trading losses, excess interest charges and management expenses. Until now, both the surrendering company and the claimant company had to be resident in the UK or carrying on a trade through a permanent establishment in the UK, although in some circumstances European economic area-based companies have been able to act as surrendering companies.

The Opposition have tabled four amendments to the clause. Amendments 51 and 53 would require a review of the impact on payments of corporation tax of the different elements of these proposals. Amendments 52 and 54 would require an examination of the proposals' impact on property markets.

As I said, amendments 51 and 53 would require a review of the revenue effects of the clause, particularly on corporation tax. The measures in the clause appear to be part of a group of measures in the Bill that attempt to equalise the treatment of non-UK and UK-resident property companies when it comes to taxation. We have already discussed the fact that such companies will be transferred into corporation tax and standard capital gains tax. In many cases, although the measures concerned might be viewed as levelling the playing field, they might also be viewed as causing risks to revenue, not least due to the reduced rate of corporation tax, which we discussed before lunch.

Clearly, this change would benefit non-resident firms by enabling them more easily to plan when to pay corporation tax with the group of which they are a member. It would therefore to be helpful to have a clearer indication than has already been provided of the likely revenue effects of the clause. I am not saying that that ease and greater facility, in terms of planning corporation tax incidence, is necessarily a problem, but it will potentially have a revenue impact.

On a related note, we surely need a review of the impact of the clause on the UK property market, as would be required by our amendments 52 and 54. It will be particularly helpful if that review examines whether or not more non-EEA companies will be brought into the scope of this kind of intra-group transfer. It seems that that may well be the case. Currently, aside from UK-resident companies, only EEA-based companies, under certain circumstances, benefit from the ability to transfer loss, and thus tax incidence, across the group of which they are a member.

It would also be helpful to understand whether the new measures could help to incentivise more complex group structures that stretch beyond the UK and both into and outwith the EEA. There may be merits in the resultant diversification of risk, given the national specificities and risk profiles of different property markets in different countries and so on, but equally there could be a risk of contagion from poorly regulated property markets in some non-EEA countries. Those countries are not currently within the scope of these measures but will potentially be brought in by the Bill.

It would be helpful to be provided with a better understanding of the broader implications of the proposals in the clause than is currently set out in the explanatory notes. That is why we tabled amendments 52 and 54.

Mel Stride: The clause extends the definition of UK-related companies for the purposes of group relief to include non-UK resident companies within the charge to corporation tax. Non-UK resident companies are not simply those within the EEA but any company anywhere in the world.

Anneliese Dodds: With this.

Mel Stride: Yes. As the hon. Lady pointed out, clause 17 provides that a non-UK resident company that carries on a UK property business will be charged to corporation tax, rather than income tax, as we discussed earlier. This will deliver equal tax treatment for UK-resident and non-UK resident companies that carry on UK property businesses, including the application of anti-avoidance measures within the corporation tax regime, as I pointed out.

However, under the current rules, non-UK resident companies within the charge to corporation tax are not able to make use of group relief, which, as the hon. Lady described extremely well, is the mechanism by which a company is able to surrender its tax losses to another member of the group to relieve their taxable profits. Group relief is available to UK-resident companies and helps to ensure that the tax charged reflects the economic reality of the entire group.

The clause will extend the definition of a UK-related company for the purposes of group relief to include non-UK resident companies that are within the charge to corporation tax. This change will also apply to non-UK resident companies developing UK land that were brought within the charge to corporation tax from July 2016. The clause will ensure that the UK tax regime does not discriminate against non-UK resident companies. These changes come at a negligible cost to the Exchequer.

Amendments 51 and 53 would require a review of the impact of the clause on corporation tax receipts. The Office for Budget Responsibility's certified assessment

of the impact of the clause on corporation tax receipts has been estimated together with clause 17 and schedule 5, which we debated earlier. That is set out in table 2.2 of the 2018 Budget and will be updated in table 2.2 of the 2019 Budget.

Amendments 52 and 54 would require an analysis of the effects of the clause on the UK property market. The impact on the UK property market was considered in the design of the policy, but it is not expected to have any notable effect. The OBR did not consider that the clause, nor clause 17 and schedule 5, would have any impact on its UK property market forecast.

The clause is a necessary element of levelling the playing field between UK-resident companies and companies not resident in the UK. It provides for equal tax treatment so that companies in receipt of similar types of UK property income will face the same tax rules. I commend the clause to the Committee.

2.45 pm

Anneliese Dodds: I am grateful to the Minister for that explanation and for the clarifications. It is important for the Committee to be aware that while this is part of a suite of measures to equalise tax treatment in terms of tax responsibilities, obviously the measure also provides some of the benefits of the UK tax system to non-EEA firms. Doing so could potentially increase the attractiveness of the UK property market for those non-EEA firms, which might be a good thing, but might also have other consequences. That is all I wish to say in response. I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 24 ordered to stand part of the Bill.

Clause 25

INTANGIBLE FIXED ASSETS: EXCEPTIONS TO DEGROUPING CHARGES ETC

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

Mel Stride: The clause amends the corporate intangible fixed assets regime, which I will refer to as the IFA regime, to align the degrouping adjustment rules more closely with the equivalent rules in the chargeable gains code. The clause responds to concerns expressed during the Government's consultation on the IFA regime, and in previous consultations, that the IFA degrouping adjustment is distorting how genuine commercial transactions are structured. The main criticism is that there are two different tax treatments for intangible assets, depending on whether the chargeable gains code or the IFA regime operates in respect of such assets.

The IFA regime provides corporation tax relief to companies on the cost of their intangible assets, such as patents or trademarks. The IFA regime, like the chargeable gains regime, allows groups to transfer assets between companies within the same group on a tax-neutral basis. That prevents gains or losses arising on transactions between companies within the same corporate group and reflects the fact that the group can constitute a single economic entity. Instead of recognising the market value of the asset on transfer, the company acquiring the asset inherits the tax history and costs of the transferor.

The rules contain an anti-avoidance provision which applies when an asset leaves the group. That is often referred to as a degrouping adjustment or charge. The degrouping adjustment effectively removes the benefit of a previous tax-neutral transfer to ensure the full economic gain or loss made by the group is taxed.

The chargeable gains tax code includes a similar set of rules, which were, however, amended in 2011 to refine the degrouping anti-avoidance rules where the sale of the shares in the degrouping company is exempt from a tax charge under the substantial shareholding exemption rules.

The clause seeks to address concerns commonly expressed by stakeholders during the recent IFA regime consultation and those raised during the 2016 review of the substantial shareholding exemption. Part 8 of the corporation tax code is amended so that the degrouping adjustment will not apply when a company leaves a group as a result of a share disposal that qualifies for the substantial shareholding exemption. That exemption applies only to disposals of trading companies, or parent companies of trading groups. In doing so, it aligns the clause with the treatment in the chargeable gains regime.

In summary, the clause makes a sensible change to the degrouping rules in the IFA regime to align them with the treatment elsewhere in the tax system. The clause responds to legitimate business concerns that existing legislation is distorting how genuine commercial transactions are structured. I therefore commend the clause to the Committee.

Jonathan Reynolds (Stalybridge and Hyde) (Lab/Co-op): It is, as ever, a pleasure to serve under your chairmanship, Mr Howarth, and to follow the many valuable contributions of other members of the Committee.

The clause that the Financial Secretary has just introduced forms part of a rather technical but important pack of items in the miscellaneous corporation tax section of the Bill. The provisions mark the latest change in a long history of reforms to the intangible fixed asset tax regime, which I will also refer to as the IFA, which began in 2002. Intangible fixed assets refer to items such as patents, copyright, brand recognition, goodwill and other items of intellectual property. It is clear that those types of assets, as opposed to tangible assets, have become increasingly important to modern businesses and are likely to continue to do so, especially for the tech industry.

Typically, such assets could be moved within companies that all belonged to the same UK group without incurring any new tax liability, by simply taking their existing tax history with them. If one of the companies that received the assets was subsequently sold within six years, that incurred the so-called degrouping charge. The clause will stop that charge being triggered if the company leaves as a result of a share disposal that would qualify for the substantial shareholding exemption.

In principle, the Opposition have no objection to the measure, which clarifies the intent of the legislation and prevents assets from being drawn into the regime unintentionally. The changes remove an artificial barrier in the tax system that could have been acting as a deterrent to merger and acquisition activity, given the disparity in treatment between chargeable gains assets and those within the IFA regime, as the Minister explained.

[Jonathan Reynolds]

However, we would like to raise some wider concerns about the intangible fixed asset regime and how the new provisions will operate. Intangible assets will only grow in importance, so it is vital we get the system right. We must also consider the potential impact on foreign direct investment, especially at a time when our international competitiveness is under pressure as a result of us leaving the EU.

My questions to the Minister relate to what the impact of the changes might be on foreign direct investment and on merger and acquisition activity. I also want to ask about the impact on the UK intellectual property market, for two reasons. First, although we all want to see the best in Britain's companies, we know that, unfortunately, certain operators seek to game the system, including by artificially shifting assets internally among subsidiaries, which is a time-worn tactic for unscrupulous actors seeking to avoid their true obligations. The long history of transfer pricing shows us that, as do the pitifully low corporation tax returns of some of the most profitable multinationals operating in the UK. By its very nature, transfer pricing—when companies make charges within a group for goods, services or indeed intangible assets—can be more easily exploited for that purpose, as can be seen from the role of brand loyalties in the transfer pricing arrangements of some famous tax minimisation schemes.

Tax rules have fallen short, and still fall short, of always recognising such arrangements for what they really are. We know that we suffer from a significant—and, some argue, underestimated—tax gap in the UK. As we often refer to in debates with the Government Front Bench, the tax gap has consistently fallen under Labour, coalition and now Conservative Governments, but we all know that the assessment does not truly cover such practices. Therefore, it is imperative that we do not put any loopholes into the statute book that could be exploited. Can the Minister explain what action the Government have taken to ensure that the measures cannot be undermined by tax avoidance?

Secondly, the measure is important in relation to the consultation published alongside this year's Budget to look again at so-called goodwill taxation. Goodwill is the sum paid for a business over and above its paper value, which often has a strong connection to intangible assets such as brand value, reputation and other items of intellectual property. Stakeholders have expressed concern about the treatment of goodwill, which we ask the Government to consider as part of the overall IFA tax regime.

Although we supported the restriction of that relief for anti-avoidance purposes in 2015, it has been reported to us that some people believe that some aspects of the changes have had a dampening effect on commercial transactions and the overall attractiveness of the UK as a business location. Therefore, some further context around the proposal in the 2018 Budget to reverse part of those restrictions would be welcome.

I seek some reassurance from the Minister as to his future plans for the treatment of goodwill and how precisely this relief will be used as a tool to attract further business activity to the UK. Is an estimate available of the costs to the Exchequer at this stage? How has this been assessed, in terms of wider value for money, against perhaps extending other types of relief available? How will the connection between intellectual property and goodwill be properly established? In particular, how will the valuation of intangibles be achieved for tax purposes? What action is being undertaken with regard to anti-avoidance measures?

Continuing to attract business to the UK, as well as strong inward investment, is critical as we contemplate our departure from the EU. Therefore, we would appreciate some clarity from the Government on these provisions. We must assess their cost against the value of incubating the type of intellectual property-rich businesses that we would all like to see more of in the UK. Equally, we must do everything that we can to protect the statute book from any loopholes that may be exploited by unscrupulous companies seeking to avoid paying their fair share.

Mel Stride: I thank the hon. Gentleman for his contribution. He asked specifically what impact these measures may have on foreign direct investment. I would argue that they are relieving, in that they are facilitating the ability of companies in these circumstances to gain value from the transfer of their losses where they genuinely fall under the substantial share exemption, so the answer to that question is that this is a positive move in that respect.

The hon. Gentleman asked, more specifically, a series of questions relating to how we would ensure that avoidance was not entered into in a number of scenarios. I think that he referred specifically to transfer pricing, for example, and one thinks of intangible asset elements such as royalty payments. He will be aware that we have already clamped down on the making of royalty payments through to low and no-tax jurisdictions. There is a lot of activity in that space, albeit that in the context of this clause, that is probably out of the scope of the measure that we are considering.

The hon. Gentleman asked whether we were introducing a loophole, as he termed it. I think I can reassure him that we are not. We are simply, as I think he said when he summarised the clause at the start of his remarks, ensuring that intangible assets are treated in the right way when it comes to their transfer within and outside corporate groups.

The hon. Gentleman made several points surrounding our intentions in respect of goodwill and its treatment. To support UK investment in intangibles, the Government are introducing a targeted relief for goodwill in acquisitions of businesses with eligible intellectual property. We will legislate for that change through an amendment on Report, to allow for a further brief consultation on the detailed design of the policy. The consultation will seek to ensure that the proposed policy design achieves the Government's objective to provide targeted relief for goodwill in the acquisition of IP-intensive businesses, and mitigates any unintended consequences.

Question put and agreed to.

Clause 25 accordingly ordered to stand part of the Bill.

Clause 26

CORPORATION TAX RELIEF FOR CARRIED-FORWARD LOSSES

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

The Chair: With this it will be convenient to discuss that schedule 9 be the Ninth schedule to the Bill.

Mel Stride: Clause 26 makes technical amendments to the corporate loss relief rules introduced in 2017: they ensure that the rules function as originally intended and protect revenue by preventing companies from claiming excessive relief. When a company makes a loss, it can carry forward that loss and use it to offset its taxable profits in future years. The Finance (No. 2) Act 2017 reformed the UK's loss relief regime. The main effects of that reform were as follows. First, the amount of profit that can be relieved by carried-forward losses is restricted to 50%, subject to a £5 million allowance. Secondly, losses arising after 1 April 2017 can be carried forward and set against different types of income and against profit of other members of the same group. The loss restriction ensures that companies cannot use carried-forward losses to reduce their tax bill to nothing in an accounting period in which they make substantial profits. Legislation for the new loss relief rules needed to be sufficiently detailed to ensure that they were robust for the complex arrangements of large companies operating across a diverse set of activities. The Government have since identified limited circumstances in which the rules are not functioning as intended.

The clause amends the way that companies calculate their relevant profits for the purposes of loss relief restriction. Specifically, the clause changes the way basic life assurance and general annuity businesses, or BLAGAB, calculate relevant profits. That will ensure that BLAGAB insurers use profits that are chargeable to corporation tax for calculating the amount of loss relief they can claim.

3 pm

The clause also makes several minor technical amendments to the loss reform rules in respect of the deductions allowance, terminal loss relief, transfer of a claim without change of ownership, oil and gas losses, group relief and the transfer of deductions. Due to the £5 million allowance, 99% of companies are not financially affected by the carried-forward loss restriction, and that will not be changed by these amendments. Some companies will also benefit from the simpler rules for calculating their loss relief restriction.

The amendments to group relief for carried-forward losses are effective from 1 April 2017, the amendments to the calculation of relevant profits and BLAGAB profits are effective from 6 July 2018, and the other amendments are effective from 1 April 2019. This clause introduces technical amendments to ensure that the corporation loss relief rules work as intended, and to protect revenue by preventing companies from claiming excessive relief. I therefore commend the clause and schedule to the Committee.

Jonathan Reynolds: I shall speak briefly on this clause. As the Minister said, the clause seeks to restrict relief for certain carried-forward losses and allow them to be used more flexibly. It then drills down into particular details for specific business segments: for instance, insurers require special consideration due to the shock losses they are uniquely exposed to.

Given the rather generous package of corporate support that the Government espouse and the ineffective corporation tax cuts, which we have already had an opportunity to discuss at length, the Opposition clearly have no issue with restricting excessive relief. However, this change appears to be a tidy-up measure on legislation that was only introduced in 2017, suggesting that the Treasury does not quite have a grip on this properly. Clearly, we would all like to see any mistakes on the statute book or in the tax code corrected, but could the Minister explain why this legislation needs correcting such a short time after its implementation? Should we perhaps anticipate further changes to the original legislation? What consultation took place with stakeholders at the time?

It seems that we have always known there were issues with this relief ever since it was first introduced, after consultation in summer 2016, in the Finance (No. 2) Act 2017—perhaps the first Finance Bill for the shadow Chief Secretary, my hon. Friend the Member for Bootle, if he can segment them in his own mind—

Clive Lewis (Norwich South) (Lab): Happy memories!

Jonathan Reynolds: Yes, a classic. At the time, the Chartered Institute of Taxation warned that the legislation had not been given proper due consideration. As it said in its briefing:

"From the time the proposals were announced at Budget 2016 it was clear that the legislation would be voluminous and highly complex. As we highlighted in our response to the consultation (in August 2016) the timetable proposed was not sufficient to properly consider all of the issues and to produce clear and workable legislation.

The unsatisfactory draft legislation published as part of Finance (No. 2) Bill 2017 was then removed from the pre-election Finance Bill, which caused more uncertainty for taxpayers. Although the delay in enacting the legislation has allowed a period of further informal consultation, which has improved the legislation, it inevitably led to a degree of uncertainty among those affected and has also resulted in taxpayers having to consider draft legislation which is not yet in force,"

but which will be retrospective once enacted.

"With regard to the short timetable, it is also worth noting that these provisions are not anti-avoidance provisions",

which is when we tend to use a shorter timeframe for introduction.

"Rather, the changes were proposed as part of a package intended to 'simplify and modernise the tax regime', although in our view there are aspects of the changes which are very complicated and, in many cases, will involve a large number of detailed calculations, meaning that simplification will not be achieved."

That is probably true of much of what the Treasury does, to be honest. The briefing also said:

"Legislation for these new rules has, in our view, been 'rushed'…and, in this case, the Government has not balanced its desires to raise some modest revenue with its duty to produce legislation that can be followed with predictability and certainty."

Unfortunately, the Chartered Institute of Taxation's assessment that the timeframe was too short turned out to be exactly correct, and that is why we are obliged to revisit this legislation today. Continuous tweaks to matters such as these do not help to instil confidence among businesses that rely on this framework. They need certainty in their long-term operation, and endless rounds of changes are not helpful, especially in an environment where Brexit is clearly causing significant wider uncertainty.

I should also be grateful to learn from the Minister what preventive measures have been put in place to ensure that we will not go through the same legislative process in another year's time, with further nips, tucks

[Jonathan Reynolds]

and fixes to defects. Finally, I would just like to know whether an estimate is available of the cost up to now of businesses having claimed this relief, which the Minister himself has said may have been excessive, and which we are today removing.

Mel Stride: It is a perfectly fair question for the hon. Gentleman to ask why we are now having to revisit this, having consulted on it. He himself raised the issue of the large volume and the highly complex nature of the original legislation. I think therein probably lies the answer. While we did consult extensively, this was a large volume and a highly complex area, and we have subsequently discovered a deficiency with it, which we are now putting right, in a responsible way.

It is important to briefly enlighten the Committee as to the extent of the consultation that did occur, lest it be imagined that we rushed this or did not properly look into matters. The Government's consultation ran for 12 weeks, from 26 May to 18 August 2016. The Government received 79 responses from stakeholders, and from a broad range of professions and industries. There was also a technical consultation on the draft legislation itself. It is obviously right that we put these deficiencies right at the earliest opportunity. In answer to the hon. Gentleman's question about how much revenue may already have been impacted by the original issue, I do not have a precise answer. I am happy to look into it. I know that the Treasury sees this clause as something that is there to protect revenues in the future, rather than one that is about rectifying problems that may have arisen in the past.

Question put and agreed to.

Clause 26 accordingly ordered to stand part of the Bill.

Schedule 9 agreed to.

Clause 27

Corporate interest restriction

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.

Mel Stride: Clause 27 and schedule 10 make changes to ensure that the corporate interest restriction rules will continue to operate as intended, limiting the amount of interest expense and similar financing costs that a corporate group can deduct against its taxable income. The UK's corporate interest restriction rules were announced at Autumn Statement 2016 and took effect from 1 April 2017. These rules prevent groups from using financing expenses to erode their UK tax base, where these expenses are not aligned with the group's UK taxable activities. These rules are complex because they operate at both the worldwide group and individual entity levels. As businesses have begun to apply them, HMRC has identified some technical amendments that are needed to ensure that the rules operate as intended and to address practical compliance issues.

Clause 27 and schedule 10 make a number of technical amendments to the interest restriction rules. To ensure the rules are applied as intended, the schedule will clarify that real estate investment trusts are in scope of the interest restriction rules, but that they do not suffer a double restriction of financing costs where they are highly leveraged. It will confirm that where a company holds a significant pension fund asset or a deferred tax asset, or where the company is reimbursed for certain variable operating costs, it is not prevented from applying the alternative rules for public infrastructure. It will provide confirmation of how the rules deal with capitalised interest.

To ease the practical operation of the rules, the schedule will extend certain timings, in particular for appointing a reporting company and for submitting an interest restriction return, following an acquisition. The schedule will allow unused amounts and debt cap to be carried forward for a new holding company that is inserted into the group structure, but the shareholders of the group remain substantially unchanged. To align the rules more closely with the normal UK tax rules the schedule will require, where appropriate, employee remuneration that is not paid within nine months to be disregarded in the calculation of a group's earnings, until it is paid. It will also amend the calculation of the group's financing costs to ensure that it is not distorted when a debt is released by a company that is connected to the group but not in it.

Finally, this schedule will allow HMRC to specify information that is reasonably required for risk assessment purposes, which is to be included in the interest restriction return. This clause and the accompanying schedule make amendments to ensure that the interest restriction rule continues to operate as originally intended. I commend this clause and schedule to the Committee.

Jonathan Reynolds: We have before us in clause 27 another tweak to the 2017 legislation, which originally brought about this change. The clause is designed to bring about technical amendments to the corporate interest restriction rules. Again, the Opposition are supportive of any measure that aims to correct the tax situation, which could potentially be exploited. These rules restrict the ability of large businesses to reduce their taxable profits through excessive UK interest.

The explanatory notes tell us that this is part of the Government's policy to align the location of taxable profits with the location of economic activity—not before time, many people in the country would argue. We are very much looking forward to seeing the Government rigorously apply this approach to the multinational companies in the UK, which mysteriously report profits quite unrelated to their tax bills. As my right hon. Friend the Member for Barking (Dame Margaret Hodge) recently calculated, Facebook's corporation tax bill represents just 0.62% of its revenue here, as it pays £7.4 million in corporation tax on sales of £1.3 billion.

We are pleased that the Government have found the time to tidy up the statute book by implementing the measure before us today. Surely, the Minister must agree that there still appears to be one rule for big companies, such as Facebook, and another for everybody else. Rather than arguments about things such as the tax gap, which addresses things such as how much cash-in-hand has been paid for trade in services, this

imbalance is what the public really want to see addressed. If there is one thing that the whole Committee might agree on, it is that we all welcome innovation and technology, and all the benefits they bring. However, part of what makes this country so lucrative for these big companies is our infrastructure, our legal system, our transport connections and our businesses, which want to be able to advertise on these platforms. It is not unreasonable for the likes of Facebook to contribute to that, just as every other business does.

The clause is clearly more modest than that, being, as I said, just a tweak to the 2017 legislation. It would have been infinitely preferable to get this right first time. The explanatory note sets out in detail the consultation process that was undertaken in relation to this legislation between 2015 and 2016. That seems to have discussed issues related to domestic implementation and, we must remember, will have been carried out at a cost to Her Majesty's Treasury and, therefore, the taxpayer. Again I have to ask, what fell short in that process, so that we are discovering these defects in the Bill only one year later? Could the Minister provide some further insight on the further engagement with affected businesses that is mentioned in the explanatory notes?

Mel Stride: The answer to the hon. Gentleman's understandable question as to why we have to revisit this matter in this Finance Bill is similar to that which I gave in the context of the last clause—the complexity and the volume of the legislation. We published the draft legislation originally, so that it could be considered. I think it is right that we are now coming forward to make the necessary changes at this time. The hon. Gentleman mentioned his aspirations that the corporate interest restriction would bite and be effective. For that, I am sure he has looked at the amount that is scored for this particular measure—it is one of the more significant anti-avoidance measures that we have come forward with in recent times.

The hon. Gentleman also commented on the tax gap and sought, perhaps, to characterise the tax gap as being all about—I think he used the expression—cash-in-hand dealings, so as to suggest that it was not also about ensuring that large companies pay their fair share of tax. I assure him that we are constantly looking at larger businesses. The tax gap is disaggregated in a way that shows that. I reassure him that of the largest roughly 200 or 210 companies in the United Kingdom, about 50% are under active investigation at any one time. That does not mean in any way that any of them have done anything wrong, but that we do look at larger companies very carefully.

Jonathan Reynolds: I was simply trying to make the point that the tax gap is a series of estimates by HMRC as to avoidance in different areas—yes, for large companies as well as small. Surely, what the public really want action on—the Chancellor himself referenced this in his Budget speech—is the impact of very large technology companies internally charging vast amounts for intellectual property transactions within their groups and not reflecting their economic activity in a country the size of the UK.

3.15 pm

Mel Stride: The hon. Gentleman makes an important point. I thank him for clarifying his comments on the tax gap. He asserts that the public expect us to take tax avoidance by large companies seriously. I assure him that that is exactly what the Government are doing. We have introduced more than 100 measures relating to avoidance, evasion and non-compliance since 2010. We have brought in and protected around £200 billion in that period. Of course, in this Committee we have debated at length both the diverted profits tax, which is bringing in more than originally anticipated and is aimed at exactly the businesses to which he refers, and the digital services tax. We are even changing the way in which the tax regime operates in order to ensure that we get a fair level of tax from those companies, whether they are the smallest businesses in the land or the largest.

Question put and agreed to.

Clause 27 accordingly ordered to stand part of the Bill.

Schedule 10 agreed to.

Clause 28

Debtor relationships of company where money lent to connected companies

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

The Chair: With this it will be convenient to discuss that schedule 11 be the Eleventh schedule to the Bill.

Mel Stride: Clause 28 is part of a package of changes that the Government are making to the tax rules for hybrid capital instruments, which are issued by some companies to raise funds. Further changes are made by clause 88. Together, those changes ensure that hybrid capital instruments are taxed in line with their economic substance and take into account forthcoming changes in financial sector regulation. The new rules cover issuances by companies in any sector and replace rules covering regulatory capital instruments issued by banks and insurers with effect from 1 January 2019.

Some companies raise funds by issuing instruments, referred to as hybrid capital, that sit close to the border between debt and equity. Hybrid capital instruments have features, such as provisions for write-down or conversion to shares in certain circumstances, that may affect their accounting and tax treatment. As a result, instruments that a company uses to raise funds externally may be taxed on a different basis from instruments used to distribute those funds internally to other group companies. Recent changes to financial regulation have highlighted that issue.

In June 2018, the Bank of England finalised its approach to setting a minimum requirement for own funds and eligible liabilities—MREL. The Bank set out how it would use its powers to require firms to hold a minimum amount of equity and debt with loss-absorbing capacity from 1 January 2019. That will allow the Bank to ensure that shareholders and creditors absorb losses in times of financial stress, allowing banks to keep operating without recourse to public funds.

For banking groups, funding that counts towards MREL is usually raised from the capital markets by a holding company. The holding company passes on most or all of the funds raised to operating companies within the group. The Bank of England requires those intra-group

[Mel Stride]

loans to include terms that allow them to be written off or converted into shares at times of severe financial stress. That can result in the external and internal loans being treated differently for tax, leading to unintended tax volatility unrelated to the economic substance of the loans.

In the changes made by clause 28 and schedule 11, our overall aim is to eliminate that unintended tax volatility by ensuring that external and intra-group loans are taxed on the same basis if they have a qualifying link. A qualifying link arises when funds raised externally by a group are wholly or mainly lent within the group. Clause 28 and schedule 11 will ensure that external financial instruments are taxed on the same basis as intra-group loans to which they have a qualifying link. That will eliminate the tax volatility that can arise if the terms of the intra-group instrument contain hybrid features. That is expected to affect a small number of companies, mostly in the banking sector, that raise funds externally and lend them intra-group in circumstances that would otherwise give rise to a tax mismatch between those instruments.

These changes will ensure that our tax rules eliminate unintended and unnecessary tax volatility from financial instruments issued by any company. I therefore commend this clause and schedule to the Committee.

Jonathan Reynolds: This clause changes the treatment of linked loan relationships in company groups. Put simply, that means that where one company borrows funds externally and lends on to another company in the group, no tax liability will be triggered by fluctuations in the value of the internal component of the loan. It stands to reason that companies should be protected from what might end up being double taxation. In reality, there is no economic exposure on the internal loan, whereas that does apply to the external arrangement, which remains within the scope of taxation.

Although this appears to be a relatively straightforward measure, will the Minister elaborate on what has prompted its inclusion in the Bill? Is there an assessment of its impact on the Exchequer? An example has been provided in the explanatory notes of the issuance of debt instruments by banking or insurance companies to meet regulatory capital requirements. Are there companies outside the financial sector that could be affected by these regulations? I think he said most but not all.

What engagement has taken place with the business community on these measures? We have seen from the two preceding clauses that unintended consequences can sometimes arise. If we are not vigilant of those first time round, legislation will have to be revisited, with endless amendments in subsequent Finance Bills.

The Opposition strongly believe that one of the best ways to make the UK an attractive place to do business is to create a robust, consistent, transparent and well-enforced corporation tax regime. Business prizes certainty—something that no one has been able to offer of late. We want to ensure that measures have been taken with the proper consultation and with proper justification, so that we do not endlessly increase the compliance burden of companies doing business in the UK.

Finally, and perhaps most critically, I refer to my earlier comments on transfer pricing in our discussions on clause 25. We all want to believe that this is a simple measure that tidies up the statute book. However, we must all be mindful that the shifting of assets and loans between UK subsidiaries has historically been abused by companies seeking to avoid tax. Have the Government done all due diligence possible to ensure that this clause is not open to such exploitation? Given the consequences of getting it wrong, we all share a duty to ensure that no loophole is left anywhere on the statute book.

Mel Stride: The hon. Gentleman asks whether banks are solely affected by the changes; they go beyond banks but are most relevant to banks, driven as they have been by the changing requirements of the Bank of England and others on the operation of our financial service marketplaces. They are also driven by the importance of hybrid capital debt and how it is valued as it comes into the holding company, and the way debt might be valued as it is passed down in the companies beneath the holding company at the top.

The hon. Gentleman asked about consultation and the importance of getting the proposals right; there has been no public consultation on this clause due to time constraints—one has to bear it in mind that the Bank of England finalised the requirements for internal loss-absorbing instruments only in June. That has not given us much time to consult. We have informally consulted with a small number of trusted advisers ahead of the Budget announcement. HMRC and HMT have worked closely with the Bank of England and the Prudential Regulation Authority to ensure that alignment between the tax and regulatory rules is as close as possible.

Question put and agreed to.

Clause 28 accordingly ordered to stand part of the Bill.

Schedule 11 agreed to.

Clause 29

Construction expenditure on buildings and structures

Jonathan Reynolds: I beg to move amendment 57, in clause 29, page 17, line 8, at end insert—

"(14) No later than two months after the passing of this Act, the Chancellor of the Exchequer must lay before the House of Commons a report on the consultation undertaken on the provisions in this section."

This amendment would require the Chancellor of the Exchequer to report on the consultation undertaken on Clause 29.

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

Amendment 58, in clause 29, page 17, line 8, at end insert—

"(14) The Chancellor of the Exchequer must review the revenue effects of the relief that will be created as a result of the exercise of the powers in this section and lay a report of that review before the House of Commons within six months of the passing of this Act."

This amendment would require the Chancellor of the Exchequer to review the revenue effects of the changes made by Clause 29.

Amendment 59, in clause 29, page 17, line 8, at end insert—

"(14) The Chancellor of the Exchequer must review the uptake of the relief that will be created as a result of the powers in this section by the groups set out in subsection 15.

(15) The groups that must be considered under the review in subsection 14 are—

(a) companies with between zero and nine employees,

(b) companies with between 10 and 250 employees, and

(c) companies with more than 250 employees.

(16) A report of the review under subsection (14) must be laid before the House of Commons no later than 12 months after the first exercise of the powers under this section."

This amendment would require the Chancellor of the Exchequer to review the uptake of this relief among micro-businesses, SMEs and large companies.

Amendment 60, in clause 29, page 17, line 8, at end insert—

"(14) No draft instrument may be laid under this section until the Treasury has carried out a consultation with stakeholders on the qualifying arrangements for the relief that would be created as a result of the powers in this section."

This amendment would require the Treasury to carry out a consultation with stakeholders on the qualifying arrangements for this allowance.

Clause stand part.

Jonathan Reynolds: I will speak to Labour's amendments to clause 29, which opens up the new section on capital allowances. It is always right and sensible to think about ways to promote business growth in the UK, but allowances like the ones in these clauses are not free. The Committee must judge them in the context of what represents good value for money. We will talk about each of them as we move through the clauses.

These clauses also represent a significant round of chopping and changing reliefs, but in our view businesses are really asking for certainty. The changes are many and varied, and the constant shifting of the goalposts creates costs and complexity for businesses. Given that the Government's central case for reducing corporation tax is that they are trying to increase corporate investment, which has not happened, it seems strange to have a set of policies reducing and incentivising capital allowances to do exactly the same thing. I have spoken to a number of concerned stakeholders who have told me that there has been little or no consultation on some of these measures.

The lack of consultation on the allowance in clause 29, in particular, is worrying. The initiative was announced with immediate effect on the day of the Budget—29 October. Stakeholders have raised the valid concern that it remains framework legislation with none of the detail necessary for proper scrutiny—not just by the Opposition but by industry and the people whom the Bill will directly affect. Presumably the Government did not preannounce the measure to ensure that no investment decisions were delayed in anticipation of it, but they must be clear about what business will be getting. Immediate implementation is an important power in the Treasury toolkit, but it is usually an anti-avoidance measure. It is hard to see how that applies in the case of this allowance. It has simply generated more opacity about what will qualify.

We are talking about a big item of spend. Businesses need to be able to attach numbers to their construction plans, and they need absolute clarity about what qualifies as expenditure and what does not. The regulations do not yet specify what "qualifying use" is. The allowance is also a big-ticket item for the Exchequer. According to the Red Book, by 2023-24 it will cost more than half a billion pounds—£585 million—yet we cannot be 100% sure about that number because there is so much uncertainty about what the exact scope will be. Labour's amendment 58—I urge hon. Members to support it when we press it to a vote—requests that the Government review the revenue effects of the relief so we can fully assess its costs.

As professional bodies have argued, it would have made much more sense to do this process in reverse. The Government are only now seeking views on the relief, with a view to changing it via secondary legislation in 2019. Anyone who has had the pleasure of sitting on any of the Brexit-related Delegated Legislation Committees will agree that there is as large pile of statutory instruments to get through, so adding to that is a strange decision.

Why did the Government not consult before they drew up the legislation? A concern that stakeholders have raised with me is that businesses cannot have confidence in the new relief during the consultation period as the detail is not yet known. That seems a strange way to encourage investment. We believe that one of the problems that is likely to be revealed in the consultation is the complexity of the measure. As tax professionals have warned, the relief will introduce another type of asset classification for tax purposes. The Office of Tax Simplification advised against that when it reviewed capital allowances. Why are the Government contravening the recommendations of the report that they commissioned? Tax simplification has generally been of considerable interest to Conservative Members, but they appear to be ignoring the review. Given the lack of consultation, will the Minister elaborate exactly how the conclusion was reached that the relief would cost £585 million? What evidence is there that it will promote investment in productivity?

I also urge hon. Members to support Labour's amendment 57, which would oblige the Chancellor to lay before the House a report on the consultation undertaken on the provisions in this clause so that we can get as clear grasp of the concerns they are targeted at. Amendment 60 goes further and states that no draft instrument can be laid under this clause until consultation is carried out with stakeholders on qualifying arrangements for relief. It must work for all the businesses it is targeted at.

In addition, amendment 59 would oblige the Government to disclose how the take-up of the relief is distributed among microbusinesses, SMEs and large corporations. We must be able to assess whether this relief is of genuine value to small businesses or is yet another poorly targeted giveaway.

3.30 pm

I also find it peculiar that the relief has been made available on overseas property. Why is the UK offering tax breaks for the construction of buildings and commercial developments that might be located abroad? That seems counter-intuitive to the purpose of this allowance.

The seemingly generous inclusion of the allowance is in perpetuity. As the Bill reads, it appears that the allowance can get sold on for the duration of the building's existence if the building is purchased by another business. That seems an unusual extension of a relief, from a one-off measure to promote investment by

one particular company to an incentive to purchase the building by another company that may be in a quite different position.

Those are all issues that could have been covered in dialogue with the people whom this measure will affect. I ask all colleagues to support Labour's amendments today, which will reveal the conversations that took place before this relief was decided and—crucially—what the real revenue effects will be.

Kirsty Blackman: I rise to speak very briefly on this clause. The questions that have been asked by the Opposition are incredibly useful and interesting ones; they have gone into this matter in some detail. Given the amendments that they have put forward, the SNP will be happy to support any of them that are pressed to a vote.

Mel Stride: May I address very directly the question that the hon. Member for Stalybridge and Hyde has posed regarding consultation and the level of consultation before the announcement, which of course he recognises is in part at least due to the fact that on announcing this measure we do not want to have forestalling in terms of businesses taking investment decisions?

Indeed, with matters or measures of this kind, we have a number of things that we need to balance. As I say, we need to ensure that businesses do not delay investment; we also have to give businesses the certainty they need that the measures will actually be implemented; and we are of course consulting on the technical details, including the very pertinent issue of the qualifying use that he referred to. And we will of course consult on the draft legislation when it is brought forward.

The hon. Gentleman asked about the figures and the cost of this measure, and how that cost has been established. The OBR will score these measures in the normal manner. He also made the specific point about the desirability of these reliefs being available to construction projects and other qualifying activities overseas. Of course one should make the point that that would occur only where it was on the part of a company that fell due to the UK corporation tax charge, and would reflect exactly the same situation in reverse, were it to be, say, a French business constructing something in the United Kingdom and in turn receiving reliefs from the French tax authorities. So it is a kind of equality of treatment in those particular respects.

The UK was previously the only G7 economy that gave no capital relief on structures and buildings. The CBI's recent report, "Catching the peloton", asked the Government to explore how the incentive regime could support investment in commercial buildings. *[Laughter.]* I am assuming that this is some kind of sub-atomic particle that requires a Large Hadron Collider, or whatever these things are, to be built, with huge tax reliefs associated with it.

The Government recognise the importance of providing tax reliefs for genuine business costs, supporting investment and growth, and driving our future prosperity. Therefore, this relief will reduce the cost of doing business in the UK, alongside our corporation tax reductions.

The changes made by clause 29 will give the Government the power to introduce secondary legislation, as we have discussed, to provide capital allowance on the costs of non-residential structures and buildings. Key features of the policy are outlined in the technical note published on Budget day, which invites businesses to express views on detailed aspects of this policy.

This legislative process will provide taxpayers with certainty that the allowance will come into force as soon as possible, while allowing the Government to consult on important policy decisions. The new relief will provide businesses with an additional £1.9 billion of tax relief in the next six years, growing to £2 billion annually by year 50. The allowance will be available to any unincorporated or incorporated business that builds a new structure or a building, or that acquires one directly from a developer. The allowance will apply across all sectors and sizes of UK trade, improving our collective economic position as we go into 2019 and beyond.

Amendments 57 and 60 seek to commit the Government to carry out and lay before the House a report on the consultation with stakeholders on arrangements for the allowance. The Government, however, have already invited stakeholders' views on the detailed aspects of the allowance, and have made it clear to the public that a further technical consultation will be issued on the draft secondary legislation. That is set out in the technical note, published alongside the 2018 Budget.

Amendments 58 and 59 seek a Government review of the revenue effects and the uptake of the relief among different-sized businesses. The estimated revenue effects have been published in the Budget 2018 document. The relief is expected to provide £1.9 billion of additional support over the next six years to businesses of all sizes. That figure has been subject to detailed challenge and to the scrutiny of the independent Office for Budget Responsibility.

Amendment 58 requests that the Government lay a report on the revenue effects before the House within six months of the enactment of the Bill. That would not be technically possible, due to the time needed for businesses to make new claims and for the Government to carry out the necessary analysis. However, HMRC publishes annually the cost of capital allowances claimed and the capital allowances available, split by asset type and by industry, in the "Estimated costs of the principal tax reliefs" and "Corporation Tax Statistics" documents. Those publications will include the new allowance costs as soon as sufficient data are available. I therefore urge hon. Members to withdraw their amendments, and I commend the clause to the Committee.

Jonathan Reynolds: To make an appropriate level of progress, with the leave of the Committee, I will not press all amendments save for amendment 59. I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Amendment proposed: 59, in clause 29, page 17, line 8, at end insert—

'(14) The Chancellor of the Exchequer must review the uptake of the relief that will be created as a result of the powers in this section by the groups set out in subsection 15.

(15) The groups that must be considered under the review in subsection 14 are—

(a) companies with between zero and nine employees,

(b) companies with between 10 and 250 employees, and

(c) companies with more than 250 employees.

(16) A report of the review under subsection (14) must be laid before the House of Commons no later than 12 months after the first exercise of the powers under this section.'—*(Jonathan Reynolds.)*

This amendment would require the Chancellor of the Exchequer to review the uptake of this relief among micro-businesses, SMEs and large companies.

Question put, That the amendment be made.

The Committee divided: Ayes 8, Noes 9.

Division No. 16]

AYES

Black, Mhairi
Blackman, Kirsty
Dodds, Anneliese
Dowd, Peter
Lewis, Clive
Reynolds, Jonathan
Smith, Jeff
Sobel, Alex

NOES

Afolami, Bim
Badenoch, Mrs Kemi
Ford, Vicky
Jenrick, Robert
Keegan, Gillian
Lamont, John
Stride, rh Mel
Syms, Sir Robert
Whittaker, Craig

Question accordingly negatived.

Clause 29 ordered to stand part of the Bill.

Clause 30

Special rate expenditure on plant and machinery

Jonathan Reynolds: I beg to move amendment 61, in clause 30, page 17, line 35, at end insert—

‘(9) The Chancellor of the Exchequer must commission a review on impact of the amendments made by this section on CO2 emissions from plant and machinery operated in the United Kingdom.

(10) A report of the review under subsection (9) must be laid before the House of Commons by 1 April 2020.’

This amendment would require the Chancellor of the Exchequer to review the effects of this Clause on CO2 emissions from plant and machinery, and report on those changes by the end of the tax year 2019-20.

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

Amendment 62, in clause 30, page 17, line 35, at end insert—

‘(9) The Chancellor of the Exchequer must commission a review on impact of the amendments made by this section on the prices of—

(a) household heating and electricity, and

(b) insulation material.

(10) A report of the review under subsection (9) must be laid before the House of Commons by 1 April 2020.’

This amendment would require the Chancellor of the Exchequer to review the effects of this clause on the cost of heating, electricity and insulation material and report on those changes by the end of the tax year 2019-20.

Amendment 63, in clause 30, page 17, line 35, at end insert—

‘(9) The Chancellor of the Exchequer must commission a review on impact of the amendments made by this section on the automotive market in the United Kingdom.

(10) A report of the review under subsection (9) must be laid before the House of Commons by 1 April 2020.’

This amendment would require the Chancellor of the Exchequer to review the effects of this Clause on the automotive market in the UK and report on those changes by the end of the tax year 2019-20.

Amendment 64, in clause 30, page 17, line 35, at end insert—

‘(9) The Chancellor of the Exchequer must commission a review on impact of the amendments made by this section on the level of investment in plant and machinery included as special rate expenditure, where such plant and machinery was made before April 2019.

(10) A report of the review under subsection (9) must be laid before the House of Commons by 1 April 2020.’

This amendment would require the Chancellor of the Exchequer to review the effects of this clause upon business decisions to invest in eligible plant and machinery made before April 2019 and report on those changes by the end of the tax year 2019-20.

Amendment 65, in clause 30, page 17, line 35, at end insert—

‘(9) The Chancellor of the Exchequer must lay before the House of Commons a report on any consultation undertaken on the provisions in this section.

(10) A report of the review under subsection (9) must be laid before the House of Commons within two months of the passing of this Act.’

This amendment would require the Chancellor of the Exchequer to report on any consultation undertaken on the provisions in this clause.

Clause stand part.

Jonathan Reynolds: The clause proposes reducing the special rate for qualifying plant and machinery assets from 8% to 6%. It is reassuring to see something in this package of measures that raises some revenue, but it represents another small change to the way businesses are asked to operate. It is more change, more complexity and less certainty, all at a very difficult time for British business. I understand that this measure, as the Chancellor said in his Budget speech, has been introduced in part to fund the buildings allowance outlined in clause 29, which we have just discussed.

One of the problems with a change like this is that businesses make their plans on the basis of what tax rates are when they make those decisions. As the Chartered Institute of Taxation has warned, this gives the rate

“an element of retroaction, as investment decisions may have been taken on the basis of an 8% rate of allowance”

that is now being shifted to 6%. In its words:

“Tinkering with rates and allowances in this way undermines the principles of stability and certainty and as a result reduces the international competitiveness of the UK’s tax system.”

The Chartered Institute of Taxation also highlights the potential flaw in the logic that people will be able to balance off one cut against another:

“The impact of this change in rate will be different for different businesses.”

Any business that is unable to take advantage of the new structure and buildings allowance will find that it is simply worse off. It is therefore concerning that no prior consultation took place regarding these measures, so we simply do not know the different ways in which businesses might be impacted, or what they will make of these various allowances.

For that reason, the Opposition have tabled a package of amendments to dig deeper into what the impact of those changes will be. Amendment 65 prompts the Government to present to the House a report on any consultation that was undertaken with regards to this measure. As I have just stated, we have significant concerns about how little consultation was carried out regarding any of these measures, and the potential problems that might arise in implementation, given the

[Jonathan Reynolds]

scope of what is being proposed. We need to know what opinions were sought from the companies this will impact upon, and how those opinions were taken into account, if at all. Further to that, amendments 62 and 63 call for specific reviews of how the special rates will impact on both the use of household insulation—which would be included as an integral feature—and the automotive industry. Higher-emission vehicles would attract the lower rate of relief, rather than the full relief of 100% for lower-emission vehicles.

That brings me to the huge missed opportunity in this clause to promote business investment in green technologies. If the Government are going to endlessly tinker with this regime, why not do it to benefit green investment? Amendment 61, connected to this, would oblige the Government to publish a review of the CO_2 emissions that result from investment in plant and machinery at the special rate. I urge Members to support this amendment, which is critical to showing us the potential environmental impact of this change, and will allow us to assess what we can achieve by promoting relief through investment in cleaner technology.

According to the Government's own statistics, published in March 2018, carbon dioxide emissions from the business sector accounted for 18% of all emissions in 2017. While there has been a laudable 41% drop in carbon dioxide emissions from the business sector since 1990, we all know that we have to do more, as quickly as possible, to achieve the change that is so urgently needed to avert climate catastrophe. I therefore urge all Members to vote in favour of these amendments, to give us the information we need to get a clear picture of the impact this will have on business, industry and the environment.

Mel Stride: Clause 30 makes changes to ensure that the capital allowances special rate is reduced from 8% to 6% from April 2019. The change will improve the alignment between the rate at which the special rate pool assets were written down for tax purposes and depreciation in business accounts, which is part of the rejoinder to the hon. Gentleman's charge that we are introducing greater complexity. We are actually aligning those rates in a way that will inject some further simplification.

The change made by clause 30 will provide businesses with the same amount of relief overall, but over a longer period. Under the new rate, businesses will receive relief on 50% of the cost of special pool assets within 11 years, compared with eight previously. The vast majority of businesses will be unaffected by the rate reduction, because expenditure on new special pool assets qualifies for the annual investment allowance every year. The temporary increase of the annual investment allowance to £1 million for the next two years will further help businesses to bring forward their investment, and write it off in full in the first year. The change is expected to raise £1.6 billion in revenue over the next six years.

The capital allowances package announced in the 2018 Budget will provide around £1 billion of additional support to businesses over the next six years. That change, combined with the new structures and buildings allowance, will make our capital allowances system more balanced by moving the relief from an area in which the rate was relatively generous to an area in which no relief was previously available.

Amendments 61, 62 and 63 would commit the Government to reviewing the impact of the rate reduction on CO_2 emissions from plant and machinery, the prices of insulation material, household heating and electricity, and the automotive market. The Government have already published a tax information and impact note for the reduction. I assure hon. Members that the careful consideration of impacts is a standard process for all tax policy changes.

The Government's commitment to meet the emissions reductions target has never been stronger. The Climate Change Act 2008 provides a world-leading governance framework, which already ensures that our overall progress is robustly monitored and reported to Parliament. As the hon. Member for Stalybridge and Hyde pointed out, benchmarked against 1990, there has already been significant progress. The Committee on Climate Change provides regular advice to the Government on how best to achieve our targets, and on the impact of existing policies.

3.45 pm

The Office of Gas and Electricity Markets is the Government regulator for gas and electricity markets. It takes account of all factors affecting electricity transmission networks and distribution, including which capital allowances it can claim as part of its normal cost with individual companies. Ofgem can provide information on those markets, including through accessible factsheets, and explanations of the work it does to protect consumer interests.

Amendment 63 seeks a report on the effect of capital allowances on the automotive market. At the Budget, the Chancellor announced a review of the effects of changes in the test procedures for new vehicle CO_2, which will have a much more significant effect on new car sales than the writing-down rate.

Amendment 64 would require the Government to review the impact of the rate reduction on the investment in special rate plant and machinery, where such assets were made before April 2019. The rate reduction will improve the fairness of our capital allowances across various types of asset, which will improve the alignment with average accounts depreciation for the special rate assets. Furthermore, the independent Office for Budget Responsibility estimated that the package of capital allowances measures is expected to increase overall business investment by 0.4% by the end of the scorecard, which supports our economy as a whole.

Amendment 65 would commit the Government to reporting on any consultation on the provisions of this section. As the Government stated in "The new Budget timetable and the tax policy making process" published last year:

> "The government will generally not consult on straightforward rates, allowances and threshold changes"

because they do not benefit from the process. I therefore urge the Committee to reject the amendments. I commend the clause to the Committee.

Jonathan Reynolds: I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 30 ordered to stand part of the Bill.

Clause 31

Temporary increase in annual investment allowance

Jonathan Reynolds: I beg to move amendment 66, in clause 31, page 18, line 4, at end insert—

'(3) The Chancellor of the Exchequer must commission a review on the estimated impact of the provisions of this section and Schedule 12 on the level to which businesses claim annual investment allowance.

(4) The review shall in particular compare the estimated impacts of increasing the annual investment allowance for—

(a) the period specified in subsection (1), and

(b) the period of three years beginning with 1 January 2019.

(5) A report of the review under subsection (3) must be laid before the House of Commons within three months of the passing of this Act.'

This amendment would require the Chancellor of the Exchequer to report on the estimated impact of the provisions of this clause, and compare them to the estimated impact of extending the temporary AIA relief for an additional year.

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

Amendment 67, in clause 31, page 18, line 4, at end insert—

'(3) The Chancellor of the Exchequer must commission a review on the impact of the provisions of this section and Schedule 12 on businesses able to claim annual investment allowance.

(4) A report of the review under subsection (3) must be laid before the House of Commons by 1 April 2020.'

This amendment would require the Chancellor of the Exchequer to review the impact of the provisions of this section and report on that impact by the end of the tax year 2019-20.

Amendment 68, in clause 31, page 18, line 4, at end insert—

'(3) The Chancellor of the Exchequer must commission a review on the costs and benefits of extending the increase in annual investment allowance beyond the period specified in subsection (1).

(4) A report of the review under subsection (3) must be laid before the House of Commons within 3 months of the passing of this Act.'

This amendment would require the Chancellor of the Exchequer to review the costs and benefits of extending the increase in AIA relief beyond two years.

Amendment 69, in clause 31, page 18, line 4, at end insert—

'(3) The Chancellor of the Exchequer must lay before the House of Commons a report on any consultation undertaken on the provisions in this section and Schedule 12 within two months of the passing of this Act.'

This amendment would require the Chancellor of the Exchequer to report on any consultation undertaken on the provisions in this clause.

Amendment 70, in clause 31, page 18, line 4, at end insert—

'(3) The Chancellor of the Exchequer must make a statement to the House of Commons within 2 months of the passing of this Act on the matters specified in subsection (4).

(4) Those matters are—

(a) the results of any analysis undertaken by the Treasury regarding the provisions of this section and Schedule 12,

(b) any evidence that he is aware of that supports the provisions of this section having a positive economic benefit, and

(c) any evidence that he is aware of that does not support the provisions of this section having a positive economic benefit.'

This amendment would require the Chancellor of the Exchequer to make a statement on the evidence base for the temporary AIA increase.

Amendment 71, in clause 31, page 18, line 4, at end insert—

'(3) The Chancellor of the Exchequer must, within 3 months of the passing of this Act, lay before the House of Commons an analysis of the distributional and other effects of the provisions of this section and Schedule 12 on companies of different sizes.'

This amendment would require the Chancellor of the Exchequer to lay before the House of Commons an analysis of the distributional and other effects of the provisions of this section on companies of different sizes.

Clause stand part.

That schedule 12 be the Twelfth schedule to the Bill.

Jonathan Reynolds: I am pleased that we have got on to this clause, which is one of the most substantial in the Bill. As it stands, it will increase the annual investment allowance from a one-off £200,000 to a substantial £1 million for two years.

To be frank, it feels like the limit has been increased to try to lessen some of the damage that has been inflicted on the country by the Government's Brexit negotiating approach, but the constant chopping and changing of such an allowance risks mitigating the benefits of the allowance entirely, because it presents a regime that is impossible for companies to plan around as it is constantly shifting. By my count, the allowance has now changed five times in the 10 years since it was introduced.

The measure is not cheap; it carries a significant up-front cost. The Red Book that accompanied the 2018 Budget estimates that the cost of the allowance will be up to £1.24 billion. Some of that is projected to be recouped in the three years after it is introduced, but there is still £760 million of lost revenue after six years.

The structure of the allowance favours bigger businesses to such an extent that it could penalise small businesses by making it impossible for them to spend even the lower £200,000 allowance. These businesses are unlikely to ever get near to the full £1 million allowance, but they face the ludicrous situation whereby their capacity to use even the pre-existing lower £200,000 allowance will be restricted. This is a complicated point, but I will try to properly explain it.

The legislation has been quite poorly drafted, with a disregard for small companies. The Opposition believe that, with just a simple change via an amendment, it could be easily fixed. However, because of the Government's undemocratic approach, which we have talked about and which has prevented us from tabling substantive amendments, it is actually not possible for us to propose anything other than a review. I will therefore use this speech to urge the Minister to consult the Treasury on implementing a quite simple change to the legislation to prevent it from having the opposite effect to that which was intended.

The annual investment allowance has been subject to numerous tweaks, which is often unhelpful in promoting a regime of certainty and stability. One particular problem posed here is that the allowance has been designated for a very specific period—1 January 2019 to 31 December 2020. However, many companies operate a different

[Jonathan Reynolds]

accounting period, typically in line with the tax year but in some cases with particular dates suited to their specific activities.

The problem that this poses is that the allowance period will not match up with the accounting period. If a company's tax year does not match the fixed timescales of this allowance, there needs to be what is called a straddling calculation for the way the allowance is split over both timescales, because it will change. It will go from being an annual calculation to a daily one. The legislation makes specific provision for this straddling period.

I might need a whiteboard to explain this to the Committee, but I will try my best without one. I have kindly been supplied with a real-world example by a professional body. Imagine if a company with a tax year that ended in March had spent £60,000 just after the allowance period had ended. Owing to the straddling calculation, it would be entitled to relief on only £49,315 of that expenditure, even though the expenditure was well below the existing £200,000 allowance and clearly lower than the new higher limit. Had the company incurred that expenditure evenly throughout the year, or indeed before 1 January 2021, the full expenditure would have been relieved. I may have to put this in writing to the Minister to make it clear.

The simplest way to fix this issue would be to give small businesses the chance, if they wished, to opt out of the new limit, so that they did not get caught between the two periods. We know from HMRC's own statistics that small businesses rarely ever get close to using the full allowance as it stands, let alone needing the new £1 million threshold. It makes no sense to penalise them with a higher rate that they will never be able to utilise.

What consultation was undertaken regarding this measure? This issue should surely have been caught at an earlier stage, or even pre-empted, given that it occurs every time the allowance threshold and periods shift. Given that the regime has been subject to many changes already, the Opposition have tabled amendments requesting a package of reviews that would oblige the Government to disclose the impact on businesses eligible to claim the allowance.

Our amendment 66 requests a review of the estimated impact of the provisions on the level to which businesses are claiming the allowance, assessing the take-up in the different periods to see whether the increase in the allowance is really worth while. Amendment 68 drills down further into the costs and benefits directly, which is essential given the substantial amount of revenue involved in this change. Amendment 69 asks the Government to put before the House a consultation on the provisions within two months of the Bill's passage. This is essential so that we can hear directly from small businesses that will be affected by the point I just raised.

We need to understand, from a distribution perspective, who is taking up this relief and why. We need to know the details of who will use it and how it will benefit them, so that we can properly assess its impact. We also need to correct the change to the thresholds, which seems reasonable, given that businesses have been affected by previous changes and will certainly be affected by this one. I therefore urge all Members to vote for our package of amendments, which will give the Committee the information it needs to make the right call on this substantial and significant change.

Mel Stride: I will deal with two points raised by the hon. Gentleman before I speak more broadly to the amendments under consideration and the clause itself. On the issue of consultation, where we have an additional relieving measure coming in, where one would consult on it well in advance, one would expect the market to see the change coming and, therefore, forestall on activity as a consequence, in order to ensure that it benefited from the reliefs being brought in. For that reason, these kind of measures in general, and this one specifically, would not be appropriate to the kind of consultation that the hon. Gentleman has in mind.

The hon. Gentleman raised the specific issue of the way the straddling arrangements operate. Even in the absence of a whiteboard, he did a pretty good job of explaining the conundrum that he referred to. His example is well made: one could end up in a situation with a relatively limited relief available, because of straddling. However, the answer to that is that one would know about it in advance and, therefore, adjust the arrangement of one's affairs accordingly.

Clause 31 and schedule 12 will temporarily increase, as we know, the AIA limit to £1 million from its current level of £200,000 from 1 January 2019 for two years. The AIA allows businesses to deduct the full cost of qualifying expenditure up to a specified annual limit or cap, where anything above this will be relieved at 18% in successive years. Where businesses spend more than the annual limit, any additional qualifying expenditure will attract relief under the normal capital allowances regime, entering either the main rate or the special rate pool, where it will attract writing-down allowances at the main rate or special rate respectively. This change responds to a consistent ask from business groups such as the Confederation of British Industry, Institute of Directors and the British Chambers of Commerce. The increase will provide a timing benefit, giving businesses 100% first-year relief on qualifying plant and machinery investments up to the value of £1 million.

The changes made by schedule 12 will increase the current AIA amount for two years. It is expected to cost £685 million over the scorecard, with positive returns to the Exchequer from 2021-24. This will provide an incentive for those businesses already spending up to the £200,000 threshold to increase or bring forward their capital expenditure on plant and machinery, by providing a cash flow benefit.

Amendments 66 to 68 and 71 seek a review of the impact of this temporary increase. These reviews would concern the number of businesses affected, the distributional impact, and the cost and impact of extending the increase to three years. By definition, this clause has a positive impact on businesses and business investment, enabling more firms with qualifying plant and machinery expenditure to claim 100% first-year relief. This also makes tax simpler for businesses making qualifying investments up to £1 million, which will not have to account for individual assets.

Much of that information is also available in the tax information and impact note, and policy costings note, published at Budget 2018. These notes include details

on business impacts, including for companies of different sizes, and projected costs of the temporary increase. The change has been limited to two years given our continued need to consider the right balance between our fiscal, tax and spending objectives in order best to support the economy, while keeping debt falling and increasing fiscal resilience. This means maintaining fiscal discipline, which involves decisions such as keeping this higher level of AIA temporary rather than permanent. I therefore urge Opposition Members not to press the amendments.

Amendment 69 would commit the Government to publishing a report on consultation undertaken for this provision. No consultation was undertaken for this temporary change. It is important that this increase begins promptly following any announcement or engagement, in the way that I suggested in my earlier remarks.

Amendment 70 seeks a statement on the evidence base for the economic impact of this change. Prior to the Budget, the Government received representations from a range of businesses and business groups calling for this measure and outlining the positive impact an increase in the AIA amount would have on investment behaviour. Through this increase, the Government are giving even more businesses access to 100% first-year relief. I commend the clause and schedule to the Committee.

Question put, That the amendment be made.

The Committee divided: Ayes 8, Noes 9.

Division No. 17]

AYES

Black, Mhairi
Blackman, Kirsty
Dodds, Anneliese
Dowd, Peter
Lewis, Clive
Reynolds, Jonathan
Smith, Jeff
Sobel, Alex

NOES

Afolami, Bim
Badenoch, Mrs Kemi
Ford, Vicky
Jenrick, Robert
Keegan, Gillian
Lamont, John
Stride, rh Mel
Syms, Sir Robert
Whittaker, Craig

Question accordingly negatived.

Clause 31 ordered to stand part of the Bill.

Schedule 12 agreed to.

Ordered, That further consideration be now adjourned.—*(Craig Whittaker.)*

4.1 pm

Adjourned till Tuesday 4 December at twenty-five minutes past Nine o'clock.

Written evidence reported to the House

FB02d Chartered Institute of Taxation (clauses 50 to 52 —VAT)