PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT
GENERAL COMMITTEES

Public Bill Committee

FINANCE BILL

(Except clauses 1, 4, 8, 189 and 209, schedules 1, 23, and 33 and certain new clauses and new schedules)

Ninth Sitting

Tuesday 12 June 2012

(Morning)

CONTENTS

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Saturday 16 June 2012

STRICT ADHERENCE TO THIS ARRANGEMENT WILL GREATLY FACILITATE THE PROMPT PUBLICATION OF THE BOUND VOLUMES OF PROCEEDINGS IN GENERAL COMMITTEES

The Committee consisted of the following Members:

Chairs: †Mr Peter Bone, Mr Jim Hood

† Baldwin, Harriett *(West Worcestershire)* (Con)
† Barclay, Stephen *(North East Cambridgeshire)* (Con)
† Blenkinsop, Tom *(Middlesbrough South and East Cleveland)* (Lab)
† Burley, Mr Aidan *(Cannock Chase)* (Con)
† Elphicke, Charlie *(Dover)* (Con)
† Garnier, Mark *(Wyre Forest)* (Con)
† Gauke, Mr David *(Exchequer Secretary to the Treasury)*
† Gilmore, Sheila *(Edinburgh East)* (Lab)
Gyimah, Mr Sam *(East Surrey)* (Con)
† Hamilton, Fabian *(Leeds North East)* (Lab)
† Hands, Greg *(Chelsea and Fulham)* (Con)
† Harrington, Richard *(Watford)* (Con)
† Hilling, Julie *(Bolton West)* (Lab)
† Hoban, Mr Mark *(Financial Secretary to the Treasury)*
† Jamieson, Cathy *(Kilmarnock and Loudoun)* (Lab/Co-op)
† Kirby, Simon *(Brighton, Kemptown)* (Con)
† Lavery, Ian *(Wansbeck)* (Lab)
† McKenzie, Mr Iain *(Inverclyde)* (Lab)
† McKinnell, Catherine *(Newcastle upon Tyne North)* (Lab)
† Malhotra, Seema *(Feltham and Heston)* (Lab/Co-op)
† Mann, John *(Bassetlaw)* (Lab)
† Mearns, Ian *(Gateshead)* (Lab)
† Mills, Nigel *(Amber Valley)* (Con)
† Morrice, Graeme *(Livingston)* (Lab)
† Morris, Grahame M. *(Easington)* (Lab)
† Pugh, John *(Southport)* (LD)
† Rees-Mogg, Jacob *(North East Somerset)* (Con)
† Reeves, Rachel *(Leeds West)* (Lab)
† Smith, Miss Chloe *(Economic Secretary to the Treasury)*
† Swales, Ian *(Redcar)* (LD)
† Syms, Mr Robert *(Poole)* (Con)
Williams, Stephen *(Bristol West)* (LD)
† Williamson, Gavin *(South Staffordshire)* (Con)
Wilson, Sammy *(East Antrim)* (DUP)

Simon Patrick, James Rhys, *Committee Clerks*

† attended the Committee

Public Bill Committee

Tuesday 12 June 2012

(Morning)

[Mr Peter Bone *in the Chair*]

Finance Bill

(Except clauses 1, 4, 8, 189 and 209, schedules 1, 23 and 33 and certain new clauses and new schedules)

Clause 18

Qualifying time deposits

10.30 am

Catherine McKinnell (Newcastle upon Tyne North) (Lab): I beg to move amendment 23, in clause 18, page 11, line 30, at end add—

'(3) HM Revenue and Customs shall draw up plans to ensure that investors who are eligible to receive interest payments gross are made aware of the need to register with their account provider, to ensure that they do not overpay income tax.'.

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

Catherine McKinnell: It is a pleasure to serve under your chairmanship today, Mr Bone.

Clause 18 relates to qualifying time deposits and will take effect from this financial year. Prior to the Bill, individuals who invested in qualifying time deposits were paid interest gross and they—or their accountants acting on their behalf—made the appropriate arrangements for paying the tax due to Her Majesty's Revenue and Customs. The clause means that account providers—banks and building societies—will instead deduct sums representing income tax at source from anyone investing in a new qualifying time deposit on or after 6 April 2012, and those deductions will be paid directly to HMRC.

The provision will align tax collection arrangements for qualifying time deposits with those already in operation for many comparable savings or investment products. It will also reduce the burden on individual taxpayers, which is a worthy aim that we support. It also means that more of the tax due on savings income will be collected by the Revenue. As the impact note states, that could bring in as much as £40 million a year in additional Exchequer revenues, which is again something that we support.

Fewer investors will be eligible to receive interest payments gross than would have been if the qualifying time deposits exemption had remained. Those who are eligible to receive interest payments gross will need to complete form R85. Will the Minister clarify what estimate has been made of the number of individuals likely to invest in a qualifying time deposit in the financial year 2012, and how much that estimate may have been reduced by the removal of the qualifying time deposits exemption?

It is important that those investing in qualifying time deposits and other investors who are eligible to receive interest payments gross are made aware of the need to register with their account provider, so that they do not overpay income tax. It is obviously in everybody's interests that people do not overpay income tax. I am sure that the Minister has seen the result of the freedom of information request—it was widely reported in the media yesterday—which showed some of the frustrations that can occur when tax calculation mistakes are made. That is why our amendment calls on HMRC to draw up plans to raise awareness of the change. Is a basic communication plan in place for basic rate taxpayers who will be affected by the change in their tax code?

The Low Incomes Tax Reform Group has looked at the problem and has noted that it is especially an issue for pensioners. I know that the Exchequer Secretary is aware of the scale of the problem of the overtaxing of pensioners' savings. In a previous Finance Bill debate, he referred to the pensioner "Taxback" project, which repaid 50,000 pensioners some £20 million in 2005. The bereavement helpline has recently been introduced and has been warmly welcomed. It is already assisting people, and we hope that it will do so much more in future. The £3 billion tax bill for pensioners that will result from the unfair granny tax, on which a U-turn is not as yet proposed, will make it even more important that they do not overpay on their savings tax. Is HMRC doing enough to ensure that those people do not overpay?

The Low Incomes Tax Reform Group makes recommendations that would go some way to improving the situation, and I would be grateful for the Minister's comments on them. First, it suggests that HMRC should encourage banks and building societies to provide information to taxpayers more proactively about the possibility of registering R85s. It also suggests that all deposit-takers stock up-to-date copies of the form and help sheet to give to customers on request. Secondly, it believes that it would be helpful if deposit-takers automatically issued certificates of tax deducted to taxpayers, without having to be asked. Thirdly, it suggests that HMRC's "Taxback" campaigns do not go far enough. Instead, it makes the case for HMRC to engage further with stakeholders in looking at the information that people get from deposit-takers about interest and tax deductions at source, and how that can be matched to individual taxpayer records, so that refunds can be automated.

There is already a proposal in the Budget to issue new personal tax statements, which will detail income tax and national insurance contributions paid, average tax rates and how that contributes to public spending. It is thought that if savings income and tax deducted at source is not included, the statements would be incomplete and misleading. I shall be interested to hear from the Minister on what proposals there are to match all those tax sources together within that proposed statement.

We support HMRC's customer commitment to ensure that taxpayers pay the right amount of tax. I am sure that the Minister will agree that taking action to strengthen that commitment would be welcome. For that reason, I ask hon. Members to support our amendment.

John Mann (Bassetlaw) (Lab): It is a pleasure, Mr Bone, to be back here after the recess, under your exuberant chairmanship. It is good to see the Government Whip here on time for the new mini-Session, together with a full team of Ministers—I spotted all three a minute or two ago. It is good to see that they remain busy, U-turns, of course, taking up a considerable amount of their time. *[Interruption.]* We do indeed now have the full team of three Treasury Ministers.

There will be plenty of opportunities this morning for more U-turns. Here we have another one. I know that U-turns are in fashion—*[Interruption.]* In vogue, as my hon. Friend the Member for Newcastle upon Tyne North says. The next U-turn will concern pensioners, the Government having dealt with caravans, charities and pasties. This proposal is a modest start to a series of U-turns that we expect the Government to make, because, more than anyone else, the Budget hits pensioners. Here is a modest opportunity. I look again at the ranks of the Government Back Benchers: does any of those sincere hon. Members wish not to vote for this amendment, which would encourage, indeed allow, fewer people to overpay income tax unnecessarily? The majority of those people are pensioners. Can there be any reasonable person in this room who would say to a pensioner, "We are not prepared to assist you; we will allow you to overpay income tax, and then taxpayers will pay officials to correct those mistakes"? That is not logical.

My hon. Friend the Member for Newcastle upon Tyne North aptly and eloquently outlined a modest little suggestion that would aid the taxpayer, Government and pensioners. Can it be possible that the Government are so nervous about the suggestion of a further U-turn, when we all know that there will have to be further U-turns on pensions, not least draw-down pensions? Those are not the subject of the amendment, so I will not go into them, but they are part of the Budget's victimisation of pensioners above all others. Looking at the faces of Opposition Members and even Liberals who have made it here today—

Mark Garnier (Wyre Forest) (Con): Government Members; you are the Opposition.

John Mann: Are we? I am jumping two years ahead of myself. The Opposition are getting more confident these days. When I look into the eyes of Government Back Benchers, I can see that they want to support the amendment. They know it is right and sensible. I suspect that Ministers will accept the proposal, knowing that it will cut bureaucracy and red tape, minimise public expenditure and help British pensioners not to overpay tax.

Seema Malhotra (Feltham and Heston) (Lab/Co-op): It is a pleasure to serve under your chairmanship, Mr Bone. Does my hon. Friend agree that making tax processes as simple as possible is about not only providing good service to the citizen, but ensuring that people do not incur unnecessary cost? The average time that people wait for HMRC to answer a call has risen from one minute and 53 seconds in 2009 to five minutes and 45 seconds. People have to pay for those calls, so pensioners will have to pay to get advice when the system could have been made simpler for them.

John Mann: My hon. Friend makes an excellent point, which I had not considered. Today's weather must have fuzzied my brain when I was thinking through the matter. She rightly points out that in addition to the problems I have outlined, people will have to pay to hang on the phone. We live in a complex, intricate world and we all agree that making it simpler for the British citizen, and particularly for the British pensioner, is a good thing. Here is the opportunity to do that.

Jacob Rees-Mogg (North East Somerset) (Con): The hon. Gentleman is being a bit mealy-mouthed. Should we not go a good deal further and get rid of tax on savings below the inflation rate, and get rid of tax deduction at source? That is an area where the Government's convenience is better served than Her Majesty's subjects.

John Mann: I would not say that you are giving me the evil eye, Mr Bone, but I can see from the glint in your eye that I should not stray too far into that territory. I will simply say that I have put forward proposals during the past six or seven years relating to pensioners and taxation. I look at how, in my constituency, hard-working former coal miners and textile workers with pensions are taxed, and see how unfair that is. The hon. Member for North East Somerset and I should get our heads together and come forward with a cross-party proposal to persuade the decision makers in Government. I will have to persuade my Front Bench—I will leave the Liberals to him—of the common sense of what he is suggesting.

We are beginning to reach consensus on the U-turns that are required, which is good news. I look forward to this overly modest proposal being adopted. The Government's plans will, as my hon. Friend the Member for Feltham and Heston said, cost pensioners money, waste their time and cause them the inconvenience and distress of waiting on the phone at their expense. Here is an opportunity to do things sensibly; can the Government resist?

10.45 am

The Financial Secretary to the Treasury (Mr Mark Hoban): Yes is the answer, Mr Bone. It is a pleasure to serve under your chairmanship. I am glad that the recess has re-invigorated the hon. Member for Bassetlaw and that he has come back full of vim and vigour.

The measure is relatively straightforward, as the hon. Member for Newcastle upon Tyne North pointed out. Qualifying time deposits are savings and investment products in which, among other criteria, a single deposit of at least £50,000 is invested for up to five years. The latest estimate is that up to 30,000 individuals hold such deposits, and the hon. Lady was right to say that the clause applies to new deposits. It is not clear yet what the clause's behavioural impact will be, but clearly, for some taxpayers, having interest paid gross will be beneficial, and the fact that tax will now be deducted at source, at the basic rate, may mean that some people look to other forms of savings. The clause will ensure that income earned on qualifying time deposits is subject to tax in the normal way, so it does not create a new tax burden; it merely simplifies arrangements for tax collection on qualifying time deposits.

[Mr Mark Hoban]

We have made the change by removing qualifying time deposits opened or made by individuals after 6 April 2012 from the list of exemptions to the general principle that banks, building societies and other financial institutions should deduct tax at source from the interest that they pay to customers. As a result, tax will be deducted from the deposits at the basic rate under the tax deduction scheme for interest.

The clause brings qualifying time deposits in line with other comparable products, removing any requirement for basic rate taxpayers to notify HMRC separately of tax that is due on their interest. Investors in qualifying time deposits who are not eligible to pay tax on their savings income—for example, because their total income is below the personal tax-free allowance—can register with their provider to continue to receive interest without tax being deducted.

Amendment 23 would commit HMRC to ensuring that eligible investors are made aware of the need to register with their account provider in order to receive interest without tax being deducted, but such a change is unnecessary. HRMC already takes a range of steps to make eligible savers aware of how they can register to receive interest tax-free. Specific help and guidance on that point can be accessed from HMRC's website or through contact centres, and HMRC produces a help sheet on how to register for gross interest, as well as a tax checker that allows savers to calculate whether they are eligible to register. Additional help is also available through the Money Advice Service.

The hon. Lady also referred to the Low Incomes Tax Reform Group's suggestion that banks and account providers should play a more proactive role, and she is right. They have regular contact with savers and make account information available to their customers. I know that many account providers make considerable efforts to inform eligible customers of how to register to receive interest gross, and I encourage them to continue to do so.

A project under the previous Government attempted to raise the profile of the issue. In 2009, the "Taxback" campaign had mixed results. There was a risk that a letter telling a person that they might be eligible to receive interest gross could create further confusion. In fact, many calls received in response to the "Taxback" campaign, which was targeted at recipients of pension credit, were from people telling HMRC that they already received their interest gross, or people asking not to be contacted again. Although I am keen to ensure that HRMC helps savers to understand whether they are eligible for gross interest and how they might register, it is right that the interventions should be more targeted and cost-effective.

The hon. Lady asked about the personal tax statements that we will introduce. The intention is to capture all sources of income; again, that will help to raise the issue's profile and ensure that as many people as possible register to receive their interest income gross. I hope that the hon. Lady is reassured that work is being done to encourage the people who are not eligible to pay income tax to register to receive their interest income gross. HMRC and the Money Advice Service can help with that. Account providers, as the hon. Lady said, have an important role to play in this.

Catherine McKinnell: I imagine that Labour Members are not particularly reassured by the Minister's comments. My hon. Friend the Member for Bassetlaw set out, in a rational argument, why the amendment is reasonable. It asks the Government to

"draw up plans to ensure that investors who are eligible to receive interest payments gross are aware of the need to register with their account provider".

The message that we are getting loud and clear from the public is that they want to see proactivity from HMRC. They expect a decent service from the organisation, and they want to avoid a situation in which they have to contact HMRC to try to rectify mistakes after they have occurred, because the time it is taking members of the public to do that is getting longer, not shorter. On that basis, it seems sensible to suggest that the Government "ensure"—that is the key word in the amendment—that they engage with providers to make sure that mistakes and overpayments do not occur, and that steps are taken before the change to make sure that savers are aware of the implications for their tax position, so that they do not have to reclaim overpayments, but instead can pay the correct amount from the start. For that reason, I urge members of the Committee to support our amendment.

Question put, That the amendment be made.

The Committee divided: Ayes 12, Noes 17.

Division No. 9]

AYES

Blenkinsop, Tom	Malhotra, Seema
Gilmore, Sheila	Mann, John
Jamieson, Cathy	Mearns, Ian
Lavery, Ian	Morrice, Graeme *(Livingston)*
McKenzie, Mr Iain	Morris, Grahame M. *(Easington)*
McKinnell, Catherine	Reeves, Rachel

NOES

Baldwin, Harriett	Kirby, Simon
Barclay, Stephen	Mills, Nigel
Burley, Mr Aidan	Pugh, John
Elphicke, Charlie	Rees-Mogg, Jacob
Garnier, Mark	Smith, Miss Chloe
Gauke, Mr David	Swales, Ian
Hands, Greg	Syms, Mr Robert
Harrington, Richard	Williamson, Gavin
Hoban, Mr Mark	

Question accordingly negatived.

Clause 18 ordered to stand part of the Bill.

Clause 19

PROFITS ARISING FROM THE EXPLOITATION OF PATENTS ETC

Catherine McKinnell: I beg to move amendment 24, in clause 19, page 11, line 36, at end add—

'(2) The Chancellor of the Exchequer shall review the impact of this provision on businesses and shall consider where there are other opportunities to introduce targeted support for business. A copy of the report shall be placed in the House of Commons Library.'.

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

Clause stand part.

That schedule 2 be the Second schedule to the Bill.

Catherine McKinnell: Before the recess, we thought that the dust had settled on this year's Budget, and that we would be debating the intricacies of the changes being made by this Finance Bill. However, over the recess we learned of not one, or two, but three U-turns, and a 90° turn that has been described recently as a clarification. This has left the public in quite a spin. Now that there has been a welcome reversal of the pasty tax, the caravan tax and the charities tax, as well as clarification on the skip tax, we wait in hope of an announcement of the removal of the granny tax and, most of all, a reversal of the tax cut of £40,000 for 14,000 millionaires.

One measure in this Budget that is certainly welcome, and which we hope will not be followed by any U-turn, is covered by the clause and our amendment. Indeed, it is an idea that was introduced by the Labour Government, which is why, viewed in the light of the chaos and confusion created by the Chancellor's Budget, his attempts at attributing GlaxoSmithKline's decision to build its first UK factory in 40 years to his shambles of a Budget seemed at the time, and certainly seems now, rather ludicrous.

Let me remind hon. Members of the Chancellor's comments on the BBC's "Breakfast" programme the morning after the Budget announcement:

"You have GlaxoSmithKline, one of the world's biggest companies, one of the great British success stories, saying the Budget has changed their view of Britain as a place to invest. They're going to create 1,000 jobs here. Now, surely my responsibility as the country's Chancellor is to get the economy moving, to get jobs created, and when big companies say that about Britain, people should sit up and notice that we are changing the British economy for the better."

I do not think that leading the country into a double dip recession was quite what the Chancellor had in mind when he made those comments. Clearly the news that GlaxoSmithKline was to build its first new UK factory in 40 years and in doing so create 1,000 much needed jobs is warmly welcomed, but it was Labour's proposal that gave GlaxoSmithKline the confidence to invest and create these jobs. In 2009, following the Labour Government's pre-Budget report, its chief executive officer welcomed the idea of the patent box, saying:

"The patent box is exactly the sort of active, long-term and creative support that we need from the Government to ensure that the UK remains an attractive place for highly skilled sectors such as pharmaceuticals. For GSK, assuming the new regime will apply to patents currently under development it will have the immediate impact of making the UK a priority area for future investments".

A year later, GlaxoSmithKline confirmed that the successful implementation of the patent box would ensure that the UK was the location for its next biopharmaceutical manufacturing plant. In our 2009 Budget, the Labour Government set in motion the idea of the patent box as a way of encouraging innovative activity. The industrial activism clearly worked, and I would welcome the Minister's estimate of the number of jobs, in addition to those announced by GlaxoSmithKline, that he thinks could be attributable to Labour's patent box. That is the first part of our amendment.

The amendment goes on to urge the Chancellor and the Government to look at how they can support business in a more targeted way. From my reading of this year's Budget, there were just two measures along the lines of targeted support for businesses. The first—the patent box—was the previous Labour Government's idea, as was the second: tax relief for the video games industry to be legislated for in 2013. While hugely supportive of the announcement, the video games industry must also be scratching its head at how quickly the Chancellor turns.

11 am

In the Chancellor's first Budget, he announced the scrapping of Labour's plans for a tax relief for the video games industry. Developers had previously heralded those plans as inspired. In our last Budget before we left office, we set out plans to introduce the relief, but the Chancellor scrapped them in 2010, saying that that tax break was poorly targeted. If we fast-forward to the March Budget this year, the Chancellor re-announced Labour's policy of two years ago, claiming it as an effective way to support the video games industry.

Cathy Jamieson (Kilmarnock and Loudoun) (Lab/Co-op): Does my hon. Friend find it all the more astonishing that the Scottish Affairs Committee undertook an inquiry into the issue and made recommendations to the Government? They did not take up those recommendations at the time, only to U-turn later.

Catherine McKinnell: Indeed, that is shocking, and I shall describe some of the reaction from the industry when the initial proposal was scrapped. The research was ignored—it was dismissed, as it was clearly not considered relevant—yet there was a U-turn not two months later, but two years later. That U-turn is welcome all the same, but it prompts the question whether the Chancellor did his homework in the first place, in listening to experts in the field who know what the industry now needs to encourage investment.

Sheila Gilmore (Edinburgh East) (Lab): It is a pleasure to serve under your chairmanship, Mr Bone.

Has my hon. Friend considered whether and to what degree the Government have assessed the damage done to the industry, which is so important to places such as Dundee in Scotland, by the decision not to give it the relief over that period? Obviously, we are pleased that the relief will now be given.

Catherine McKinnell: My hon. Friend makes an important point. I was about to put that question to the Minister. Two issues should be considered. First, how many investors or potential developers, having had the good news that they would receive support and a tax relief on investment and then having been told that such a relief was poorly targeted and would be scrapped, have failed to go ahead with their projected plans? Do the Government have any indication of the numbers involved?

Secondly, there is the broader issue of business confidence—of confidence in this Chancellor and this Government, in promises made that are then broken and in policies made that are then reversed. To what extent can the fact that business is sitting on investment at the moment and not investing, as a result of which we

[Catherine McKinnell]

are in a double-dip recession, be attributed to the uncertainty created by our very own Treasury? That prompts this question: what are the Government doing proactively to propose ideas that will inspire confidence in industry?

Will such promises be delivered? The second part of the amendment would require the Chancellor to consider "other opportunities to introduce targeted support for business." He would also have to place a copy of his report in the House of Commons Library. The business community is crying out for not only stability, but investment. Rapid U-turns and shifts in policies are creating uncertainty and, I have no doubt, are stalling the investment that this economy so desperately needs.

The Government should not underestimate the uncertainty that such flip-flopping can cause. On hearing the news last year that the Government would not go ahead with the tax-relief plans, The Independent Games Developers Association, the trade association representing the video games industry, called the Chancellor's announcement a "betrayal". The director general of the Entertainment and Leisure Software Publishers Association said,

"It's a terrible blow. Our industry will be rightly puzzled as to how tax breaks can be lauded before an election, only to be seen as 'poorly targeted' and scrapped just six weeks later."

I would be grateful if the Minister could estimate the number of developers who lost out as a result of that decision. Is there a way to estimate how much investment was lost in the period of uncertainty between the announcement that scrapped the incentive and the recent announcement that it is likely to be re-introduced next year?

Will the Minister confirm whether there are other areas where the Government are considering introducing targeted support for businesses? The message from businesses is that they are struggling—they are struggling to borrow from the banks; they are struggling to get investment from the £754 billion currently being sat on by businesses. The Committee has heard how the forecasts for growth and business investment have been slashed by the Office for Budget Responsibility; they are down from an 8.9% growth forecast in 2011 to the most recent and far more sombre forecast of 0.7% growth. It remains to be seen whether that forecast is also not over-stating reality, given the double-dip recession that the Government led us into.

The Government must take steps and the purpose of the amendment is to assist them in that. They need to instil confidence and provide incentives for businesses to start investing. Labour's patent box is a welcome measure in the Budget, but the Government can do much more to look for opportunities for a more targeted approach. Knowing that the Government are behind an industry or technology can reduce uncertainty and promote confidence and, most of all, investment. The amendment hopes to change the tide of events currently pursued by the country. I urge hon. Members to support it.

Nigel Mills (Amber Valley) (Con): It is a pleasure to serve under your chairmanship, Mr Bone. I rise to speak not on the amendment but on the clause stand part debate on this welcome measure; it is testimony to exactly how Government should respond to lobbying. There was clearly a lot of concern in the pharmaceutical industry, mainly that there were many disincentives against holding intellectual property in the UK. We saw tax being lost as new drugs ended up being owned off-shore.

We have ended up with a wide-ranging relief that applies not only to the pharmaceutical industry but to every industry that uses or registers patents. That is the right way to respond, rather than focusing on one particular industry where we see a problem. It may have been more charitable to refer to this as the "patent capsule", as a tribute to the industry that generated it. We have here a sensible and welcome proposal that I happily accept was originally talked about under the Labour Government, but has been brought forward and funded by the current Government. We want to see this come into operation and work.

I have a few questions on the detail. Why do we not have some detail? What sounds like a simple idea to let companies with profits from patents be taxed on that income at 10% has turned into about 40 pages of legislation and 80 pages of guidance. I suspect that is due to a fear that businesses will try to refresh every old patent or try to get every pound of income they possibly can into this net to reduce their corporation tax. We have had to go through a series of legislative steps to determine how we calculate IP profit, what expenses have to be there and what avoidance arrangements there are.

There are a few things that merit clarification. Perhaps the Minister could first help me with how exactly we apportion income. Say I am selling a car. I suspect that the patent on most bits of a car expired a long time ago, but if I have a patent on a new braking system and I can sell the car for £20,000 and make a whacking profit, does the fact that I have a patent on a small part of the thing I am selling mean that all the profit I get is in this lower tax rate? Alternatively, must I apportion the fact that most of the car's technology is no longer covered by patent—at least not one that I hold—and is only the relatively small premium I can get from that new braking component covered? I assume that the second case would apply, but I could not quite work out how, through all the apportionments in the Bill, I would get to that if I owned all the IP for the car completely.

My second area of concern is the anti-avoidance rules at paragraph 357F in the schedule. Paragraph 6.1.2 of the guidance published by the Treasury effectively lists a whole load of situations where the anti-avoidance rules would not be applied. Most of them are perfectly sensible, but I am a little concerned that we are already issuing guidance that says that there are some situations that we do not mean to be caught by the legislation and which the Revenue can take away by guidance—particularly, for example, transferring qualifying IP into the UK.

We clearly want people to bring qualifying IP into the UK so we get the tax benefits from it. That is, I suspect, part of the idea of this scheme. Yet as the anti-avoidance provisions are drafted, that would not be allowed and people would not be allowed to get the 10% tax rate if they did that. The Revenue is having to clarify and take that out in guidance.

It would probably have been better to have had some of those things listed in the Bill rather than in guidance. Most of the things there are relatively sensible. Companies would not expect to make an election to trip them into the anti-avoidance legislation; I should be a little surprised

if that was an interpretation. The drafting of the anti-avoidance clause at paragraph 357FB(1)(c) catches people if their main purpose in being party to a scheme is

"to obtain the chance of securing a relevant tax advantage."

We are lowering that threshold; it used to refer to being party to a scheme to secure the advantage, not to have a go at securing it. Presumably if people do not secure it, they do not need to be in the anti-avoidance section—they have already been caught.

Finally, a lot of the industries we are trying to encourage as part of generating growth probably do not get to register patents for the valuable IP they produce. I clearly accept that we would not want to incentivise trademarks or marketing intangibles. But it is clear from the shadow Minister's comments that there are important growth industries that are producing complicated pieces of computer software in code. As I understand it, it is not possible to have a patent on software or code under UK laws, but in the US and some other places it is possible to patent code.

Those businesses will not be eligible for the relief and that might be one of the reasons why we have to go for a targeted thing separately. Once the legislation is working effectively, are the Government prepared to consider whether there are other types of IP we should bring in to encourage that activity and get those valuable assets in the UK that we so desperately need to grow our economy and also to protect our taxpayers?

John Pugh (Southport) (LD): The Labour party's amendment as a demand is quite legitimate, and we should find out what exactly the Government intend to do through the measures they are adopting. I generally support a review of measures, particularly measures like tax exemption for things like video games: I just think that the Government are not necessarily the appropriate body half the time to do it.

I should like to refer briefly to the case raised by the hon. Member for Newcastle upon Tyne North. The video games industry was a very interesting debate at the time. There were Adjournment debates on it. As I understand it, the case was not overwhelmingly made that should the relief end, all businesses would go off to Canada or wherever simply because there was insufficient evidence. I had a personal interest in it because I was surprised by the number of small video games designers in my constituency and scattered throughout the Merseyside area.

There was a general presumption against exemptions for particular industries simply because it adds to tax complexity. A general case can be made for trying to avoid exemptions wherever possible. That seemed to be the line that the Treasury was pursuing; it simply did not see the need. One gets into analogous discussions where people argue that tax exemptions must be given to wealth creators. Other people—usually on the Labour side—say that such exemptions are completely unnecessary because the effect that the Government fear, namely that the wealth creators will decamp, will not transpire. Similar debates take place about the pharmaceutical industry.

11.15 am

Such things cannot be known a priori; they can be known only from data and evidence. The Government have had the data on the video games industry, the evidence is there and they have responded as we would expect them to. That is evidence-led policy. When the Government initiated the change, it was not possible to say in advance whether it would have the effect that it did, but now that the Government have the evidence and have responded appropriately, we have to welcome the outcome.

The Exchequer Secretary to the Treasury (Mr David Gauke): It is a pleasure to serve under your chairmanship once again, Mr Bone. Clause 19 introduces the patent box. The patent box will apply a reduced 10% rate of corporation tax to profits from patents and related types of intellectual property. The patent box will help to maintain the UK's position as a world leader in patented technologies and encourage companies to locate high-value jobs associated with patents here.

Encouraging businesses to develop and use their patents will play a key part in supporting a strong and growing private sector. Clause 19 and schedule 2 could benefit up to 5,000 of our most innovative companies. They will benefit a wide range of sectors, particularly high-tech industries such as life sciences, manufacturing, electronics and defence. They are equally applicable to the smallest and to the largest companies.

The patent box will benefit active, innovative businesses that hold or exclusively license patents. Companies must have developed the patent themselves or be actively managing it in order to be eligible for the patent box. Companies can benefit however they choose to use the patents in their business. The technology can be licensed, included in patented products, or used in internal processes or to provide services.

Companies will be able to apply the 10% patent box rate to profits that are attributable to patents, but not to profits that are attributable to routine activities or to commercial brands. For many companies, the rules allow a largely formulaic approach to simplify the potentially difficult task of determining patent profits. This should improve certainty and minimise administrative burdens. My hon. Friend the Member for Amber Valley asked what would happen in the case of a car, an element of which related to a patent. All turnover from the car would be included, but a routine profit element would be excluded—10% on certain costs—as would a marketing return profit. Not all the profit on such a car would be included, therefore, but there would be an amount to reward the technological innovation and intellectual property in the patent.

The patent box will be phased in over five years from 1 April 2013, with the full benefits available from April 2017. It is expected to cost £350 million in the first year, rising to £960 million in steady state.

I will also outline for the Committee future changes. To qualify, the patent must have been granted by the UK or European patent office. Schedule 2 includes a power to include patents granted by the patent offices of other EEA countries. A statutory instrument will be introduced before April 2013 under the negative procedure to include patents from EU countries with similar patentability criteria and patent examination processes to the UK. A draft has been provided to the House.

Powers are also included to permit the Treasury to make consequential changes as a result of changes in EU or national law relating to patents and other qualifying rights; to adjust the definitions for the types of expenses

[Mr David Gauke]

used to calculate the excluded routine profits of the company; and to update references to international standards for calculating tax profits. The powers will be used to keep the regime up to date and to provide additional clarity if required. We will also keep the regime under review to ensure that it is benefiting business in the way intended, and we will take appropriate action if aggressive attempts are made to exploit it for tax avoidance.

Amendment 24 proposes that the Government publish a review of the impact of the patent box on business and of opportunities to introduce other targeted support for business. As I have discussed in relation to clauses 5 and 6 on corporation tax rates, the Government continue to prioritise reforms to the corporation tax system as part of their action to repair the UK's model of economic growth. It is because the private sector is critical to the economic recovery and tackling the deficit that the UK must demonstrate that it is open for business.

The Government have taken action to improve the UK's tax competitiveness in a number of areas. This action includes reductions in the main rate of corporation tax, which will benefit all companies; reform of the controlled foreign companies regime; and introducing an above-the-line research and development tax credit, which will support further R and D investment in the UK by improving the visibility and certainty of the credit. The patent box is also a key part of that commitment.

In November 2010, the Government published the corporate tax road map, which set out a five-year plan for the Government's approach to reform of the corporate tax system. The proposals were subject to open and transparent consultation with business. The Government have helped to provide stability by delivering the reforms to the timetable first set out 18 months ago in the road map. It is the Government's view that, in general, a low corporation tax rate with fewer reliefs and allowances will provide the best incentive for business investment, with the fewest distortions. The corporate tax road map has given certainty to business that the tax system will be stable, and therefore the Government are not intending to make any further significant changes at this time. Producing another report on introducing further targeted reliefs is therefore unnecessary.

The Government also routinely publish detailed information on the corporation tax system: HMRC publishes detailed statistics on corporation tax receipts; the OBR publishes information on the corporation tax forecast in its economic and fiscal outlook; and, at Budget, HMRC publishes detailed information on proposed changes, in particular tax information and impact notes and the policy costings document.

HMRC's existing arrangements will ensure that the impact of the patent box is effectively monitored. This will include capturing data on the level of uptake of the regime and the benefits that the regime delivers to business. However, full information covering the impact of the regime will not be available for several years. The immediate impact is clear from the reactions of business to the introduction of the regime.

I am delighted that already the introduction of the patent box has resulted in £500 million of investment by GSK, including a new manufacturing plant in Cumbria and generating about a thousand new jobs. GSK's announcement of its intention to invest was first made in November 2010 in response to the corporation tax road map, not in 2009 when the previous Government announced the patent box. It was, after all, contingent on the successful design of the regime: something that we have been able to deliver.

John Pugh: The Minister mentioned that the regime will be monitored. Will information be publicly available as a result of the monitoring process?

Mr Gauke: The information that we obtain through monitoring the regime can be made available through the usual means. We will be happy to share information with hon. Members who are able to obtain information through parliamentary questions and so on. We will certainly give consideration as to how that information can be best shared. I appreciate my hon. Friend's interest in this area. I welcome the chance to discuss the issues raised in the amendment. I do not think there is a case for the Government to produce a further separate report on these subjects.

The hon. Member for Newcastle upon Tyne North remarked that the previous Government made an announcement in the run-up to the 2010 general election, and therefore the previous Government should take all the credit for the announcement that GSK, for example, is investing in Cumbria. I am struck by how often we hear arguments that, notwithstanding the desperate state of the public finances that we inherited and the unbalanced economy, the previous Government can accept no blame for the existing difficult economic conditions. I am interested, however, that in the context of the patent box—a policy announcement that was some distance away from having a developed, implementable regime—the previous Government take the credit.

During the process, significant changes have been made to the original proposal to ensure that the regime is competitive and cost-effective. The Government have conducted extensive consultation on the patent box, and there has been very positive engagement with business and representative bodies on all aspects of the policy design. The final provisions have been warmly welcomed. I am pleased that Opposition Members support the patent box's introduction and that they agree that it will encourage innovative businesses to invest in the UK. It is, however, stretching it a little for the previous Government to take all the credit for the proposals.

In terms of the impact, figures from the Institute for Fiscal Studies show that the patent box will lead to more than double the number of patents being held in the UK. The specific design of the patent box has been developed with considerable input from businesses during the consultation to ensure that the final regime is practical and competitive, and we hope that it will be warmly welcomed.

My hon. Friend the Member for Amber Valley asked whether the provisions should be extended to other forms of intellectual property. A broader box would be very expensive. Most companies hold some kind of intangible assets, and cutting the main rate of corporation tax has been our general focus. Given the state of the public finances, decisions must be made about where the impact can be most useful. Copyright, for example, is automatic on all written material and no inventive

step is required. It is therefore difficult to use copyright as a market innovation in the same way as patents. We must bear in mind that this area is competitive and that capital is mobile, so it is important that the UK is as competitive as possible.

The hon. Member for Newcastle upon Tyne North made a point about the tax reliefs announced for the creative industries, including video games. The Budget stated that three creative sector reliefs will be introduced in 2013, and those measures are designed to incentivise investment. Generally, as I have said, the Government have adopted the corporation tax system with a lower rate and a broader base, but in respect of the reliefs, evidence has been provided showing that market failures exist. Internationally, there has been a move towards introducing such reliefs, as it is a very competitive area. Although it may be the case that the previous Government announced the introduction of a relief for video games, when we arrived in government in 2010, little work had been done or evidence collated to support such a relief. That work has now been undertaken, which is why the decision has been made for targeted reliefs to be introduced for three creative sectors—high-end television, animation and video games.

I am glad that the patent box has widespread support. It will encourage innovative business to invest in the UK and locate high-value jobs and activity here, as well as enhancing the competitiveness of the UK tax system for high-tech companies. I am delighted that the clause is part of the Bill.

11.30 am

Catherine McKinnell: Once again, the Minister's comments are deeply concerning, in terms of the complacency with which this Government seem to view this country's economic situation. Moreover, we are in a double-dip recession, the economy is not growing, and serious action needs to be taken to try to stimulate growth.

I accept the Minister's warm welcome and praise for the patent box initiative. I also welcome the probing questions that the hon. Member for Amber Valley asked about the technicalities, and the implications of the patent box for businesses, in order to ensure that, before the Bill is passed, the Government iron out any issues. Our amendment focuses on the impact of the provision, which the Minister said will be available, in due course, on an ongoing basis. My hon. Friends and I accept that, but he seems to dismiss the requirement to consider

"other opportunities to introduce targeted support for business."

Our point is that the Government have introduced the ideas and suggestions advanced by the previous Labour Government, but have so far come up with very few suggestions on how to stimulate growth in the economy.

Mr Gauke: Will the hon. Lady clarify her position? She will be aware that the main rate of corporation tax has fallen from 28%, which was what we inherited, to 22%, which helps all businesses that pay the main rate of corporation tax. Is she saying that she would prefer us not to have done that? Would she prefer us to provide more targeted reliefs to help specific sectors, rather than make a general reduction in corporation tax?

Catherine McKinnell: I have two comments to make. First, we have not seen that reduction yet; it will be made over several years, and its impact has yet to be felt. We are in a double-dip recession. Those are the economic facts. Secondly, we have discussed at length Opposition concerns that this Government and Chancellor seem to approach the economy as a one-club golfer: corporation tax cuts is all that they seem to have to offer to business. There could be much more innovative and ingenious approaches. Particularly in this economic climate, the Government should address themselves to finding ways to get investment into the economy and to the businesses that need it, and to get growth into our economy.

Mr Gauke: The hon. Lady will be aware that the patent box is effectively a corporation tax cut. Is she saying that some corporation tax cuts are good and some are not good?

Catherine McKinnell: The Minister is twisting my words somewhat. He is trying to confuse a very straightforward discussion about the cut in the headline rate of corporation tax being all that this Government are offering, and this cut in corporation tax—the patent box—and potential tax reliefs for video games. Other than that cut, very little is on offer to give businesses the confidence that this Government are behind them, are backing their industry and are going for growth.

Ian Mearns (Gateshead) (Lab): Over the weekend, I had a significant discussion with people at a company in my constituency who are expert in producing marine and yacht paint and protective coatings, including fire retardants. They have a major onsite research and development arm in my constituency. One of their major problems is that once they have produced and patented a product, they do not receive assistance from the Government to get it into the European market, where there are restrictions. They have not received any such help from the British Government, which is needed because the European testing authorities take up to five months to clear British products for sale in the European market.

Catherine McKinnell: My hon. Friend raises an important example of the point I am making. The Government believe that, if they get out of the way and cut taxes, industry will spring up from below, businesses will thrive, we will have growth and the economy will move forward.

John Mann: I encourage my hon. Friend to stick to her guns. The Opposition Front-Bench team are calling for lower taxation and more support for businesses, not least in light of the evidence recently supplied by the OECD that British industry, because of the banks' interest rate hikes, is now paying the highest effective interest rate in the 27 member states of the European Union.

Catherine McKinnell: I thank my hon. Friend for that sobering statistic. The point is that it is not enough for the Government simply to stand aside and get out of the way. The clause introduces the patent box, which is a prime example of where the Government can make a real difference. By the same token, our amendment calls

[Catherine McKinnell]

on the Government to consider other opportunities for targeting support at businesses and specific industries. I am shocked, and I can hear from the murmurings behind me that Opposition Members are also shocked, that the Government seem reluctant to invest time in doing so.

Mr Aidan Burley (Cannock Chase) (Con): The hon. Lady says that the Government need to think of ways to support business other than through tax cuts. The previous Committee I sat on in this room increased from one year to two years the amount of time that an employee has to work for an organisation before he or she can make an unfair dismissal claim against that employer. Businesses, especially small businesses, had been crying out for that move to make it easier to hire and fire people. Does she support that move?

The Chair: Order. We are straying a little wide of the mark. We need to come back to the clause and the amendment.

Catherine McKinnell: Thank you for calling the Committee to order, Mr Bone. I would briefly say that it is not sufficient for the Government to get out of the way, and the point raised by the hon. Member for Cannock Chase is another example of that.

The Chair: Order. Actually, the shadow Minister is not going to say a brief word about that measure; she is going to come back to the clause.

Catherine McKinnell: Thank you, Mr Bone.

The Government could introduce many other more innovative measures, and I will cite just one that is in Labour's five-point plan for growth. There should be a one-year national insurance break for every small firm that takes on extra workers. I would have thought the Government would support such an initiative; I know that businesses do. Rather than making it easier to sack workers, the amendment would make it easier for businesses to hire workers, which would get our economy moving. That is why I urge hon. Members to support our amendment.

Question put, That the amendment be made.

The Committee divided: Ayes 13, Noes 17.

Division No. 10]

AYES

Blenkinsop, Tom
Gilmore, Sheila
Hilling, Julie
Jamieson, Cathy
Lavery, Ian
McKenzie, Mr Iain
McKinnell, Catherine
Malhotra, Seema
Mann, John
Mearns, Ian
Morrice, Graeme *(Livingston)*
Morris, Grahame M. *(Easington)*
Reeves, Rachel

NOES

Baldwin, Harriett
Barclay, Stephen
Burley, Mr Aidan
Elphicke, Charlie
Garnier, Mark
Gauke, Mr David
Hands, Greg
Harrington, Richard
Hoban, Mr Mark
Kirby, Simon
Mills, Nigel
Pugh, John
Rees-Mogg, Jacob
Smith, Miss Chloe
Swales, Ian
Syms, Mr Robert
Williamson, Gavin

Question accordingly negatived.

Clause 19 ordered to stand part of the Bill.

Schedule 2 agreed to.

Clause 20

RELIEF FOR EXPENDITURE ON R AND D

Nigel Mills: I beg to move amendment 32, in clause 20, page 12, line 3, at end add—

'(2) The Chancellor of the Exchequer shall review the extent to which intellectual property created as a result of research and development expenditure which falls within Part 13 of CTA 2009 is vested in companies whose income is not within the charge to corporation tax, and place a copy of the report in the House of Commons Library.'.

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

Clause stand part.

That schedule 3 be the Third schedule to the Bill.

Nigel Mills: I do not propose to take up much of the Committee's time with amendment 32. We have just seen the Government's carrot to encourage businesses to hold IP in the UK, and we all understand why it is important for our economy to be based on such knowledge and on the high-tech sector. Clause 20 and schedule 3 demonstrate the Government's other angle of trying further to encourage businesses to enter into research and development, in the hope that we will end up with valuable IP that is owned in the UK and creates jobs in our businesses.

The purpose of amendment 32, on which I suspect I will not test the Committee's view, is to ask whether there is a risk that R and D tax credits and incentives will effectively incentivise offshore entities to have their research done in the UK without the valuable IP that may result being owned in the UK and generating tax receipts. I am not sure from a public policy perspective that that is what we are trying to achieve. We want that valuable IP to be owned in the UK and to create jobs and tax revenues here, not in Switzerland or somewhere else.

Through amendment 32, I want to ask whether the Minister is aware that that might be a problem. I believe the rules allow an offshore company to contract with a UK company to have research done here, with the clear proviso that any fruits of that labour will be owned by the company that commissions the research, not the one that carries it out. That has been a constant theme throughout the R and D rules, certainly for large companies. Originally, for small and medium-sized companies, the company that claimed the credit had to own the resultant IP. I am not asking for that, but I am asking that the IP be effectively owned in the UK, or at least that the income that it generates is within the charge to UK tax.

In a time of fiscal constraint it is difficult for people to understand why we would want to incentivise offshore companies to have their R and D done in the UK but allow them to own the valuable assets that result, keep them offshore and not pay UK tax on them. If such companies own the assets offshore, I suppose there might still be an attraction to the research being done in the UK; we would get value from that because our science base is used and we get the income and the tax flows from having the work done in the UK. I am not totally convinced, however. If I were a big Swiss company spending millions on research, I would want that research to be done by the best scientists who had the best chance of producing a valuable product, which I could sell to make back the millions I have spent on that research. I suspect that I would choose the best researchers who were most likely to produce some valuable output. If that happens to be people in the UK, which I am sure it is in many cases, I am not sure that the existence of this tax credit will make a material difference to where I choose to have that work done. The other argument might be that if we do not do this, all our valuable scientists might emigrate to Zug or the Cayman Islands, effectively to get the people commissioning that work the tax credit there.

11.45 am

I suspect that if I were a very successful, highly desired scientist—which I am not—and I wanted to go to Zug, I could probably pay a third of the income tax I would pay in the UK. So if I move there for tax advantages, I might do it for my own advantage rather than my employer's. If I have not done it for my own sake, I am not sure that this little 3% on the bottom end would make that difference. We now have the carrot in place for people to have their IP owned in the UK. It is clearly right that we do everything we can to encourage people to do that research, for our businesses to do that, and to get those new products and new and exciting things owned in the UK. But should we be incentivising them to do that work in the UK if that product is not owned here should they be successful in that research?

John Mann: I congratulate the hon. Member for Amber Valley on his boldness in tabling what may well be a probing amendment. He is the only Conservative Back Bencher who has had the courage and wisdom even to question something in the Bill so far. It is quite extraordinary how we do our politics, and that this is the way things tend to be done. The advice that I would give, having pursued many of my own amendments in previous Bill Committees, is that doggedness in pursuing the right argument through a range of different methods can often have positive results. It needs a lot of pressure on Ministers and a recognition that the role of Whips is not to tell us what to do but simply to advise us what the business might be over the next few weeks so that we can schedule our time more effectively. I look forward to the hon. Gentleman, as I was, being appointed to the Unopposed Bill Committee, which meets in strange places and strange ways to deal with things that no one else ever wants to discuss.

I share the hon. Gentleman's concerns, although I do not necessarily agree with some of the angles he views this from. The fundamental weakness in the way we have tried to develop innovation in this country, going back over many Governments and probably two generations, is our attempt to compartmentalise it. That is the weakness of what the Government are doing here. There is one paragraph in the schedule which is helpful and which I fully support. But compartmentalising in the hope of getting something is a fundamental weakness with unforeseen consequences. The hon. Member for Amber Valley highlights a major one.

Back in the 1980s, we were ahead of the world in some of the creative industries, and we got nowhere. A good example was interactive video. I myself was involved on the periphery. I won the top world award for interactive video in 1988 as a project leader. Britain was in the lead in the technologies that were available then, but within a decade we had totally lost that lead. We lost out on everything—CDs, DVDs, 3D and the rest. But we lost out on the technological lead. Part of the problem was then that it was very old style. It was Government grants then. The problem with Government grants was not that they were not helpful but that they were project based. That was not good enough to create innovation. One could apply existing knowledge to a project base; that is part of the danger of compartmentalising. What I would like to see from Government and my own party is innovation around enterprise zones. For example, I would like to see Sheffield city region, of which my constituency is part, zoned as a whole. I do not want people shifting their business from one piece of land in the region to another, so that my area battles—we have particularly good pieces of land available—against the other side of Sheffield city region, almost the M1 versus the A1. Which bit of land should be incentivised?

Frankly, the good business entrepreneur with a good idea will pick the cheapest bit of land. It is a marginal impact, though I do not discount the fact that sometimes that can be important. Usually, it is not. Far more significant would be an overall cohesive policy that links to the research base of the universities, with a long-term plan that ties in those investors. The plan should say, "Here is the establishment in the universities; here is what we are prepared to give you. You come and dictate some of the way in which that goes forward, not just for next year but for the next decade and beyond." That way, we can begin to create some of the world-leading and, therefore, innovative and patented developments.

In sports technologies, this country and Sheffield are ahead of the world. However, there is a knowledge gap in development of the next phase of marketable products. There is a requirement for innovation that also links to health products; for instance, how to apply the latest digital technology to health or sports performance. How can that be marketed as a saleable product? That time is clearly going to come; there will be a requirement for brilliance in innovation. We do not tie those things together in this country. Sheffield city region is a perfect example of where zoning could work; all work in that ambit would get the various Government incentives. One could, for example, see the city of Cambridge and its hinterland and other areas getting a specific advantage, giving us the concept that the university and its resources are there to back potential winners, similar to the way that Silicon valley was conceptualised around Stanford university.

That can involve a few risks, but on the back of that those companies get wedded into the area because of the creative atmosphere and environment. Why would

[John Mann]

they move elsewhere if they are settled in an area? It is the source of intellectual stimulus. That is how Silicon valley managed to succeed. We have rather missed the point. I am clear that that has occurred across successive Governments. I am not simply criticising this Government, although I am criticising them to this extent: the irony of the last debate was that it was about who should take the most responsibility for a rather old-fashioned view of patenting. Should it be the previous Labour Government or the current coalition?

With this schedule we are in the same mindset: it is far too limited. That is why in a range of technologies—digital technology is another example—this country was, not in the lead but catching up, and then fell well behind. Others developed the technology. Take the microphones we have in this room: we were world leaders. Tannoy and Auditel were world leaders.

When it came to the shift to digital, we did not put in the investment, because all we did was offer around small grants. That was a fundamental weakness in the British approach. Having said that, I will commend one small aspect, as I understand it, of what the Government have done in the Bill. They have removed the de minimis opportunity for the micro-business. I used the example of digital technology. My family's company was the first importer of digital microphones into this country. A number of adaptations could have been done that might have beaten the patent test for the big multinationals that had developed the technology, and that would have allowed us to experiment and create some bespoke technology. One needed to experiment. Even if the micro-business understands what is going on, it cannot suddenly say, "Here's £10,000 for research and development this year, and another £10,000 for next year." That is what is required to pay the rates bills and other bills to keep the business afloat.

Once a company is big and successful, it has more ability to speculate, but often the micro-business will hit on the crest of the wave of where the technology is going. That was the example in Silicon valley, where the ultra micro-business suddenly realised that there was a way forward. It was not a case of blue-sky thinking—"I'm going to invent something that no one's ever thought of"—but a case of seeing what was there and adapting the technology. That is how real innovations take place. That is real entrepreneurship. We in this country are not creating the space to allow that to happen so, for the sake of the nation and our manufacturing and innovation, it would be a good idea for the Government to be honest in reporting back the successes and the failures and how they work.

What the Government are doing for the real entrepreneurs and innovators is far too limited. They are using the same mindset as the previous Labour Government, which used the same mindset as the Major Government. We could go back to the '70s. We could almost say that this is Wilsonian in its style. In my view, that is a weakness that we have to break. We are looking at too many bits and pieces rather than taking a bigger, calculated gamble. I would like to see the Government come forward—it may not happen in an amendment to the Bill—with greater boldness. Therefore, I commend the hon. Member for Amber Valley, who, after the boundary changes, may or may not be my neighbour if Bolsover goes in with him. However, in a spirit of generosity, one should work with potential neighbours—if we are both successful. I commend him on his boldness, and I encourage others to come forward with their own amendments, because the Government, strangely, do not have and never have all the answers. There will be some, even on the Back Benches of the Houses of Parliament, who have good ideas to put forward. I congratulate the hon. Gentleman.

Grahame M. Morris (Easington) (Lab): It is a pleasure to serve under your chairmanship once again, Mr Bone. I want to echo the sentiments of my hon. Friend the Member for Bassetlaw and compliment the hon. Member for Amber Valley on having the strength of character to put forward a probing amendment. It raises interesting questions. After all, our role in Committee is to scrutinise the Government's proposals, so I would like to pose a series of questions to the Minister, not least to seek clarification on how we are to define research and development. My hon. Friend mentioned particular niche industries. Clearly, Labour members of the Committee agree that one of the keys to success is investment in research and development, which is a vital part of our UK economy and ensures international competitiveness.

Will the Minister explain what R and D covers, because there seems to be a broad definition? I can fully understand how important it is to come up with a system that will support research and development. It is important for business, but it is also important that it is simple for HMRC to administer this particular proposal.

Will the Minister confirm whether the measure is part of the plan to boost growth? When will the changes come into effect? Are they to be implemented on 1 April 2013? I understand from reading the Government's consultation document that the Chancellor announced in the Autumn statement last year that the Government intended to introduce an above-the-line research and development credit in 2013 to encourage research and development by larger companies. I also understand that the proposal is to encourage research and development from small and medium-sized enterprises.

12 noon

I fully accept and agree with the proposal in the consultation document, which indicates that the UK Government

"is committed to putting research, development and innovation at the heart of its growth agenda and ensuring that the UK provides an internationally competitive environment for all companies to innovate."

However, I would be interested to know which particular companies the Government feel are likely to benefit most from the tax relief. According to the Office for National Statistics, in the UK economy £26 billion a year is spent on research and development and only 12% of that is from Government, non-profit or research councils. Allowing relief for that seems to be a common-sense approach that the Opposition would support. It is also a good idea to allow small businesses to benefit more from research and development relief, so scrapping the £10,000 limit is welcome.

There are, however, some problems. There is a real worry that if the chief beneficiaries are likely to be large multinationals, the measure could be seen as a tax cut for such organisations. It is important to ascertain the

details of the relief proposed in the clause. My concern is that the definition of what constitutes research and development is too loosely applied. For example, we would normally assume that oil and gas exploration is fairly speculative, but could it be counted as research and development? One would assume that it constituted a profit-seeking endeavour. It is not an attempt to refine a process or to improve sustainability or efficiency, which are what we would normally assume to be research and development objectives.

At present, the ONS and the Government use a very loose OECD definition of what constitutes research and development. Has the Minister considered tightening up that definition? It currently allows for manipulation by accountants by the shifting of incurred costs through normal processes or the day-to-day functioning of business into the research and development category. I would welcome any clarification that the Minister is willing to give.

Catherine McKinnell: I join my hon. Friend in commending the hon. Member for Amber Valley for tabling this probing amendment and for raising some of the important issues that the Government need to consider in terms of their research and development investment strategy.

I want to talk briefly about clause 20 and schedule 3 and tax relief for expenditure on research and development. My hon. Friend the Member for Easington raised some queries about the clause, but it does make some important changes to the existing relief and it is vital that those changes are measured against the level of impact that they have on decisions made by businesses to invest in research and development—particularly here in the UK. The hon. Member for Amber Valley made a point about the importance of measuring that value to the UK economy. It boils down to how many jobs will be created in the UK by the relief that is afforded. I am interested to hear from the Minister what consideration has been given to the queries raised by the hon. Member for Amber Valley. How will the Government ensure that the investment is properly targeted on the UK economy and on how such investment will benefit it?

Paragraph 2(5) of schedule 3 will cut the rate at which losses can be surrendered for the payable tax credit from 12.5% to 11%, which follows a reduction from 14% to 12.5% in the Finance Act 2011. The explanatory notes state that that is required

"to keep the value of the relief within the 25 per cent. threshold set out in EU State aid rules."

Will the Minister elaborate further and explain its significance in more detail? Does it mean that some businesses will be worse off and, if so, what estimate does he make of the overall impact of the reduction? Does it mean that some businesses will not be helped as much as was implied in the 2011 Budget? Will he clarify the impact on loss-making businesses?

Some of the changes set out in the schedule are certainly welcome. The Institute of Chartered Accountants in England and Wales has stated that scrapping the minimum spend of £10,000 will help more small businesses to take advantage of the relief. We know how important it is to provide support for small businesses and how little the Budget offered them, so the change is particularly welcome in that context. I would be grateful if the Minister provided us with more details. How many additional businesses does he estimate will be able to benefit from the relief, following the abolition of the minimum expenditure rule?

As I mentioned earlier, in his autumn statement, the Chancellor announced that the Government intended to introduce an above-the-line R and D tax credit in next year's Finance Bill, which will encourage R and D activity by larger companies. My hon. Friend the Member for Bassetlaw made a passionate case for attracting businesses to invest in research and development in this country. The above-the-line R and D tax credit is certainly a welcome step in that direction, because it will put the clear financial benefits of such investment into the hands of decision makers, which will make it easier for companies to conclude that investment in research and development in the UK would be positive and viable. We welcome the commitment that small and medium-sized enterprise R and D incentives will not be reduced by that change. Will the Minister comment, if he can, on the interaction between the two reliefs?

My final point relates to how research and development fits into the broader context of manufacturing and the overall investment process. Under clause 19, we talked about the patent box, which will provide companies with a clear incentive to invest in research that leads to patents and to the benefits from the new tax reliefs. We have also discussed the R and D tax reliefs that will arise from such research and development. However, one concern is that those reliefs will be paid for by the removal of the manufacturing investment allowances. In some respects for some businesses, that will rip out the core of how they turn research and development projects—the patents that they eventually acquire—into working, viable manufacturing businesses.

Today, we have received the shocking news that manufacturing output has actually fallen. The Office for National Statistics figures—April's figures came out today—show a 0.7% drop in manufacturing output in April, which is a huge concern and needs to be considered in light of the patent box support and the R and D tax credits that are being provided, but, by the same token, also in light of the manufacturing investment allowance, which was taken away in the last Budget and which we will be seeing the effects of from this year. The Government need to look at their proposals in the round, because, while the individual measures are welcome, when they are looked at in totality, many businesses, particularly small ones, are left without the incentive to invest in manufacturing capability.

Cathy Jamieson: Does my hon. Friend agree that it is particularly concerning that the ONS has commented that the manufacturing data has been

"dragged lower by falls in pharmaceutical products and preparations, as well as in other manufacturing and repair"?

Those are exactly the kind of areas that we need to ensure that we support.

Catherine McKinnell: I absolutely agree. One of the points that has been made about the patent box—the pharmaceutical industry has particularly welcomed the patent box—is that it will not benefit the companies that manufacture pharmaceutical products here. It will encourage research and development, but we need to

[Catherine McKinnell]

ensure that the incentives are there for companies to invest in their manufacturing capability. The pharmaceutical industry is one that I feel particularly keenly about, because Sanofi Aventis is based in my constituency and recently announced that it would close its manufacturing centre there. These are the types of businesses that need the incentive to invest and enable Britain to start making and building more things, and to move into growth, and these are the kinds of things that are being removed with this Budget. While giving with one hand, with R and D tax credits and the patent box, the Government are at risk of stifling the investment that is required to transform that process into actual manufacturing capability. The ONS figures released today are deeply concerning, and I hope that the Government take on board the major concerns that are being expressed, in the Committee and outside, about our manufacturing capabilities.

Mr Gauke: Clause 20 makes changes to improve and simplify a number of the rules governing tax relief for expenditure on research and development, particularly for SMEs. These changes will improve the competitiveness of the UK tax system by increasing the incentive for companies to carry out R and D in the UK. That will boost productivity and growth, with targeted support for young and innovative businesses as they grow. In November 2010, we opened a consultation with business on ways to enhance further the R and D tax relief schemes for large businesses and for SMEs. Larger businesses favour changing the way in which R and D relief is given and want to move to an above-the-line credit. That will increase the profile of UK R and D activities, particularly in multinational groups, by changing the relief from a deduction against profits to a credit that directly reduces R and D costs in company accounts.

As my right hon. Friend the Chancellor announced in the Budget, we will be introducing this change in Finance Bill 2013, following consultation on its design. Smaller companies, however, were far more concerned with improving the current scheme. They wanted more relief, and the removal of some of the barriers to benefiting from the scheme. The clause addresses those concerns.

The changes that the clause makes will increase the rate at which tax relief is given to over 7,000 companies that claim under the small company R and D scheme, from 200% of qualifying expenditure to 225%. As that rate of relief increases, state aid considerations require us to reduce the proportion of that relief that can be paid to loss-making companies in the SME scheme, so the payable tax credit rate for loss makers who wish to surrender some of their tax losses reduces from 12.5% to 11 %. It is worth pointing out that no business will be worse off from the change in rates, which is balanced by the reduction in the corporation tax rate, which is beneficial. I hope that that provides some reassurance to the Committee.

12.15 pm

Clause 20 also widens access to the R and D scheme. Government assistance is particularly important for the smallest companies that are just starting out on the road to growth and creating employment. We have recognised that by abolishing the £10,000 minimum expenditure for R and D tax credit claims. Smaller growing companies are also more likely to subcontract elements of their R and D activities to third parties if their own employee base is too small to manage all of a project. We are therefore removing the cap on the amount of relief that they can obtain by way of a payable tax credit when they make a loss. Previously, that could not exceed the amount that a company paid in PAYE tax and national insurance contributions for its employees.

In a related area, we have also widened the scope of the relief so that it is available for all expenditure on externally provided research workers, rather than just those supplied directly by a single intermediary.

Perhaps I could speak about the going concern test. We have made a change to ensure that taxpayer support is not wasted on failing companies by clarifying the condition requiring a company to be a going concern at the time it makes a claim. In future, a loss-making company that is in liquidation or administration will not be eligible to claim R and D relief by way of a payable tax credit.

Finally, one minor technical change has been made to the draft legislation issued for consultation last December to ensure that the provision on externally provided workers is clear.

Before turning to the amendment, I will pick up some of the points raised by hon. Members. The hon. Member for Easington raised the definition of R and D in the context of R and D relief. The current definition for tax purposes is set out in the 2004 guidelines issued by the Department for Business, Innovation and Skills. It includes those aspects of design intrinsic to R and D, including product development activities, when that involves making advances in science or technology to overcome the scientific or technological uncertainty.

Which companies will benefit? Most of the changes in these measures will benefit small and medium enterprises rather than large companies, and will focus on R and D. The hon. Gentleman asked about oil and gas exploration, and that is not excluded in the definition of R and D for these purposes. He also asked about the date of introduction. The changes that we are debating today will be introduced from April 2012. The above-the-line R and D credit for larger businesses, on which we are currently consulting, will be introduced in next year's Finance Bill, in effect from April 2013. We all look forward to the opportunity to debate those measures next year.

Turning to amendment 32, tabled by my hon. Friend the Member for Amber Valley, I understand that he is worried that the taxpayer is supporting the development of intellectual property which ends up in the hands of companies outside our jurisdiction. He may prefer us to support only those companies whose R and D activities are aimed at creating intellectual property that will remain in the UK. Any change of that nature would deny R and D tax credits to companies undertaking R and D for a client that will own any IP created, but whose income is not subject to corporation tax. I certainly sympathise with my hon. Friend's concerns, but I believe that any move in that direction would be ineffective, and would result in the denial of relief to claimants that we all want to continue to support. In particular, such a change would certainly be detrimental to the UK's thriving contract research sector. Such companies conduct

R and D as the central activity of their business, and are significant contributors to the UK's invisible exports of services such as pharmaceuticals and defence. They work for clients who are generally unrelated parties and will often not take ownership of any intellectual property created in the course of their work. Such a change would be more likely to reduce both inward investment into the UK and our invisible exports in R and D services, through a reduction in the level of R and D carried on here by and for multinational enterprises.

Any move to restrict who can claim tax credits based on where the ultimate client is situated may not be compliant with the UK's obligations under the EU treaty. Doing so would seem to treat work carried out for a domestic client more favourably than for a client based in another member state, potentially inhibiting cross-border trade in R and D services within the European Union.

John Mann: I am listening carefully. May I just confirm that we are not able to do what we might choose in respect of our R and D tax policy because of EU law? Which piece of EU law did a previous Government agree that restricts our ability to determine what we do today?

Mr Gauke: Were we to modify our R and D tax credit regime in such a way as to discriminate against companies that hold patents and intellectual property in another part of the European Union, that would potentially inhibit cross-border trade in R and D services and could breach our single market obligations. That is where the amendment could bite. We in the Government do not think that we should make such a restriction, but if we did we would run into difficulties with some of the fundamental freedoms in providing cross-border services.

John Mann: The Minister seems to suggest that the relevant legislation is the Single European Act, signed by Mrs Thatcher in 1986, but I want to clarify that. It has long been a principle that we in this country should be free to set our own taxation without the European Union interfering. The Minister is giving a clear example of the EU dictating to the Committee, Parliament and the Government that we cannot set a tax that we want to set because a previous Conservative Government signed a European Act. The public need to be clear and we Committee members need to be clear, for the record, that that is what the Minister is saying.

Mr Gauke: That fundamental freedom is contained in the EU treaty—essentially, the constitution that was not a constitution. I recall members of my party voting against that EU treaty and the Act that brought it in. My memory fails to recall whether I saw the hon. Member for Bassetlaw in the Lobby with us. I am sure that he will tell me if he was not.

John Mann: Unfortunately, when the Single European Act was voted through by the Conservative Government, I was not present because I had not yet been elected. I shall ask the Minister my question again, because I am not getting clarity. He used the word "freedoms". Does he think it might be wise to strike that from the record, because he is saying that there is a lack of freedom for the Committee to determine our taxation policy on R and D for businesses, owing to what the European Union dictates? For the record, we need to be clear that that is what the Government are proposing and what the Minister is recommending to us with the clause.

Mr Gauke: The expression "fundamental freedoms", if I remember correctly, comes from the EU treaty voted through by the previous Parliament, when both the hon. Gentleman and I were Members of this place. We have heard him make many speeches during our debates about how Whips are present to provide advice, but I seem to recall that in the previous Parliament he followed the advice of his party's Whips and voted in favour of that EU treaty.

John Mann: To my knowledge, I have not voted in favour of anything that restricts the right of Parliament to set taxation law. When I have asked questions, the ability to set our own taxation has always been stated to be a principle. The Minister is unable or unwilling to confirm precisely which Act we are talking about; if it is the Single European Act, we are going back some considerable time. If that is the Act that we need to amend to give the House, and the British people through us, the right to set our own taxation policy, we need to be clear. The issue is not a minor one—it may be minor in the context of one clause in the Bill, but it is not minor in terms of the responsibilities of the Bill Committee to Parliament. Parliament will want to know if its rights to set taxation law is being impinged upon by the European Union. If so, it will want to know not vague references but precisely which bit of European legislation restricts our right as a Committee when we report to Parliament to set taxation law as it relates to R and D and support for business. I am not hearing an answer.

Mr Gauke: I shall make another attempt. In the previous Parliament, the various EU treaties and the powers under them were consolidated into a single EU treaty that was then enacted. So there is a fundamental freedom to provide services, and member states have the ability to set taxes, of course, but where there is a clash with the fundamental freedom set out in the treaty on the functioning of the EU then we face restrictions. I, for one, am not going to deny that: there are constraints on what we can do with R and D tax credits. State aid requirements, for example, mean that we do not have complete flexibility as to what the rates are—the 11% rate, rather than the 12.5% rate, is as high as we can go within those requirements. Also, there are potential constraints in the particular policy being probed by my hon. Friend the Member for Amber Valley. I do not wish to conceal that in any way from the Committee.

Nigel Mills: I presume that the Minister is not saying that there are no circumstances in which the UK Government can restrict reliefs to entities and individuals that are within the charge to UK tax. That must have been a fundamental defence by the UK for various reliefs on asset transfers, loss transfers and things like that. I assume that he is making his points narrowly about the proposal that I made on the scope of the services freedom, rather than as a general change in UK tax policy.

Mr Gauke: I am not making any particular change of policy. The rate of payable credit available to loss-makers has to be reduced to 11%, however, to ensure compliance

[Mr Gauke]

with EU law. That is the highest value permissible under aid intensity levels set out in European Commission guidelines. That is the point that I am making.

This is a vital and growing area for the UK economy. We need to be certain that the taxpayer gets best value for what we invest in the incentive and, indeed, that is one of the themes in the rest of schedule 3. The changes brought about by the clause and schedule will encourage more small businesses to engage in research and development. Limiting the application of the clause to IP retained in UK companies would reduce its impact and the incentives that it provides to business. Growth through support for innovation and the development of new high-technology businesses are central themes in the Bill. They are vital to the future of our economy, and the changes help to ensure that the UK is open for business.

12.30 pm

Nigel Mills: It has been an interesting debate on an important topic. I was keen to press the Minister to set out his views on whether we should effectively be giving incentives for assets that do not end up in the UK, and I still have concerns. If the amount becomes significant, then it ought to be considered. However, I have no intention of testing the Committee's view, so I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 20 ordered to stand part of the Bill.

Schedule 3 agreed to.

Clause 21

REAL ESTATE INVESTMENT TRUSTS

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

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

That schedule 4 be the Fourth schedule to the Bill.

Cathy Jamieson: It is a pleasure to be back in the Finance Bill Committee under your chairmanship, Mr Bone. I am sure that we have all had a very enjoyable break and are desperately keen to be back discussing the future of real estate investment trusts. I can see by the looks of excitement on the Government Benches that everyone has their speeches ready.

It is important to put it on the record that the clause aims to make improvements to the real estate investment trust regime by addressing barriers to entry and investment, and by reducing the costs of complying with its requirements to help support the expansion of the property sector and so encourage further investment and stimulate the construction industry. When considering what I would say on this matter, I used my trusty red pen and marked down that at this point I must not tempt the wrath of Mr Bone too much by straying on to any other issues that relate to the macro-economic situation or the construction sector. However, it is worth noting that in the summary of impacts published by the Government, they state that the changes:

"should facilitate increased investment in REITs and the private rental sector. This may in turn stimulate the construction sector. No significant macroeconomic impacts are anticipated."

That is important to mention ahead of the comments that will undoubtedly be made if I mention Labour's five-point plan. Of course, there are other, additional ways to stimulate the construction sector, not least of which is to find other ways of investing in the housing sector, to ensure that we have a social housing programme and a programme to ensure that any repairs, retrofitting and various other things are taken forward.

Charlie Elphicke (Dover) (Con): The hon. Lady talks about welcoming the idea of REITs for social housing. Are we now to understand that the Labour party therefore welcomes the effective privatisation and market quoting of social housing?

Cathy Jamieson: Well, there is a big difference between supporting this particular initiative—which was, of course, introduced by the Labour Government; I will go on to say a bit more about that—and supporting wholesale privatisation of social housing, and I am sure the hon. Gentleman is well aware of that. I hope that we have his support not only for social housing through the various means by which in general it is provided but for the fully mutual co-operative housing option that all too often does not receive the support it deserves.

Charlie Elphicke: I have a lot of sympathy with the hon. Lady on the idea of mutuals and social enterprises for housing, particularly social housing, and it is right to develop that. Let me press her again. A REIT is a quoted enterprise on the stock market that would own social housing. Are we to understand that the Labour party is in favour of social housing being quoted on the stock market?

Cathy Jamieson: As I said to the hon. Gentleman, I will come on to some of those points when I discuss the detail of the legislation. It is important to set this in context as one method of trying to stimulate further work in the social housing sector, although not the only one. In due course, it would be interesting to extend the support that the hon. Gentlemen seems to be indicating to other ways of ensuring that affordable housing is available, in particular for the co-operative model.

I will resist the temptation to talk about other housing issues that relate to people being removed from their local areas because no adequate social housing is available for those on the homeless list, or the impact of the so-called bedroom tax—that is another area in which a Government U-turn would be welcome, but I do not want to stray too far from the clause.

Clause 21 aims to change the barriers to entry to the scheme and come up with some improvements. Specifically, the entry charge paid by a company joining the regime is to be abolished; the requirement for a REIT to be listed on a recognised stock exchange is to be relaxed; and, the diverse ownership requirement a REIT has to meet is being reduced. The condition improvements state that,

"the rules regarding the REIT's assets are being relaxed to reduce the likelihood that commercial decisions are being influenced by the conditions of the REIT legislation; the condition regarding the level of borrowing for a REIT is being made simpler to comply with;".

It is important to understand the background to this provision, and the hon. Member for Dover referred to some of the changes that are going to be made. Real estate investment trusts are a tax advantage vehicle that was originally introduced in the Finance Act 2006 and subsequently incorporated into further legislation in part 12 of the Corporation Tax Act 2010. As I said, that was set up by Labour to encourage investment in the property sector, and the regimes came into force on 1 January 2007. As of 1 April 2012, I understand that there were 24 REITs in the UK, with a particular focus on commercial property investment and an aggregate market capitalisation of approximately £20 billion.

REITs are exempt from corporation tax on the profits and gains arising from the property rental business, and they must distribute 90% of the profits from the property rental business to shareholders in whose hands that income is treated as income from property. In that way, taxation of income from property is moved from corporate to investor level.

There have been some concerns that the UK regime has not yet had the success of similar regimes such as, for example, those in the US. That is partly, it is argued, because of the depressed property market, and partly because of the number of conditions that a company has to meet to become a REIT. In particular, the entry charge has been identified as one thing that has served as a deterrent. Unlike some Government Members—I am not trying to provoke a row or argument by saying this—I never thought that any Government of any colour had all the answers when pieces of legislation were introduced, and it is always important to improve legislation where we can.

On this occasion, I have resisted the temptation to table amendments to the clause and ask the Government to carry out further work, and I will say something about that at the end of my contribution. It is important, however, to recognise that this legislation was set out by the Labour Government, and we want to see improvements to the regime.

In their response to their consultation, "Investment in the UK private rented sector" in September 2010, the Government indicated that they would look further at the barriers to entry to the REITs regime with a view to facilitating greater take-up and, in the longer term, the establishment of residential REITs. Further consultation with interested parties suggested that the best way to support the REITs industry, and in particular, the development of residential REITs, was to reduce the barriers to entry and ensure that the regime did not inhibit good business practice. That is why the Government, as I understand it, announced in the Budget 2011 that, subject to informal consultation, legislation would be included in the Finance Bill 2012 to support good business practices and remove the barriers to entry and investment in the REITs regime. A subsequent consultation took place between April and June 2011, which provided the opportunity to firm up and improve some measures that have been included in the Bill.

In the Budget 2012, the Government announced that they would consult this year on the REITs regime, and specifically, the role that REITs can play in supporting the social housing sector, as well as whether to change the treatment of income received by a REIT when it invests in another REIT. I have not tabled an amendment to the clause because I recognise that a consultation is under way, and I am willing to look, as I am sure we all are, at what the Government may propose. Dependent on the outcome of the consultation, which will run until the end of June, the Government may suggest further changes in the Finance Bill 2013. If we are spared from reshuffles or other acts of greater powers, I am sure that we are all already looking forward to that Bill—I see that the Whips are thinking, "If we ever get to the end of this one", so I will not press that point.

I want to raise a few issues about the summary of the proposals. The clause has an extensive explanatory note and although I will not go through every point in detail, it is worth putting on record some changes that are being made to the Corporation Tax Act 2010.

Section 528 of that Act requires that a REIT is listed in a recognised stock exchange. It also requires that a REIT is not a close company—in other words, that it cannot be controlled by a small number of people, which is described as the non-close company requirement. Section 530 requires that a REIT distributes 90% of its profits from its property rental business to investors, while section 531 ensures that a REIT is primarily a property investment company by requiring that profits and assets of the property rental business of the REIT are 75% or more of the total profit or assets of the REIT. Section 538 requires a company joining the REIT regime to pay a conversion charge equivalent to 2% of the value of its assets involved in its property rental business. Section 543 restricts the amount of borrowing undertaken by a REIT in respect of its property rental business by charging to tax the amount by which its financing costs exceed a limit. Section 556 determines the treatment of assets involved in the property rental business, and specifies that when the asset is disposed of, the REIT does not benefit from the exemption from tax. Those are only some of the issues that the extensive explanatory note lays out.

Among the proposed revisions are that the entry charge will be removed, on the understanding that that will make REITs more competitive with other forms of investment, such as funds and authorised unit trusts. The requirement for a REIT to be listed in a recognised stock market is to be relaxed so that listing on other foreign exchanges will be possible. That is supposed to encourage smaller entrants to join the regime, with the suggestion that by keeping operational costs down, REITs may be more attractive to the residential sector. Cash and cash equivalents will be a good asset, which was not the case in the past. That point was raised by the industry during the previous consultation, and the industry wishes to see that cash can be included in the test that 75% of the total value of assets must relate to the property rental business.

A REIT is currently exempt from corporation tax on both rental income and gains on sales of investment and properties used for a property rental business. Tax is instead borne by the investors on their share of rental income and gains, which are distributed to them by the REIT as a property income distribution. There is to be no breach if the distribution is made within six months to settle an underpayment, whereas previously a period of three months was allowed. That relief has limited application because it applies only if a stock dividend is offered in particular circumstances.

12.45 pm

One important change is that institutional investors will now include charities and registered providers of social housing, as well as partnerships, sovereign wealth funds, pension funds, insurance companies, and managers and trustees of authorised unit trusts and open-ended investment companies. That is intended to increase the diversity of ownership. There will also be a power to make regulations to add, modify or remove categories of investors on the list. Will the Minister tell us what she has in mind in that context?

There is also to be a grace period for new REITS of three accounting periods—up to three years—which prompts a question that I want to ask the Minister. In the explanatory notes and the schedule, different periods are referred to at different times. Sometimes the legislation refers to three years, but at other times it relates to three accounting periods, yet those terms are not absolutely interchangeable. There are also some issues around changes applying from different dates. For example, paragraph 21 of schedule 4 sets out that paragraphs 14 to 20 apply from the date of Royal Assent, and paragraph 26(1) sets out that the same applies to paragraph 22—I hope that the Minister or some other inspiration is following this—but paragraphs 23 to 25 apply

"for accounting periods beginning on or after"

Royal Assent. Such things may seem technical or unimportant, but I raise the matter to give the Minister the opportunity to clarify the position and to draft any amendments that may be required.

The legislation also provides for the introduction of anti-avoidance to prevent the extension of the close period for a transfer of business. The profit finance ratio cost will be amended, and I understand that the industry was particularly keen for that to happen. I hope that I have made it clear that we do not oppose clause 21, and we await further consultation with interest.

The Bill lists a new range of institutional investors, and although the concept of allowing institutional investors is welcome, it is disappointing that the definition does not include other REITs or companies that are diversely held. The legislation also gives the Treasury power to make regulations to extend the list of institutional investors. What additional groups does the Minister intend to include through such regulations?

It would also be helpful to hear from the Minister about the problem of practical barriers. Notwithstanding that the improvements to the regime will be welcomed, does she accept that there are still barriers for residential REITs, in particular because the rental income received from residential property is generally low, and yields from such property are usually realised by fairly regular re-sales of properties? A high turnover of properties may mean that such companies do not qualify as property rental businesses for the purpose of the regime, so they could not become REITs. Will the Minister address that, either now or in the upcoming proposals in the year ahead?

Charlie Elphicke: I just want to touch on social housing REITs. No doubt the hon. Lady is, like me, an avid reader of *Inside Housing*. On 18 May, a story stated:

"Associations to raise £500 million with stock exchange 'privatisation' plan…A consortium of 10 housing associations is to list a company made up of 10,000 social homes on the junior London stock exchange in September."

Does she support that plan—yes or no?

Cathy Jamieson: I do not have the advantage of having an iPad close to hand so that I can receive inspiration. Of course, as a former housing spokesperson in the Scottish Parliament, I take a great interest in social housing. I gently suggest to the hon. Gentleman that the fact that housing associations have chosen to raise finance from a range of sources—partly because the Government do not always supply that funding—does not equate to privatisation. That is a fundamentally important point in our allowing social housing associations to raise money from various sources.

Sheila Gilmore: Housing associations frequently raise money through banks and other private institutions as part of their building programmes because the grant never covered the full cost, even when it was higher. That is a money-raising issue. Housing associations are controlled by strict regulation, and I hope there is no suggestion that that regulation will disappear.

Cathy Jamieson: My hon. Friend has a long and honourable history of addressing housing issues during her time as a councillor in Scotland's capital city of Edinburgh, and she speaks with a great deal of authority on such matters, to which she is fully committed.

It is important to stress that the changes are an opportunity. Once again, partly because of the way in which the process of considering and scrutinising the Bill is constructed, I find myself almost trying to explain what the Government are doing, rather than the Government explaining it themselves.

I do not want to tempt fate or risk your annoyance, Mr Bone, given that we are approaching the end of the sitting, but it is important to stress that although we welcome the proposed changes, this is not the only way to ensure that the construction industry is stimulated and housing issues are addressed. There is no opportunity today for a wider debate on a range of housing matters but, as my hon. Friend has suggested, this is potentially one way to ensure that housing associations and other social housing providers can raise funds in a new way.

Sheila Gilmore: When REITs were originally introduced, they were intended to be—and were encouraged to be—part of the residential property market. They do not necessarily address only social housing; they also address the resurgence in the private letting market and they fulfil a need that has been clear in the past few years. Many people in housing were disappointed that, in their initial shape, REITs did not seem to be particularly successful in assisting the residential market. Hopefully, the changes in the Bill will allow that to happen.

As we all know, the private letting market tends to be disparate—some of it is good, and some of it is bad. The ability to operate on a larger scale and in a more organised manner improves management and stability quite a bit, which is good for residents. One of the big problems with private letting is its short-term nature. That obviously has an impact on the individual who wants to live in that kind of accommodation, but it is also a disadvantage to communities. Many of us struggle

with communities that are suffering from the impact of short-termism from the point of view of landlords and the tenants who live in these properties.

A more institutional approach to private letting, which REITs would offer in theory—that was the debate I recall taking place in the housing world at the outset—would encourage a more systematic and larger scale approach to its provision. That might make it much easier for people to live there in the longer term. Many have suggested that that might be advantageous to the economy, not just the individuals involved. One theory—I am not sure whether it is proven or simply debated a lot—about why some countries in Europe have more stable economies is that they have not gone quite so enthusiastically down the route of home ownership and an element of the private letting market has given them stability. I do not know whether that is necessarily a universal view, or even whether it holds, but it suggests that there is something worth encouraging in the private letting market.

If we had greater investment and people saw this as something in which they wanted to invest for the long term, providers could offer longer leases. That would be a very healthy development in the market and could improve a lot of communities. Without my venturing into the role of private letting for social housing, it has a worthwhile one to play. If these changes make it possible for this concept to move beyond largely commercial property and offer such an advantage, it is something that we would want to support, as my hon. Friend the Member for Kilmarnock and Loudoun said.

Enlarging those who could be part of a REIT and enabling social housing providers, charities and others to be part of one is quite an important step, although it requires some caution from those who enter into it. Some social housing providers are interested in looking at how this might assist them to expand their provision and find sources of financing, because things have become increasingly difficult. If we are serious about wanting an expansion of social housing, it is not surprising that social housing providers want to look at this as an option for them to get financing elsewhere. Sadly, they are finding it increasingly difficult to get sufficient grant funding, as grant levels have fallen in both England and Scotland in recent years. That means that we either have less housing provided, or try to find other means of funding it.

The traditional means has been through bank lending, but although one might argue that many housing associations are good, stable, long-term investments, some providers have found it difficult in the past two or three years to obtain the bank lending that they got previously. Some banks that supported this form of housing have moved out of the field and no longer provide the same loan assistance. In the absence of some of the more traditional ways of funding social housing, it is not at all surprising that people are interested in at least exploring this option, if it enables them to provide badly-needed housing.

1 pm

The Chair adjourned the Committee without Question put (Standing Order No. 88).

Adjourned till this day at half-past Four o'clock.