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PART H

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PART H

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PART H

1988 FINANCE BILL

DD's 25 years NAJS 23/11/95.

21-6-88

CLOSED
CONTINUED ON:-
PART 3

NH8/80Jo

CONFIDENTIAL

FROM: J M G TAYLOR
DATE: 10 June 1988

PS/FINANCIAL SECRETARY

cc: Chief Secretary
Mrs Case
Mr Revolta
Mr Gilhooly
Mr C Jenkins (OPC)
Mr Isaac
Mr Painter
Mr Beighton
Mr Lewis
Mr McGivern
Mr Reed
Mr Fraser
PS/IR

SHIPPING: AMENDMENTS TO THE FINANCE BILL

The Chancellor has seen Mr Reed's minute of 9 June.

2. His view is that we should make the BES move now, as a logical tidying up. We do not want to increase the burden at Report unnecessarily.

J M G TAYLOR

Inland Revenue

Policy Division
Somerset House

FROM: J D HINTON
DATE: 10 JUNE 1988

The obvious time to make a statement is when/if Sir W Clark moves New Clause 14. Meanwhile the interested bodies, like the NAPF, know what the Government is proposing

1. MR KUCZYS

2. PS/FINANCIAL SECRETARY (MISS FEEST)

10/6

LETTER OF 31 MAY FROM MICHAEL ELTON OF NAPF

1. Mr Elton wrote to the Financial Secretary to express gratification at the decision to remove an anomaly created by last year's Finance (No 2) Act (my note of 22 April about the letter of 24 March from Mr Zamboni of the ABI refers).

2. This letter needs no more than a short acknowledgement and I attach a draft.

J D HINTON

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cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Mr Culpin
Mr Gilhooly
Mr McIntyre
Mr Cropper
Mr Isaac
Mr Beighton
Mr Corlett
Mr Lusk
Mr Kuczys
Mr Hinton
Mr Gilbert
PS/IR

Michael Elton Esq
Director General
The National Association
of Pension Funds Ltd
12/18 Grosvenor Gardens
London
SW1W ODH

1988 FINANCE (No 2) BILL - CLAUSE 54

Thank you for your letter of 31 May. I am glad that you welcome the decision to deal with the anomaly that has been identified.

I am not sure, however, that an announcement when Clause 54 of the Bill is debated would be the most appropriate time - you may be aware that Sir William Clark has tabled a new clause on this point. I will however bear the suggestion in mind.

NORMAN LAMONT

The National Association of Pension Funds Limited

napf

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London SW1W 0DH.
Tel: 01-730 0585/0734
Telex: 28557 NATPEN G
Fax: 01-730 2595

31st May 1988

The Rt. Hon Norman Lamont, MP,
Financial Secretary to the Treasury,
Treasury Chambers
Parliament Street,
London
SW1P 3AG

FINANCIAL SECRETARY
REC. 2 JUN 1988
ACTION Mr. Hinton IL
COPIES TO PPS, CST, PMG, EST
Mr. Scholar Mr. Culpin
Mr. Gilhooly Mr. McIntyre
Mr. Cropper
Mr. Mucyssil
PS/IR.

Dear Mr Lamont,

1988 Finance (No.2) Bill - Clause 54

We have seen copies of your correspondence with Mr. Zamboni, the Chairman of the Association of British Insurers, concerning the anomaly in the entitlement of some employees earning over £100,000 - an anomaly created by the Finance (No.2) Act 1987.

We are delighted to see that you are proposing that regulations should be made so that an employee whose earnings exceed £100,000 in his last year - and whose pension would otherwise have to be calculated by reference to the 3-year averaging rule (probably reducing his final pensionable earnings below £100,000) - may in future have his pension calculated by ignoring earnings in excess of £100,000. This means that his pension may be calculated by reference to final pensionable earnings of £100,000.

It would be most helpful to those concerned with occupational pensions if you were to make an appropriate statement about this intention when Clause 54 of the Bill is reached in Standing Committee.

Yours sincerely,

Michael Elton

MICHAEL ELTON
Director General

Inland Revenue

Policy Division
Somerset House

FROM: ANGELA RHODES
438 6303
DATE: 10 JUNE 1988

PS/FINANCIAL SECRETARY

SCHEDULE E - CLAUSE 45 - CAR PARKING

1. We spoke this morning to confirm the arrangement proposed on Wednesday that should the Committee fail to reach Clause 45 on 9 June the amendments proposed by Counsel in place of Mr Wardle's amendment 219 could be put down for debate on 14 June.

2. I understand from Parliamentary Counsel that the amendments will appear on the Order Paper on Monday. We thought that the Financial Secretary may, however want to let Mr Wardle know what is proposed. I am therefore attaching a draft should he wish to write to Mr Wardle on Monday.

A M RHODES

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cc Chancellor
Chief Secretary
Paymaster General
Economic Secretary
Mr Scholar
Mr Culpin
Mr Cropper
Mr Tyrie
Mr J R Jones (Parliamentary Counsel)
Mr Isaac
Mr Lewis
Mr Northend
Miss Rhodes
Mr Evershed
PS/IR

Charles Wardle Esq MP

FINANCE BILL - CLAUSE 45

You will see from today's Order Paper that we have tabled a number of amendments to Clause 45.

The purpose of these amendments is to ensure that the exemption provided by the clause applies where expenditure is incurred in paying or reimbursing expenses in connection with the provision of car parking facilities for employees by third parties. As I understand it this is what amendment 219 which you have put down is designed to achieve.

I am pleased to be able to say therefore that we accept your amendment in principle. However we feel that the amendments we propose would result in a much simpler provision and I hope therefore you will be able to support them.

NORMAN LAMONT

42/2.BTW.4375/11

FROM: MISS S J FEEST
DATE: 10 June 1988

Ms A RHODES IR

cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Mr Culpin
Mr Cropper
Mr Tyrie
Mr J R Jones OPC
PS/IR

SCHEDULE E - CLAUSE 45 - CAR PARKING

The Financial Secretary was grateful for your minute of 8 June 1988 and approves the proposals therein. I understand the amendment will be dealt with at Committee Stage.

Susan Feest

SUSAN FEEST
(Assistant Private Secretary)

Inland Revenue

Policy Division
Somerset House

FROM: M J G ELLIOTT
DATE: 10 JUNE 1988

FINANCIAL SECRETARY

FINANCE BILL: WOODLANDS

1. I attach, as requested by Miss Feest, a short summary of the main representations made on the woodlands provisions in the Finance Bill, as an aide memoire for your meeting now arranged for Wednesday 15 June at 3.00 p.m.

2. Since we prepared this list yesterday, we have had a copy of Lord Sanderson's letter of 7 June in which he urges you to think further about continuing tax relief for costs of maintenance (c.f. point 2 on the attached list - this will doubtless come up in debate on one of Mr Boswell's amendments) and about total exemption of woodlands from Inheritance Tax (Mr Boswell has a new clause on that.) Lord Sanderson also asks for action now on the capital allowances cut off (a point raised with you by Lord Rees and Mr Williams but not the subject of an amendment, at any rate by Mr Boswell).

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cc. Chancellor
Chief Secretary
Mr Monck
Mr Burgner
Mr Bonney
Mr Cropper
Mr Painter
Mr Beighton
Mr McGivern
Mr Jaundoo
Mr Pearson
Mr Elliott
Mr Carr
Mr Streeter
Mr Timmins
PS/IR

3. On the merits of these points I don't think I can add to what I have said in my notes of 19 May and 3 June. All I would add at this stage is that, if you were minded to meet any of them, it would be helpful to know as soon as possible so as to enable us to set drafting of Report Stage amendments in hand.

Committee Stage official amendments

4. I am afraid that it looks as if we shall need about a dozen (linked) amendments (several however very short) to get the Schedule right on the storm damage point. I am sorry for that, but assume that you would want these amendments made at Committee, and we are pressing ahead with the work on that basis.

MJG

M J G ELLIOTT

	Representations	By Whom
1.	Allow all storm damage clearance costs within transitional period	Mr McGregor (accepted)
2.	Set-off all forestry expenses against any agricultural income	Mr Boswell (CLA etc)
3.	Extend transitional provision to surviving spouse	Mr Boswell, CLA and individual
4.	Remove possibility of Case VI schedule of charge	Mr Boswell (CLA etc) (accepted in principle)
5.	Remove possibility of Schedule A charge	Mr Boswell (CLA etc)
6.	Exempt woodlands from IHT completely	Mr Boswell (CLA etc) Lord Sanderson, Lord Rees and others
7.	Continue tax relief for maintenance costs of woodlands (conservation and forestry employment maintained)	Lord Chelwood, Lord Sanderson, Mr Fairbairn, Mr Jacques and many others
8.	Continue tax relief for maintenance costs but only against estate income (more restrictive than No 2 above)	Lord Rees, Historic Houses Association
9.	Continue capital allowances for pre-Budget expenditure until allowances exhausted	Lord Sanderson, Lord Rees, Timber Growers UK (but not on amendment notified by Mr Boswell)
10.	Continue existing relief for interest paid on money borrowed to purchase woodlands	Lord Rees, Timber Growers UK (not one of the amendments notified by Mr Boswell)
11.	Continue existing relief for rent paid by tenants of woodlands	Lord Rees, Timber Growers UK (not one of the amendments notified by Mr Boswell)
12.	Continue old tax system but claw back relief if trees sold before maturity	Earl of Seafield plus one other
13.	Reduce length of transitional period	Dr Marek and Opposition
14.	Transitional relief not to apply to pre-Budget day commitments unless	Dr Marek and Opposition

	planting already commenced	
15.	Continue old tax system unaltered	Mr Jacques and several others
16.	Administrative difficulty in distinguishing between non-allowable woodlands expenditure and allowable estate costs	Mr Boswell, Lord Rees, Timber Growers UK and others
17.	New grants not high enough to maintain incentive to plant	Two individuals

Inland Revenue

Policy Division
Somerset House

FROM: I R SPENCE
DATE: 10 JUNE 1988

PS/FINANCIAL SECRETARY

LLOYD'S CLAUSES ON THE FINANCE BILL

1. You should by now have already received notes on the Government amendments for Committee (Nos 191 to 200).

2. I am attaching a revised version of the Note on Clause 56 and Schedule 5. The speaking notes and background note reflect the present state of play, with references to the amendments and an up-date on the position on Lloyd's capital gains and indexed bonds.

3. I doubt whether, in the event, the Financial Secretary will need to go beyond the opening paragraphs of the Speaking Note on Clause 56/Schedule 5, or go into any detail on the other Lloyd's Clauses and the amendments. As you know Murray Lawrence has made it clear - and confirmed this yesterday - that Lloyd's are fully content with everything in the Bill, and have no wish to inspire any debate in the House on the issues not in the Bill (ie SRF and Lloyd's capital gains).

I R SPENCE

& top copy only.

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cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
Mrs Lomax
Mr Gilhooly
Mr Cropper
Mr Painter
Mr McGivern
Mr Miller
Mr Deacon
Mr Skinner
Mr Templeman
Mr Bolton
PS/IR

CLAUSE 56 AND SCHEDULE 5

LLOYD'S UNDERWRITERS: ASSESSMENT AND COLLECTION

SUMMARY

1. Clause 56 and Schedule 5 reform the administrative arrangements for assessing and collecting tax from Lloyd's underwriters.

2. The changes will first apply for the 1986 underwriting year, which closes at the end of 1988. Underwriters' income for that year will be assessed as income of 1986/87 but tax first becomes payable on 1 January 1990, twelve months after the close of the account.

3. Tax treatment of syndicate capital gains. Capital gains from premium trust funds will not be affected by these changes. Clause 95 adapts the existing arrangements to take account of the new proposed rates of capital gains tax proposed in the Budget.

4. Clause 59 - see separate note - makes some minor consequential amendments to the existing rules for the assessment and collection of tax from Lloyd's members.

DETAILS OF CLAUSE 56

5. The Clause provides a new rule for the basis of assessment of individual members and gives effect to the new rules in Schedule 5 dealing with the responsibilities of syndicate agents.

Basis of assessment of individual members.

6. Subsection (1) amends the existing rules in section 450 of the Taxes Act 1988. Underwriting profits and syndicate investment income will be chargeable to tax under Case I of Schedule D. But the basis of computation will be unchanged. Tax due on underwriting income, and on various types of investment income, will continue to be calculated under the existing rules, without any change in liability. The end-product will then be aggregated, and charged to tax as a single figure under Case I of Schedule D. In particular, the rules for computing accrued income chargeable to tax under the accrued

income scheme will be unchanged. So accrued income in respect of overseas securities in the hands of non-resident members of Lloyd's will continue to be excluded from the accrued income scheme charge to tax.

7. The provisions of the Taxes Act 1988 (amended by Subsection (1)) only apply to Lloyd's members for tax year 1988/89 onwards. So the Clause makes a corresponding change in the provisions of the Finance Act 1973, which govern the assessment of tax for 1986/87 and 1987/88 - ie for Lloyd's 1986 and 1987 underwriting years. The appropriate amendment to the Finance Act 1973 (Schedule 16) is made in subsection (3)(a) of the Clause.

Responsibilities of syndicate agents - Schedule 5 to the Finance Bill.

8. The rules in the Schedule are given effect for 1988/89 onwards by amendments to the Taxes Act 1988 (subsections (1) and (4)(a) of the Clause). For 1986/87 and 1987/88 there are corresponding amendments to the relevant provisions of the Finance Act 1973 (Section 39 and Schedule 16). These amendments are made by subsections (2), (3)(b) and (4)(b) of the Clause.

9. Commencement The effect of subsection (5) is that the new rules for the assessment of collection of tax will have effect for tax years 1986/87 onwards - ie they will first take effect for the Lloyd's 1986 account, which closes at the end of 1988.

DETAILS OF SCHEDULE 5

10. The Schedule provides administrative machinery for:

a. Establishing the amount of syndicate profit - syndicate agents will be responsible for making the return of the aggregate syndicate profit for tax purposes, and for appealing etc against the tax inspector's determination of the amount of taxable profit.

b. Payment on account of basic rate tax by syndicate agents - based on the agents' computation of the syndicates taxable profit.

c. Establishing the individual member's taxable profit - ie the aggregate of his taxable profits from each syndicate. When the individual member is assessed on his Lloyd's income he will get credit for the basic rate tax already paid by his syndicate agents.

11. Paragraph 1 of the Schedule contains definitions.

Paragraph 2 - Returns by agent.

12. Sub-paragraph (1) makes the syndicate agent responsible for delivering a return of the syndicate's taxable profit - ie the underwriting income and syndicate investment income chargeable to tax under Case I of Schedule D. The agent is also responsible for stating the amount of tax that would be payable if the whole of that profit were charged to tax at the basic rate (the amount he subsequently has to pay to the Revenue under the rules of paragraph 3 of the Schedule).

13. The date for making the return. (Sub-Paragraph 2) is the later of:

(i) 1 September in the year after the end of the closing year (eg 1 September 1989 for the Lloyd's 1986 underwriting year, which closes on 31 December 1988)

or (ii) 3 months after the issue of the Inspector's notice requiring the return.

14. Sub-Paragraph (3) sets out the amount of penalties due from the syndicate agent if he fails to deliver the return by the due date. Sub-Paragraph (4) provides the penalties where the syndicate agent delivers an incorrect return fraudulently or negligently.

Paragraph 3 - payments on account of tax.

15. This paragraph sets out the rules for the syndicate agent's payment on account of basic rate tax.

16. Under Sub-Paragraph (1) the amount of the payment is the tax due on the syndicate profit as computed by the agent (irrespective of any subsequent adjustments of the taxable profit agreed with the Inspector, or determined on appeal). The due date of the payment is a year and a day after the end of the closing year - eg on 1 January 1990 for the Lloyd's 1986 account which closes at the end of 1988.

17. Sub-paragraph (1) also provides for the agent to send a return to the Inspector, apportioning the tax paid on account on the syndicate profit between the syndicate members. The individual member's share of the tax paid will be given as a credit against the tax due when the individual member is subsequently assessed (sub-paragraph 3). If the tax paid on account by his agents exceeds the member's liability, the excess will be repaid to him.

18. In practice, the syndicate agent will withhold basic rate tax when he accounts to syndicate members for their profits, some six months before he is due to pay that tax to the Revenue. Sub-paragraph (2) provides a mechanism for balancing the account between the member and his agents if it turns out that the agent has withheld too little tax or withheld too much.

19. Sub-paragraph (4) provides for the syndicate agent to pay interest to the Revenue if he delays payment of the tax on account beyond the 1 January due date.

Paragraph 4 - determination by Inspector

20. This paragraph provides machinery for determinations of the amount of the syndicate taxable profit or loss. If the Inspector agrees the taxable profit or loss as returned by the agent (under paragraph 2 of the Schedule) he will determine the profit or loss in that figure (sub-paragraph (1)). If the Inspector is dissatisfied with the return or no return has

been made he will determine the profit or loss to the best of his judgment (sub-paragraph 2). He may also vary the determination if he discovers that it understates the profit or overstates the loss (sub-paragraph (3))

21. The notice of determination issued by the Inspector will give the time limit for the syndicate agent to make an appeal (sub-paragraph (4)). Sub-paragraph (5) provides that a notice of determination (like a notice of assessment) can only be altered in accordance with the express provisions of the Taxes Acts.

Paragraph 5 - Appeals

22. This paragraph gives the agent the same appeal rights against the Inspector's determination (in relation to timing of the appeal, and the Commissioners who hear it) as an individual taxpayer would have on an appeal against an assessment.

Paragraph 6 - Modification of determination pending appeal

23. This paragraph provides a system for establishing the amount of the member's tax in dispute when the syndicate agent appeals against the Inspector's determination of the amount of the syndicate profit or loss and the appeal has not been settled at the time the assessment is made on the member.

24. The paragraph achieves this by adapting the machinery of Section 55 of the Taxes Management Act, which applies when a taxpayer appeals against an assessment. The effect of the adaptation is that when the syndicate agent appeals against the Inspector's determination of the amount of the syndicate profit or loss "in dispute", the appropriate amount can be established by the appeal Commissioners. The resulting figure can then be used to establish the amount of tax on which payment should be postponed when the individual member appeals against the assessment made on him.

Paragraph 7 - Apportionments of syndicate profit or loss

25. Sub-paragraph (1) provides for the syndicate agent to give the Inspector a return apportioning the syndicate profit between syndicate members. This is necessary so that the Inspector can establish the individual member's total taxable profit (or loss) from his underwriting activity. Sub-paragraph (2) sets out the penalties due if the agent fails to make the apportionment return by the due date. The Inspector's notice requiring the apportionment return will state the date by which it has to be made (not less than 30 days from the issue of the notice)

Paragraph 8 -Individual members: Effect of determinations

26. Sub-paragraph (1) provides that the determination of a syndicate profit or loss is conclusive for the purpose of establishing the individual member's profit or loss from that syndicate. The paragraph also deals (sub-paragraph (2)) with the position where the determination of syndicate profit is varied or modified after the individual member has been assessed. A further assessment can be made on the member within a year from the date of the variation or modification of the determination of the syndicate profit. And the member is given an extension of time in which to appeal against the original assessment to meet the case when a determination of syndicate profit is reduced (or of a loss is increased) on appeal by the agent.

Paragraph 9 - Assessment of individual members: Time limits

27. This paragraph adapts the normal rule (in the Taxes Acts) which ensures that the standard six year time limit does not prevent a further assessment being made in the case of fraud, wilful default or neglect. It ensures that the six year time limit will not prevent a further assessment being made on an individual member where the determination of the taxable profit of one of his syndicates has been varied because of fraud, wilful default or neglect on the part of the agent.

Paragraph 10 - Supplemental: Penalties

28. This paragraph provides machinery for the recovery of penalties due from an agent (by reason of his delay in making a return of the syndicate profit or loss or in making an apportionment return) under paragraphs 2(3) and 7 of the Schedule respectively. It provides that these penalties shall be treated as if they were tax.

Paragraph 11 - Supplemental: Interest

29. This paragraph provides machinery for the collection of interest due from an agent if he delays making his payments on account of tax (under paragraph 3 of the Schedule).
Sub-paragraph (1) provides for the interest to be treated as if it were tax.
Sub-paragraph (2) provides that a Collector's certificate that interest is payable shall be sufficient evidence that the interest is due also and provides for the remission of interest under the provisions of Section 92 of the Taxes Management Act 1970.

PART II SPEAKING NOTES (NOT FOR CIRCULATION)

GENERAL NOTE ON CLAUSE 56
AND SCHEDULE 5

30. Clause 56 and Schedule 5 reform the administrative arrangements for assessing and collecting income tax from Lloyd's members. Clause 59 makes some consequential amendments to the existing legislative rules. The new arrangements are the outcome of extensive consultation with Lloyd's, and will benefit Lloyd's as well as the Revenue.

31. The Government amendments to Clause 56 and Schedule 5 deal with some minor technical defects which have come to light since the Finance Bill was published.

Why reform is necessary.

32. The present system has proved complex and costly for the Revenue to administer. It gives rise to excessive delays for the Revenue in collecting tax from profits from Lloyd's members. The Revenue's problems are reflected in corresponding problems for Lloyd's members. They can experience considerable delays in obtaining repayments of tax when they incur losses. And the complexity of the system imposes excessive compliance costs on Lloyd's members, their agents and their accountants.

33. The need for simplification has become particularly urgent in the light of two recent developments. One is the rapid increase in Lloyd's membership. The other is the legislation on reinsurance to close premiums, introduced in 1987, which will involve more detailed scrutiny of syndicate tax computations. So if nothing were done, the practical problems for Lloyd's and the Revenue would become even more serious in the future.

The objective of the new arrangements.

34. The new arrangements will produce a simpler and more effective system for taxing Lloyd's members. It will match the tax arrangement to the way that Lloyd's themselves operate in practice. In so doing, it will cut down the

number of separate tax calculations which bedevil the present system.

Details of the new arrangements]

34. Clause 56 - basis of assessment of Lloyds members. The first change made by the new system is dealt with in Clause 56. This is that all of the Lloyd's member's income from his underwriting activity will be charged to tax under Case I of Schedule D, as income of his underwriting trade.

At present this treatment applies to underwriting profits and losses. But it does not apply to the Lloyd's member's syndicate investment income, which is his other source of income from his underwriting activity. This change in the basis of assessment will not change the amount of tax liability on investment income. Clause 56 has been drafted to ensure this will not happen. But assessing both streams of income on the same basis will be a major simplification, because it will mean that tax calculations can be done on a single net figure.

The changes made by Schedule 5 to the Bill

36. Schedule 5, introduced by Clause 56, deals with the responsibilities of syndicate agents. The machinery is designed to ensure that agents provide the information about syndicate profits and losses which is needed to determine the tax liability of individual members.

Syndicate agents responsibility for returns etc.

37. The main feature of the machinery in the Schedule is that it will establish effective machinery for establishing the amount of taxable profit or loss made by the syndicate. The syndicate agent will be responsible for making a return of the taxable profit or loss and he will be responsible for appeals against the Inspector's determination of that profit or loss.

38. This machinery will give the syndicate agent legal responsibility for what he already does in practice. At present the agent submits

tax computations, deals with the Inspector's questions and discusses any points of dispute. This is inevitable, because he is the only person in a position to exercise these responsibilities. But at present he has no legal authority or responsibility for the process. In theory, all the responsibilities are those of the individual syndicate members, even though in practice they have no way of exercising them. This is a nonsense. If it continued there could be long delays in establishing the amount of syndicate profits. This, in turn, would produce even longer delays in settling the tax liability of individual members, because an underwriter's profit or loss cannot be established until the profit or loss from the last of his chain of syndicates has been determined.

Collection of tax from syndicate agents

39. The syndicate agent will also be responsible for making a payment on account of basic rate tax on the syndicate profit. This is a simplification and rationalisation of the existing system. At present the agent makes a payment on account for syndicate investment income. But does not do so for the underwriting profit. This different treatment of the two sources of income is a major reason for the complexity of the present system.

40. Under the new arrangement the syndicate agent will make a payment on account of basic rate tax on both sources of income taken together. This will be straightforward for the agent. He will simply pay over the basic rate tax due on the amount of the syndicate profit he has returned to the Inspector.

41. The agent will make his payment on account at the same time as he does at present. This will be twelve months after the underwriting year has closed. So for the Lloyd's 1986 underwriting year, which closes at the end of 1988, the agent's payment on account will be made on 1 January 1990.

Assessment/collection of tax from individual members.

42. The last component of the new system is the assessment of tax on individual members. Under the new system the member will be assessed on his aggregate profit for all his syndicates six months after the agents have made their payment on account of basic rate tax. The assessment will cover both basic rate and higher rate liability. It will take account of any adjustments made to syndicate profits or losses since the agent put in his tax computation. And the member will be given credit for the tax already paid over to the Revenue by his syndicate agents.

43. This new arrangement will, again, be a major simplification. At present there are different due dates for the payment of basic rate and higher rate tax by individual Lloyd's members. This duplication is another source of complication in the present system. It will be removed by the new arrangement for one assessment per individual on one amount of income.

DEFENSIVE POINTS

44. Will the administrative reforms increase/reduce Lloyd's members' tax bills? The new arrangements will not make any significant difference to Lloyd's members tax liability.

45. Responsibility of syndicate agents for making payments on account of basic rate tax - members' agents, not syndicate agents, should be responsible for it? Lloyd's and the Revenue agreed that this responsibility should continue to fall on the syndicate agent, as it has done in the past, while Lloyd's own administrative system is in its present form. However, Lloyd's are now considering a change in their own system. When Lloyd's change their own rules, it may be appropriate for the members' agent, not syndicate agent, to become responsible for the tax payment on account. The Government amendments to Clause 59 extend the regulation making powers so that this change could be made by regulation if it proves desirable. But it would be premature to consider a change in the

present tax arrangements until Lloyd's have settled on the details of the changes in their own administrative arrangements.

46. Lloyd's Special Reserve Fund (SRF) - why no action? We considered the representations Lloyd's made before the Budget for changes in the SRF. We concluded that the personal tax reductions introduced in the Budget removed any justification there might otherwise have been for changes in the SRF arrangements.

Lloyd's Capital Gains

47. The changes in the administrative arrangements will not affect the treatment of Lloyd's members' capital gains. The existing administrative arrangements for dealing with Lloyd's capital gains works satisfactorily, and there is no need to change them.

48. [From Lloyd's critics]. The present treatment of Lloyd's capital gains from premium trust fund should be changed? It is true that Lloyd's members' capital gains from premium trust funds are treated differently from those of other financial traders. Lloyd's members' capital gains fall within the individual CG code, whereas other financial traders' gains are subject to income tax as part of their income. The arguments for and against bringing the tax treatment of Lloyd's members' gains into line with that of other financial traders were considered in the pre-Budget discussions with Lloyd's. It was decided to leave the present position unchanged. But the point will be kept under review for the future.

49. Lloyd's Indexed Bonds - uncertainty as to whether the "indexed gain" component of the return on these bonds is taxable as income, or as a capital gain with CG indexation relief? The Revenue are examining the details of these bonds to determine the position under the present law.

50. [From Lloyd's critics]. Lloyd's use of indexed bonds shows need for a change in the law, to prevent exploitation of CG indexation relief? The application of the present law to these bonds is still under consideration, to

determine whether all of the return should properly be taxed as income. It would be premature to consider changes in the law until the present legal position has been established.

/BACKGROUND NOTE

BACKGROUND NOTE

51. The administrative reform package in the Bill. (Clause 56 and Schedule 5, with some additional consequential in Clause 59). The substance of these administrative changes was agreed with Lloyd's before publication of the Finance Bill. In subsequent discussion Lloyd's have confirmed they are content with the details of the legislation as well. The Government Committee Stage amendments all have Lloyd's support. The only amendment of any substance is the change to the regulation making powers in Clause 59 of the Bill (Amendments 119 and 200) which extends the regulation making powers to allow the legislative rule to be changed to accommodate future changes in Lloyd's own administrative arrangements. It is likely that these enabling powers will be used to switch the responsibility for the agent's payment on account of basic rate tax from the syndicate agent to the members' agent. This point is covered in the defensive briefing in this Note (paragraph 45), and is dealt with in detail in the Notes on Amendments 119 and 200 to Clause 59.

52. Cost and staffing effects. The administrative changes will have no significant effect on Lloyd's members' tax bills, or on exchequer yield from Lloyd's members. The Revenue's staff requirement is expected to be at least 50 lower under the new administrative arrangements than if the present administrative system had continued. Lloyd's expect that the new system will produce a substantial reduction in compliance cost for agents and members.

Other Lloyd's tax issues

53. Lloyd's Special Reserve Fund (paragraph 46 above). Lloyd's made pre-Budget representation for major improvements in SRF (which gives higher rate relief for payments into the fund to meet future losses). In particular, they argued for an increase in the £7,000 ceiling on annual contribution to the fund. Lloyd's main representation was that more generous relief from higher rate tax was necessary to compensate for the difference between the 60 per cent

individual tax rate to Lloyd's members and the 35 per cent CT rate for insurance companies.

54. Ministers decided that the Budget reductions in personal tax rates were a conclusive answer to these representations, and decided to leave the SRF arrangements unchanged.

55. Lloyd's have said they intend to return to the issue in future. But they have said they will not seek to get it raised in the Finance Bill debate.

Lloyd's capital gains

56. Defensive briefing is at paragraphs 47 to 50 above, though it is unlikely this issue will be referred to in the Finance Bill debate.

57. Pre-Budget consideration of treatment of Lloyd's members' gains from syndicate premium trust fund. Lloyd's members' gains from syndicate premium trust fund are taxed under the individual CG code. (The normal CG rule has a special adaptation to cope with Lloyd's three year accounting system - Clause 95 of the Bill revises these special rules to fit with the general CG reform). This differs from the treatment of other financial traders (eg insurance companies), whose gains are subject to income tax, as part of their trading profits. Ministers considered legislating in 1988 to bring the treatment of Lloyd's syndicate gains into line with that of other financial traders (taxing the gains as trading profits under Case I of Schedule D) for the following reasons:-

(a) in principle there seemed no strong argument for treating Lloyd's members syndicate gains differently from those of other financial traders;

(b) there was evidence that Lloyd's were using indexation relief to get a tax-free return from US indexed bonds (specially designed for the Lloyd's market);

(c) administrative simplification - the least important consideration.

58. Lloyd's made strong representations against any change. Ministers decided to leave the position unchanged for the time being, but made it clear to Lloyd's there was no guarantee that the present treatment would continue unchanged in the future. The Financial Secretary said in his 15 March letter to Murray Lawrence (Chairman of Lloyd's):-

> "The administrative changes will not apply to capital gains from premium trust funds. This is made clear in the Press Notice. In reaching this decision, we took account of the concern you expressed at the consequences of changing the law on this issue. But, while we have decided to leave the present position unchanged for the time being, we intend to keep the matter under review for the future. In principle, the case for treating Lloyd's syndicate gains differently from comparable gains made by other financial traders is by no means clear cut. We are concerned about reports that the benefits of the present treatment given to Lloyd's members - such as indexation - is being used to minimise tax liability on assets in the US premium trusts funds. Continuation of the present treatment would be difficult to justify if it became apparent that it was being used to facilitate the conversion of income into gains which bore little or no tax. I intend to make it clear in the course of the Budget or Finance Bill debates that the position will be kept under review, and I thought you would like to have this advance notice of my intentions."

59. In the event, the point has not been referred to in the House - and Ministers would probably not wish to take the initiative in raising the point at Committee, because of the subsequent developments on the tax treatment of Lloyd's indexed bonds (see below).

60. Tax treatment of Lloyd's indexed bonds. Since the Budget the Revenue have been considering how the existing law should apply to the US indexed bonds held by Lloyd's members. Two issues have been under consideration:-

(a) The basic question of whether, under the present law, the whole of the return on the US bonds issued to Lloyd's members is taxable as income (including the so-called "inflation factor" which is designed to attract CG indexation relief);

(b) If the whole of the return on Lloyd's US indexed bonds is in fact taxable as income under the present law, whether the Revenue are precluded from applying the law to past issues of some or all of these bonds because the Revenue had committed themselves to the proposition that the "inflation factor" in the return is not taxable as income - an argument put forward by Lloyd's.

61. At present (9 June) both issues are still under consideration. A decision will not be reached until after the Lloyd's Clauses have been dealt with in Committee.

62. Lloyd's position on the indexed bond issue. Lloyd's have expressed concern about the uncertainty created in the Lloyd's market by doubts about the Revenue's view of the tax treatment of indexed bonds, both in relation to future issues of bonds and those issued in 1987. But they recognise that the Revenue will not be in a position to make a decision until they have obtained the necessary information from the Lloyd's market - an area where discussions with those concerned (including Lloyd's centrally) is still continuing. Lloyd's have said they will not advise MPs to raise the issue in the House during the Committee Stage debate.

INLAND REVENUE
CENTRAL DIVISION
SOMERSET HOUSE

FROM: D DENTON
DATE: 10 June 1988

Financial Secretary

FINANCE BILL : WAYS AND MEANS RESOLUTIONS

1. The debate on the resolutions tabled on Wednesday is to take place on Monday evening, at 7.30 pm or thereabouts.

2. Mr Cayley has minuted to you separately (8 June) with briefing on the new clause on gains arising from certain settled property. Attached is briefing on the four* other direct tax measures. Customs will be minuting separately on the VAT point.

---

cc. PS/Chancellor
PS/CST
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Mr Culpin
Mr Gilhooly
Miss C Evans
Mr Cropper
Mr Jenkins (OPC)
Mr Isaac) for
Mr Painter) info
Mr Beighton
Policy Directors
Mr Hall (Sols)
Mr Stewart
Mr Fawcett
Mr Cayley
Mr McManus
Mr Fraser
Ms McFarlane
Mr Wilcox
Mr Denton
Mrs Hupman
PS/IR

* As agreed, briefing on the CGT charge to apply immediately before a company ceases to be UK resident for treaty purposes will follow later this afternoon.

3. As agreed, Revenue officials will be in the box for the debate.

D. Denton.

D DENTON

BOARD OF INLAND REVENUE

RESOLUTION: POST CONSOLIDATION AMENDMENTS

1. INTRODUCTORY

This resolution is a paving resolution for the Clause (NC 33) and Schedule of amendments (Amendment No 226) correcting errors in the Income and Corporation Taxes Act 1988 ("the Taxes Act 1988"). Some of these errors derive from pre-consolidation amendments made by the Finance Act 1987 and those errors also have to be corrected. A Ways and Means resolution is necessary because some of the amendments reimpose tax charges.

2. A LAW COMMISSION BILL - PURE CONSOLIDATION

The Taxes Act 1988 was drafted under the authority of the Law Commission. The draftsman had the support of Inland Revenue officials. A consolidation Act does not change the law.

3. PRINTING PROBLEMS REDUCED TIME FOR CHECKING

The Bill and Act (1041 pages) were printed on the very recently installed HMSO printing system. There were teething troubles and the time required for printing unexpectedly reduced the time planned for checking. The Act had to be published before Budget Day.

4. CONSOLIDATION ACT DOES NOT CHANGE THE LAW - CORRECTIONS THEREFORE NEEDED

The Taxes Act 1988 restates the law contained in the Taxes Act 1970 and 23 Finance Acts since then. In the Finance Act 1987 some pre-consolidation amendments were made some of which are now reflected in the Taxes Act 1988. Some of these amendments are now seen to have been incorrect and they and other errors picked up too late to be amended while the Taxes Act 1988 was being considered in either House are now being corrected.

WAYS AND MEANS RESOLUTION

CONSIDERATION FOR CERTAIN RESTRICTIVE COVENANTS

That provision may be made charging to income tax under Schedule E any consideration given in respect of certain restrictive covenants.

Speaking note

This Resolution paves the way for a new clause to the Finance Bill which will be taken during Committee Stage. The Resolution is necessary because the clause removes the present favourable tax treatment of payments to employees under restrictive covenants entered into with their employers. In future, such payments will be treated for income tax purposes as if they form part of the employee's ordinary pay. The clause will also ensure that - as in the case of pay - the payments will be deductible in the calculation of the employer's taxable profits.

The clause will apply to payments under restrictive covenants entered into on or after 9 June - the date on which it appeared on the Order Paper and was announced in an Inland Revenue Press Release.

Defensive

Why is this clause necessary now?

Some employers are now using restrictive covenants as a means of retaining employees - rather than giving them extra pay - purely because of the favourable basis on which payments under such covenants are presently taxed. We think it wrong to allow an artificial tax advantage of this kind to continue.

Which employers are exploiting the rules?

The arrangement lends itself to any engagement where the employer wishes to retain valued staff.

What is the present tax cost?

Not possible to determine this precisely. But the use of restrictive covenants could spread quickly and then the cost could be considerable.

IF PRESSED

Are payments under restrictive covenants subject to NIC?

No, but the Secretary of State for Social Services has the position under consideration.

/Background

Background

1. The new clause, which this Resolution introduces, removes the current advantageous tax treatment of payments to employees under restrictive covenants with their employers. The present rules deem a payment to have been taxed at basic rate with the effect that an employee is only taxed on such a payment if he is liable at the higher rate of tax. This reflects the assumption underlying the clause that the payment is one of capital and therefore not deductible in the calculation of the employer's taxable profits.

2. Restrictive covenants are now being used as a means of retaining employees. The advantage over increasing the employee's pay is that the covenants are for such short periods that the employer is entitled to a deduction for such payments from taxable profits and the employee pays less tax. This clause ensures that payments under covenants are treated in the same way as pay both in the hands of the employee and in the computation of the employer's taxable profits.

3. There is an added advantage for the employer in that payments are not liable to employer's NIC. Mr Portillo wrote to you about this on 7 June. He acknowledged the prudence of imposing NIC on such payments but wishes to make no public commitment while the position is under consideration.

Resolution - annual payments by Scottish partnerships

This Resolution paves the way for an amendment at Report Stage to extend Clause 35 of the Finance Bill to Scottish partnerships. It fulfils an undertaking given to Mr Butterfill by the Financial Secretary in Standing Committee on 7 June (col 286).

Clause 35 introduces the new regime for covenant and maintenance payments. As it stands, the Clause applies to annual payments by individuals. This covers individuals making payments as members of an English partnership, because in England a partnership is not a separate legal entity. But it does not cover a Scottish partnership, which is a separate legal entity under Scots law.

The amendment to be introduced on Report will bring Scottish partnerships into line with those elsewhere in the UK. The Resolution is necessary because the amendment could in some circumstances restrict tax relief. The Clause withdraws tax relief for new non-charitable covenants. It does not apply to commercial payments made in connection with the payer's business, and payments by partnerships will normally be covered by that provision, so their tax treatment is unchanged. That will cover, inter alia, partnership retirement annuities, with which Mr Butterfill was particularly concerned. But if a Scottish partnership made a non-commercial annual payment, the amendment will deny it relief. For example, if a partnership set up by a husband and wife for business purposes also made a covenant to their student son, there is no reason why it should qualify for tax relief when other student covenants will not do so. The amendment will simply bring Scotland into line with the rest of the UK, and will meet Mr Butterfill's concern that the position of Scottish partnerships under the Clause should be clarified.

Inland Revenue

The Board Room
Somerset House
London WC2R 1LB

FROM: D DENTON
DATE: 10 June 1988

FINANCIAL SECRETARY

FINANCE BILL : WAYS AND MEANS RESOLUTIONS

Further to my note of earlier today, attached is the final piece of briefing for Monday evening's debate on the above. It relates to the CGT charge being imposed where UK resident companies also establish residence abroad by dint of a double taxation treaty.

for D DENTON

---

cc Principal Private Secretary
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Mr Culpin
Mr Gilhooly
Ms C Evans
Mr Cropper
Mr Jenkins (OPC)

Mr Painter)
Mr Beighton) For Info
Mr Houghton)
Mr Fawcett
Mr McManus
Ms McFarlane
Mr Denton
Mrs Hupman
PS/IR

COMPANY RESIDENCE AND MIGRATION: WAYS AND MEANS RESOLUTION

1. This resolution is required in respect of New Clause 31. This New Clause is designed to supplement the existing provisions of Clauses 99 and 100 concerning company migration.

2. Clause 99 provides that companies which cease to be resident in the UK are deemed to have disposed of their assets (with exceptions for certain types of assets) immediately before migration and are then liable under capital gains tax legislation. This will prevent companies avoiding tax on chargeable gains by first migrating and then selling the assets.

3. But it is also possible for a company to take its assets out of the scope of UK tax without migrating. This is done by means of a "treaty migration". It becomes resident in another country for double taxation treaty purposes without ceasing to be UK resident. The UK loses taxing rights on many assets - exactly which ones depends on the particular treaty - and there is no charge under Clause 99.

4. The New Clause closes this possible loophole by providing that, where a company, while remaining resident in the UK under domestic law, becomes resident in another country for the purposes of a double taxation treaty on or after Budget Day, it is deemed for capital gains tax purposes to have disposed of its assets immediately before it became a resident of the other country. The exception under clause 100 for foreign assets of a foreign trade would be available, just as it is in relation to Clause 99 where a company actually migrates from the UK. Additionally, assets over which the UK retains taxing rights under the particular treaty are exempted.

5. I should explain that the New Clause is not intended to, and in our view does not, override the provisions of our double taxation treaties. All it seeks to do is to allow the UK to tax any unrealised gains up to the date when the company comes within the scope of the treaty "tie-breaker" provision. The charge to tax only applies to growth in value <u>before</u> the treaty comes into play; it has no effect <u>after</u> the treaty has come into play and cannot therefore be said to override the treaty in any way. Ministers are of course well aware of the importance of the principle that countries should not pass tax legislation to override their treaties; there is no question of our doing so in this case.

FP7K

FROM: D I SPARKES
DATE: 10 JUNE 1988

12/2

PS/CHIEF SECRETARY

cc Principal Private Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir Peter Middleton
Mr Scholar
Mr Culpin
Mr Odling-Smee
Mr R I G Allen
Mr Pickford
Mr Gilhooly
Mr Riley
Miss Evans
Mr Dyer
Mr Michie
Miss Hay
Mrs Burnhams
Mr Towers
Mr R Evans
Mr Cropper
Mr Tyrie
Mr Call

PS/IR
Mr Denton - IR
PS/C&E
Ms French - C&E

FINANCE BILL

... I attach details of next week's business on the Finance Bill.

D I SPARKES

FINANCE (No 2) BILL BRIEFING
STANDING COMMITTEE (8th DAY): TUESDAY 14 JUNE
STANDING COMMITTEE (9th DAY): THURSDAY 16 JUNE

The following clauses are due to be taken:

Clause 44: Car scales
(Clause taken on 9 June; note included for completeness only)

This clause sets the car benefit scale charges for 1988-89 at double their levels in 1987-88. The increase is part of the Government's general policy of reducing special reliefs so that the tax base is broadened and tax rates can be brought down. Although the change puts the valuation of company cars for tax purposes onto a more realistic basis, the charge will nevertheless still fall some way short of the true measure of the benefit.

Increases in company car scales have in the past been announced one year in advance and effected by statutory instrument. The increase in the 1988 Budget subsumes the 10 per cent increase announced for 1988-89 in the 1987 Budget and members are being given the opportunity to discuss the matter in Standing Committee.

Clause 45: Exemption for car parking space
(Paymaster General)

This clause ends the treatment as a taxable fringe benefit of the provision of car parking space for private use. The severe practical difficulties of enforcing tax on this relatively insignificant fringe benefit has meant that the Revenue has been unable to enforce the charge.

Clauses 46 to 48: Exemption for third-party entertainment
(Paymaster General)

These clauses end the treatment as a taxable fringe benefit of goodwill entertainment an employee receives from someone other than his employer. It has been difficult and disproportionately

time-consuming to value this sort of third-party entertainment and little tax has been collected. The change was announced last September and applies from 6 April 1987.

Schedule 4: Extension of BES to private rented housing
(Financial Secretary)

This schedule complements clause 49 (taken by Committee of the Whole House on 9 May) which extended the Business Expansion Scheme to investment in companies specialising in letting residential property on new-style assured tenancy terms. The schedule contains most of the detailed provisions of the extension to the relief.

Clause 50: Limit on relief under Business Expansion Scheme
(Financial Secretary)

This clause places limits on the total amount of investment in a company which can qualify for tax relief under the Business Expansion Scheme. This is £½ million generally but £5 million for companies raising money for ship chartering or for private rented housing. The limits apply to shares issued after 15 March 1988, but where a company had published a prospectus before that date and had issued shares before 6 April, the £½ million limit is instead £1 million. The purpose of the limits is to target the BES more effectively at smaller businesses which find it hard to raise money in other ways.

Clause 51: BES tax relief rules
(Financial Secretary)

This clause allows investors in a BES fund to get tax relief by reference to the closing date for investment in the fund rather than the date the fund itself invests the money in BES companies. Investors will not however be able to claim the relief until the fund has invested the money. The measure will give managers of BES funds more time to find suitable companies in which to invest and will relieve the pressure on them that can arise to invest before the end of each financial year.

Clause 52: Start date for personal pensions
(Chief Secretary)

This clause fixes 1 July 1988 as the start date for personal pensions. At the time of last year's Finance Bill the start date had been expected to be 4 January 1988 but the timetable for implementing the Financial Services Act has resulted in a six-month postponement. The clause also provides for the present retirement annuities tax regime (which was due to be phased out on the introduction of personal pensions) to be extended until 1 July.

Clause 53: Amendments to personal pension provisions
(Chief Secretary)

This clause allows DHSS minimum contributions to a contracted-out personal pension scheme for a person who leaves an occupational scheme midway through a tax year to be backdated to the beginning of that year. It also allows members of contracted-in schemes to contract-out of SERPS on an individual basis through a special personal pension. This will give employees fuller flexibility and freedom of choice in their pension arrangements. Finally, the clause exempts personal pension schemes from the additional rate tax which applies to discretionary trusts.

Clause 54: Transitional arrangements for pre-1987 pension scheme members
(Chief Secretary)

This clause enables the Inland Revenue to make transitional arrangements to protect pre-1987 members of pension schemes from the effects of last year's legislation to prevent high earners exploiting pension schemes. The transitional arrangements are necessary to ensure that existing scheme members do not lose their right to the pre-1987 rules simply on a technicality. The clause widens the scope of a similar enabling power in last year's Finance Act.

Clause 55: Lump sum benefits on deferred retirement
(Chief Secretary)

This clause exempts from tax lump sum benefits under occupational or personal pension schemes paid to people who defer retirement, in the

same way as lump sums paid to people who retire are exempt from tax. The clause puts on a statutory footing an existing concession.

Clause 56 and Schedule 5: Reform of Lloyd's tax regime
(Financial Secretary)

This clause and schedule reform and simplify the administrative arrangements for assessing and collecting tax from Lloyd's underwriters. The main features are that syndicate agents will have legal responsibility for making returns of syndicate profits; underwriting profits and syndicate investment income will both be taxed as members' trading income; syndicate agents will make a payment on account of basic rate tax; and there will be a single assessment on each member's Lloyd's income. The changes, on which Lloyd's were consulted, apply from the 1986 underwriting year, which closes at the end of 1988.

Clause 57: Lloyd's stop-loss policies
(Financial Secretary)

This clause corrects a minor anomaly in the tax treatment of Lloyd's members' receipts from personal policies taken out to insure against losses on underwriting activity. Lloyd's have been consulted and support the change.

Clause 58: Lloyd's reinsurance to close
(Financial Secretary)

This clause modifies 1987 legislation on the tax treatment of reinsurance to close premiums. These premiums are paid at the end of each account year by members of a syndicate to the members for the following year who assume the syndicate's outstanding liabilities. The clause provides relief for those who leave syndicates and simpler rules for those members who remain and thus meets Lloyd's only complaint about the 1987 legislation.

Clause 59: Lloyd's consequentials
(Financial Secretary)

This clause makes minor consequential amendments supplementary to the provisions of clause 56 and schedule 5. In particular, it allows the

Inland Revenue to modify the administrative arrangements for taxing syndicates to accommodate future changes in Lloyd's own structure.

Clause 60: Relief for disposals of oil licences
(Economic Secretary)

This clause introduces a new capital gains relief for disposals of oil licences. It applies to licence swaps of undeveloped acreage as well as to work programme farm-outs. It thus removes a fiscal impediment to licences being transferred to those best placed to explore and develop the acreage concerned. The reform arises from consultations with the oil industry.

Clause 61: Deductible expenditure on disposal of oil licences
(Economic Secretary)

This clause enables certain drilling costs to be deductible in computing the chargeable gain on disposal of an oil licence. It applies to disposals of undeveloped acreage whether consideration is in cash or in any other form. The clause thus complements clause 60 in removing tax penalties on re-arrangement of licence interests in the North Sea.

Clause 62: Definition of terms used
(Economic Secretary)

This clause simply defines terms used in clauses 60 and 61.

Clause 129: Reform of tax regime for Southern Basin fields
(Economic Secretary)

This clause reduces the petroleum revenue (PRT) oil allowance (the quantity of oil or gas production exempted from PRT) for post-1982 onshore and Southern Basin fields. Together with the abolition of royalty for these fields (announced in the Budget but to be implemented by Dept of Energy legislation), this clause restructures the tax regime in a way which relates tax more closely to profitability and thus should encourage development of more marginal fields.

Clause 130: PRT relief after production ceases
(Economic Secretary)

This clause makes deductible certain operating and maintenance costs of facilities in fields where production has ceased but where the facilities concerned continue to be used by other fields. The new relief will encourage efficient use of existing North Sea infrastructure.

FORTHCOMING BUSINESS

Standing Committee (10th day) Tuesday 21 June
Standing Committee (11th day) Thursday 23 June

Clauses will continue to be taken in broadly numerical order.

FP Division
10 June 1988

42/2.BTW.4375/20

cc: PPS, CST, PMG, EST
Mr. Scholar
Mr. Culpin
Mr. Gilhooly
Mr. McIntyre
Mr. Cropper
Mr. Hinton IR
PS/IR.

FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Michael Elton Esq
Director General
The National Association of
Pension Funds Ltd
12/18 Grosvenor Gardens
LONDON
SW1W ODH

13th June 1988

Dear Mr Elton

1988 FINANCE (No 2) BILL - CLAUSE 54

Thank you for your letter of 31 May. I am glad that you welcome the decision to deal with the anomaly that has been identified.

I am not sure, however, that an announcement when Clause 54 of the Bill is debated would be the most appropriate time - you may be aware that Sir William Clark has tabled a new clause on this point. I will, however, bear the suggestion in mind.

Yours sincerely

Norman Lamont

NORMAN LAMONT

pp

13 JUN 1988

HOUSE OF COMMONS
LONDON SW1A 0AA

FINANCIAL SECRETARY
REC. 13 JUN 1988
ACTION
COPIES TO
Mr. Elliott
PS/Chancellor
Mr. March
Mr. Burgner
Mr. Call
PS/IR.

My dear Norman,

It was a delight to see you both at lunch. I came again soon.

As promised I enclose a brief report on the effect of the proposed changes in the financial bill on many genuine private courses.

All good wishes —

Yours 9/VI/88.

From: Nicholas Fairbairn, Q.C., M.P.

Fordell Castle · By Dunfermline · Fife

The Effect of the Finance Bill on Certain Private Forestry.

In his Budget the Chancellor made sweeping changes to forestry taxation intended to prevent the abuse of large scale softwood planting by non-foresters to reduce their tax liability. In so doing, he has put in jeopardy all those foresters (of which I am an example) who have neither alternative effect in their landed business nor in their normal forestry crop. The grants are unimpeached. Previously the interest on borrowed capital for the purchase, planting, felling, thinning & tending of forestry could be set off against other general income for many years, as could all costs spent if not borrowed.

Now only those such as farmers & estate owners with other land interests can do so. There are a great many foresters such as myself who foster for the benefit of the landscape & in the furtherance of dendrology who will now have to pay all their huge costs out of net income, which is just not possible. This will result in neglect & decay of an important landscape specialty & a critical shedding of foresters with structural & characteristic effects on the rural community & the integrity of its trail ethos & its own trail economy.

I am sure some scheme can be devised which will enable the Chancellor to slay the philistine dragons without liquidating the dedicated private foresters.

N.B. | A forestry gross wage, per hour, = £1.
£ costs = the net wage of a member of unemployed

53/2/LPD/3751/001

cc. PS/CHANCELLOR
PS/CST PS/FST PS/PMG
MR SCHOLAR MR CULPIN
MR GILHOOLY MS EVANS
MR CROPPER MR DYER
MR WALTON - C+E
PS/C+E.

Treasury Chambers, Parliament Street, SW1P 3AG

Dr John Marek MP
House of Commons
LONDON
SW1A 0AA

13 June 1988

Dear John,

FINANCE (No 2) BILL CLAUSE 11

You asked during the Committee Stage of the Finance Bill on 17 May about the number of cases which would be affected by the proposed extension of the time limits for arrest and proceedings for customs and excise offences from three to twenty years. I said I would try to obtain this information and then write to you.

I should first say that there can be no simple estimate of the likely number of cases. The provision will have effect only in relation to offences committed after Royal Assent, so will not mean any increase over the present three-year limit until 1991. The time limit for proceedings will then lengthen annually until the full 20 years is reached in 2008. In the past it has not been the practice of HM Customs and Excise to maintain a record of cases which could not be pursued because they are out of time, but they do not expect to use the new provision to pursue many completed offences. They are mindful, amongst other factors, of the Attorney General's guidelines that regard must be had not only to the date when the offence was committed, but to the length of time likely to elapse before the case can be brought to trial, and will therefore only in exceptional cases pursue completed offences which have become stale.

Customs expect the main use of the provision to be to bring to court the earlier stages of continuing offences. Taken together with the increased penalties to be provided by clause 12, we believe that this will enable serious offences in the Customs and Excise area to be brought to trial and met with an appropriate deterrent sentence.

Yours ever

Peter

PETER LILLEY

42/2.BTW.4375/02

cc: PPS, CST
Mrs. Lomax
Mr. Culpin
Mr. Cropper
Mr. Tyrie
Mr. Conley IR
PS/IR.

Treasury Chambers, Parliament Street, SW1P 3AG

P W Goodwin Esq
Freshfields
Walden House
17-24 Cathedral Place
LONDON
EC4M 7JA

13th June 1988

Dear Peter

Thank you for your letter of 24 May about Clause 94 of the Finance Bill.

As you recognise, this is an exceedingly complex area. I have read Freshfields' comments and suggestions with interest and will bear them in mind. Unfortunately it may not be possible to solve the problem this year.

Yours ever

NORMAN LAMONT

I saw Lena last weekend. She very kindly asked my mother to stay for a few days after she had been in hospital.

42.2.BTW.4375/19

cc: PPs, CST, PMG, EST
Mr. Scholar
Mr. Culpin
Mr. Cropper
Mr. Tyrie
Mr. J.K. Jones OPC
Miss Rhodes IR
PS/IR.

Treasury Chambers, Parliament Street, SW1P 3AG

Charles Wardle Esq MP
House of Commons
LONDON
SW1A OAA

13th June 1988

Dear Charles

FINANCE BILL - CLAUSE 45

You will see from today's Order Paper that we have tabled a number of amendments to Clause 45.

The purpose of these amendments is to ensure that the exemption provided by the clause applies where expenditure is incurred in paying or reimbursing expenses in connection with the provision of car parking facilities for employees by third parties. As I understand it this is what amendment 219 which you have put down is designed to achieve.

I am pleased to be able to say therefore that we accept your amendment in principle. However, we feel that the amendments we propose would result in a much simpler provision and I hope therefore you will be able to support them.

Yours ever

NORMAN LAMONT

4084/27

FROM: I C SEARS
DATE: 13 June 1988

01-270 5183

PRINCIPAL PRIVATE SECRETARY
PS/CHIEF SECRETARY
PS/FINANCIAL SECRETARY
PS/PAYMASTER GENERAL
PS/ECONOMIC SECRETARY

cc Mr R Culpin - FP
Mr Gilhooly - FP
Miss C Evans - FP
Mr G Michie - FP
Mr R Evans - Press Office
PS/IR
PS/HMCE

FINANCE BILL : STANDING COMMITTEE : TUESDAY 14 JUNE

The Chairman's provisional selection of amendments for the eighth day in Standing Committee is as follows:

CLAUSE 45 (Car parking facilities)
260 + 261 + 219 + 262 + 263

CLAUSE 46 (Entertainment: non-cash vouchers)
216 + 217 + 218

CLAUSE 47 (Entertainment: credit tokens)
Clause Stand Part Debate

CLAUSE 48 (Entertainment of directors and higher-paid employees)
Clause Stand Part Debate

SCHEDULE 4 (Business expansion scheme: private rented housing)
230 + 231 + 232
242 + 243
258 + 259 + 256 + 257

CLAUSE 50 (Restriction of relief)
252 to 255 + 16
238
239 + 240 + 241
229

CLAUSE 51 (Approved investment funds)
246

IAN SEARS
Parliamentary Section

14 JUN 1988

The National Farmers' Union

Agriculture House · Knightsbridge · London SW1X 7NJ

Telephone: 01 - 235 5077

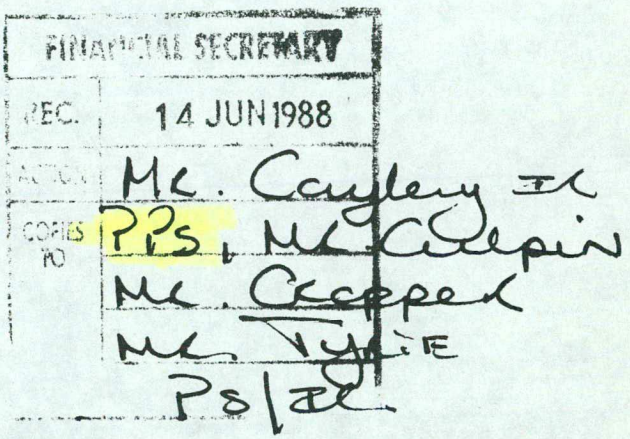
All communications
should be addressed
to the Director General

When replying please
quote the following reference:

Your ref:

Telegrams: Farmesuni, London
Telex No. 919669 NFULDN G

11 June 1988



The Rt Hon Norman Lamont MP
The Financial Secretary
H M Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

Dear Mr Lamont

Finance (No 2) Bill: Capital Gains Tax Treatment of Assets Acquired Since March 1982 with the Benefit of Rollover or Gifts Relief

I am writing with reference to the amendments about rollover and gifts relief from capital gains tax tabled by Mr Tim Boswell and Sir William Clark to Clause 91 of the Finance Bill, and to the Paymaster General's undertaking in the Committee Stage debate on 10 May that the problem which the amendments sought to deal with would receive sympathetic consideration. The amendments related to serious anomalies in the proposed legislation, and the NFU does feel very strongly that action should be taken to deal with these.

The Chancellor stated in his Budget speech "This Budget ends once and for all the injustice of taxing purely inflationary gains", yet as the Bill stands there will be a continuing problem with inflationary gains where the present owner of the assets acquired them after March 1982 with the benefit of rollover relief or gifts relief. If he disposes of the assets, the deferred gains will in principle become taxable, and at a higher rate of tax than would have applied on the original disposal. Moreover the injustice will be steadily aggravated as time passes, since the owner's indexation allowance will be based not on the true value of the assets but on their cost minus the rolled-over inflationary gain.

It is arguable that it was the intention of Parliament in 1965 that inflationary gains should be charged to capital gains tax, and that rollover relief should be no more than a deferment of tax properly due so long as the business continued to operate on the same or a greater scale. But the stated object of the present proposals is to cease taxing inflationary gains, and indeed inflationary gains that were rolled over at any time during the 17 years from April 1965 to March 1982 will now be relieved from tax.

The amendments which were debated would have provided a broad-brush solution to the problem by treating an asset which had been acquired with the benefit of rollover since March 1982 in the same way as an asset acquired without rollover, taxing it only to the extent that its value has risen faster than inflation since it was acquired. As the Paymaster General pointed out, this is open to the objection that in some circumstances this could confer a positive advantage on the taxpayer if substantial post-1982 gains had been rolled over. As far as agriculture is concerned, that would apply only to a minority of cases. In general, the value of agricultural land has not appreciated in line with retail prices since 1982 so that effectively rebasing the tax to a later date, so far from being an advantage, would generally be less advantageous than rebasing to 1982. The chief exception to this would arise where land had acquired development value since 1982. It seems to us therefore that there is much to commend the broad approach of the amendments, which would be simple to administer and marginally favourable to the Exchequer.

If the problem of development value has to be looked to, we would suggest that a two-tier approach might go a long way to dealing with this. Any substantial development value realised prior to 18 March 1985 would have been subject to the 60 per cent development land tax. We think this would more than outweigh any advantage to the taxpayer from not being taxed on the balance of post-1982 gains. We recommend therefore that the treatment suggested in the amendments, treating the new assets as acquired at their market value in calculating gains arising from disposals after 5 April 1988, should apply to land acquired with the benefit of rollover after 31 March 1982 where the old assets were disposed of prior to 18 March 1985. For disposals between that date and 5 April 1988 which are the subject of rollover, we recommend that the gain arising on that disposal should now be recalculated on a March 1982 basis, and a corresponding notional adjustment made in the rollover computation. The acquisition value of the new assets would thus be established on a comparable basis to other assets, and only post-1982 real gains would remain potentially chargeable. There should be no great administrative problem since in the vast majority of such cases the indexation allowance will have been based on the March 1982 valuation so that the relevant information should already be on the file.

Similar considerations arise with the gifts relief which, coupled with the easing of the former capital transfer tax rules, has encouraged many farmers to pass on land in the family. In these cases, the simple solution would appear to be to treat the present owner as if he were also the owner of the assets at March 1982, very much as in the case of husband-to-wife transfers.

As I have said, the injustice of the present proposals in these cases is compounded as time passes because the indexation allowance will be based not on the true cost of the assets but on their cost minus the rolled-over or held-over gain. We do not think that correcting this would in itself adequately deal with the main problem, but there would be no administrative difficulty in calculating the indexation allowance on the actual cost or value of the assets, and we trust that this will be part of whatever measures the Government brings forward.

Yours sincerely

S.W Passmore.

S W Passmore
Chairman, Taxation Committee

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Standing Committee A

FINANCE (NO. 2) BILL

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

Eighth Sitting
Tuesday 14 June 1988
[*Part II*]

CONTENTS

SCHEDULE 4, as amended, agreed to.
CLAUSE 50, as amended, agreed to.
CLAUSE 51 agreed to.
Adjourned till Thursday 16 June at half-past Four o'clock.

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Standing Committee A

Tuesday 14 June 1988

[*Part II*]

[MR. JOHN HUNT *in the Chair.*]

Finance (No. 2) Bill

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

[*continuation from col. 450*]

9 pm

On resuming—

Mr. Lamont: The hon. Member for Clydebank and Milngavie (Mr. Worthington) referred to his anger about the measure. That anger, I suspect, was mirrored on the Government Benches by our anger at the constant misrepresentation of the measure—misrepresentation of its purpose—combined with ignorance of its detail, as exposed by the hon. Member for Edinburgh, Central (Mr. Darling). But that anger was probably more than overcome by our despair about whether the Opposition will ever adopt a sensible attitude towards rented property.

The hon. Member for Clydebank and Milngavie spoke of the measure as a printing press. One of his colleagues referred to it as a racing certainty of an investment. Well, we shall see. I hope that he is right and that the scheme will be immensely successful. If it is, it will mean a massive investment in the provision of housing. After all, what is wanted? Homes for people to live in. That is why the tax relief is being provided. If the scheme results in an increase in the supply of housing why should the Opposition be so worried about the money to be made out of it? They seem far more concerned about whether people will make money out of the scheme than about whether the scheme will succeed. They do not seem interested in debating the pros and cons of whether it will work. They discuss only whether people will make money out of it. But it does not matter one damn whether they do—if it succeeds in providing a lot of accommodation in our cities.

Mr. Andrew Smith: It is clear that people will make an awful lot of money out of the scheme at the expense of the poor unfortunates who are housed in such property. However, will the Minister answer my question about those parts of the country where the supply of accommodation is limited because of limited land availability, planning permission, and so on? In such circumstances, the scheme will drive the price of property through the roof without an increase in supply.

Mr. Lamont: I shall gladly answer that point because it is utterly and wholly absurd. The fact that there is a problem with house prices in the south-east is all the more reason to deregulate the market—it is the argument for so doing. Indeed, one virtue of the business expansion scheme for rented property is that it may encourage more efficient use of the housing stock—either by bringing vacant properties into use or by converting houses into flats. It is surely right to do that. It is precisely because there is a problem in the south-east that it is right to deregulate the housing market. The hon. Gentleman has shown that he has wholly missed the point and that he misunderstands the measure.

I return to my earlier contention that if this investment is to be a racing certainty, as Opposition Members suggest, it will mean that we have achieved something that has been denied other Governments—the revival of the private sector. I shall not regret that, although I do not think that there is evidence that it is a racing certainty. I shall be delighted if the scheme is successful on the terms that Opposition Members fear because that will mean massive investment in rented accommodation. If there is such investment, what will than mean? Horror of horrors for them! It will mean that the rent that people pay will be lower, which the Opposition seem unable to accept as the consequence of our proposals.

Mr. Battle: It is not simply a question of the amount of rent and whether people can afford to pay, it is also a question of the condition of the property and of the relationship between tenant and landlord, which should be one of equality not one in which all power goes to the landlord. I thought that the Minister for Housing and Planning accepted that. Why cannot the hon. Gentleman accept the principles of the social charter?

Mr. Lamont: The hon. Gentleman talks about landlords as though all landlords were members of large companies.

[*Interruption.*]

He used the phrase "all-powerful landlords". The Committee heard him use it. Sometimes he does not follow the logic of his own arguments.

Ms Armstrong: Will the hon. Gentleman give way?

Mr. Lamont: I should like to finish replying to the hon. Gentleman before I give way to the hon. Lady.

Surely it is right to establish a position in which the tenant and landlord can strike a rent between them. This is more likely to encourage a supply of housing. The hon. Gentleman misses the point that there are already built into this proposed legislation provisions relating to standards of accommodation and to access to rent assessment committees. I do not believe that we would have the slightest chance of making the scheme a success if we went beyond the provisions that we have built in so far.

I shall develop my argument a little further. The hon. Member for Dunfermline, East (Mr. Brown) said that he believes that what we advocate would merely provide a market in second homes. That does not necessarily follow. The hon. Gentleman may have been thinking about the maximum investment figure that we have designated in the Bill for both inside and outside

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London. I do not think that this means that luxury homes alone will be involved. The limits that we have written in are specifically maxima. They are realistic, but we hope that much of the investment will take place at lower figures. I cannot guarantee that but, in fixing a maximum, we hope that that will happen.

Mr. Gordon Brown: If large numbers of these properties, especially in London, are to become second homes for international executives, what is the case for public money being used in this way to subsidise them?

Mr. Lamont: The hon. Gentleman cannot have been listening to what I was saying in the past few seconds. I specifically denied that that would happen. My arguments may have been bad, but it is rather odd of the hon. Gentleman to question me as though I had admitted that we are discussing homes for international executives. My poor, modest arguments—such as they were—were directed entirely towards denying that. The hon. Gentleman ought to deny them before asking about the point of them.

Ms Armstrong: Will the Minister give way?

Mr. Lamont: I shall, but I want to make progress.

Ms Armstrong: I appreciate what the hon. Gentleman says. However, he was unable to give guarantees as to how that will happen. How will he monitor the effect of the provision and will he come back next year if it is not having the desired effect?

Mr. Lamont: We shall judge the success of the scheme by what it does to the supply of housing. We shall watch out for what the hon. Lady and her hon. Friends said about bad landlords. However, I believe that what has been said is largely scaremongering and groundless. But if the scheme is abused we shall not hesitate to take appropriate measures.

The hon. Member for Dunfermline, East also referred to some of the grounds on which people can regain possession of a property and, in particular, to the redevelopment of properties. It is not unreasonable to allow landlords to regain possession of properties when they intend to redevelop them. But this provision is modelled on what applies to existing assured tenancies and business lettings except that the new ground is narrower because it cannot be used where the landlord bought the property over the head of the tenant.

The system is not wide open to abuse as the hon. Gentleman has implied. A landlord cannot obtain possession if the work can be done while a tenant remains in occupation, and case law under the business lettings legislation shows that courts will grant permission only when a landlord can show firm plans to do the work.

Opposition Members may disagree but I do not think that that is self-evidently outrageous. If one is going to move towards a freer market in rents there must be occasions when a landlord can regain possession of his property.

Mr. Butterfill: Does my hon. Friend agree that the possession arrangements under part II of the Landlord and Tenant Act 1954 make that difficult even when planning consent has been obtained for major alterations? Possession has sometimes been denied and it is by no means automatic that it will be given to the landlord.

Mr. Lamont: My hon. Friend is right and that has been an enormous deterrent in the past. Unless we have a balance that recognises some rights for landlords we will never get anywhere in enlarging the scope of the privately rented sector.

The hon. Member for Dunfermline, East referred to the question of the landlords' code or the tenants guarantee, and I shall repeat what I said before. Under the Housing Bill, landlords wishing to take over local authority dwellings under the tenants' choice proposals have to be approved by the housing corporation in the same way as registered housing associations. However, there the considerations are quite different. Tenants' choice landlords will be taking over tenanted public sector housing and it is right that in those special circumstances there should be a mechanism to ensure that the landlord is of good repute.

On the other hand, lettings of dwellings acquired tenanted from local authorities cannot qualify for the business expansion schemes and registered housing associations cannot be BES companies. We are taking powers in the Housing Bill for the housing corporation to issue guidance to housing associations about housing management—a tenants' guarantee. The principles of that guarantee may well be applicable to local authority housing which is taken over by private landlords under tenants' choice but it is not relevant to BES landlords who are not, by definition, taking over tenanted local authority housing.

The Minister for Housing and Planning has made the distinction perfectly clear

[*Interruption.*]

I make that point simply because Opposition Members seem to think that what I said before dinner was in some way open to argument as a statement of the principles embodied in the Housing Bill.

9.15 pm

I acknowledge that the Opposition Members know an awful lot about housing; they may know more about the housing legislation than I do. But on this point, they were talking complete nonsense and they should recognise that.

Mr. Wallace: The Minister has asserted that the situations are different. However, he has not satisfied Opposition Members as to why they should be different. If he accepts that tenants are inherited from the public sector, surely he must accept that the types of tenancies relating to the business expansion scheme are created with assistance from the public purse.

Mr. Lamont: We are talking about totally different things. The business expansion scheme cannot apply to

any property, public or private, that is tenanted. The property must be new rented accommodation, preferably newbuild. We want a new supply of rented accommodation. It is quite right that there should be a distinction between that and the safeguards that exist when transferring local authority tenants to a private sector landlord. I should have thought that prima facie, there was a strong case for having certain safeguards in the case of local authority transfer.

The hon. Member for Edinburgh, Central (Mr. Darling) asked why we should subsidise the landlord, not the tenant. The subsidies serve two totally different purposes. The tenant is subsidised if necessary to enable him to pay a market rent. The problem is that at present landlords are reluctant to provide rented property because of the legacy of rent control, among other factors, which has meant that there has been no substantial investment in the private sector for the past 50 years. The BES provisions will provide a stimulus to encourage landlords to enter that market. The negative attitude of Opposition Members does not help. They accept that there is a shortage of rented accommodation, but refuse to accept any measures targeted directly at increasing its supply.

Mr. Darling: I cannot let one of the Minister's remarks go. He said that the tenant if necessary is subsidised to pay a market rent. Surely the Minister knows that there is an upper limit on the amount of housing benefit that a tenant can receive. In many cases, certainly in Edinburgh, that is nothing like the market rent. Sometimes there is a £30 or £40 per week shortfall. How can the Minister justify that?

Mr. Lamont: There is a specific amendment—No. 233 which deals with that point and I shall come to it later. I should like to deal with all the Opposition amendments, although they have not been discussed at great length. Perhaps the Opposition were being modest and were worried that some of their amendments moved in previous sittings had not been as well targeted as they might have been. They should not be so modest. The amendments that they have tabled today have not been so wide of the mark: I shall reveal, I shall consider one or two of their amendments and I hope that that will please Opposition Members mightily.

Mr. David Nicholson (Taunton): I am sorry to delay my right honourable Friend. Before he deals with the Opposition amendments, will he reassure me on a very important point? Opposition Members made great play of the fact that someone who had been convicted of malpractices and, indeed, crimes regarding housing might benefit from the scheme? Will my right honourable Friend give an assurance that there are safeguards against that in the administration of the scheme? That point is causing considerable concern in the Committee.

Mr. Lamont: Of course it is a matter of enormous concern. Certain of the provisions that my hon. Friend the Minister for Housing and Planning is putting forward have been strengthened in relation to bad landlords. They not only strengthen the criminal penalties, but introduce new civil compensation. It is a fallacy to think that such tax relief increases the risks or potential for abuse. I shall deal with that point specifically. Amendments Nos. 239, 240 and 241 deal with parallel trading which is an anti-avoidance provision to stop a business expansion scheme company being set up to take over an existing business which is then run down as a new business is built up. Where it applies, an individual who runs the existing business is not entitled to relief for any investment in the BES company. That is to prevent relief being given for an investment where the money is indirectly routed back to the investor. With rented property the scope for that is much less. One cannot envisage transfer pricing such as occurs between manufacturing companies. It is not easy to see the scope for parallel trading in the way that hon. Gentlemen fear. Paragraph 9 of schedule 4 provides a safeguard to prevent someone getting relief for investment in a company which takes over his existing property. With the necessary modification, section 302 of the Income and Corporation Taxes Act 1988 will prevent an individual getting BES relief if the company takes over letting activities previously carried on by the individual either alone or with others or by another company which he controlled. This provision also applies if the BES company simply acquires the properties which were previously let by the individual.

These amendments are unnecessary. I shall consider what hon. Members have said. If the hon. Gentleman withdraws the amendment, I shall consider putting forward an amendment on Report to strengthen these provisions. At the moment I do not think that that will be necessary, but I shall certainly consider it.

Amendment No. 238 involves paragraph 4 of schedule 4 which prevents an individual obtaining BES relief on an investment in a company if he is or becomes a tenant of a property let by the company. The amendment would extend the provision so that it would also apply if he were a sub-tenant. There is no problem because the individual would still be the tenant of a dwelling house of which the company was the landlord even though the company was not the individual's immediate landlord. We discussed this briefly during the debate on clause 49 and I explained that we were anxious to prevent any abuse of the relief. I should like to reflect further on the Opposition's point. If I can think of a way to strengthen the provision I shall bring it forward on Report. I hope that in the light of that assurance the hon. Member for Dunfermline, East (Mr. Brown) will not press the amendment.

The hon. Gentleman also tabled amendments which would lengthen the period for which a company has to satisfy the qualifying conditions for BES to be available. The amendments would substitute the proposed four years with 10, 20 or 25 years. That would effectively mean—in practice—locking people in with no possibility of selling their shares. We want to attract investment from the private sector. If an investor did not—in practice—have that freedom for 10, 20 or 25 years, that would make a complete mockery of the scheme and ruin it. No investor would participate in such a scheme.

I cannot believe that Opposition Members are seriously proposing that to attract private risk capital people must undertake to invest for 25 years. Such a

[Mr. Lamont.]

condition applies to no other investment and would be profoundly and dramatically unattractive to investors.

The hon. Member for Dunfermline, East adduced many arguments about the incentive to obtain vacant possession of a property. He said that, because of the CGT exemption, it was in the interests of a company to sell after four or five years. I must point out that the CGT exemption applies to shares; the hon. Gentleman built his argument on the CGT exemption applying to property, and said that that would give the landlord a tremendous incentive to seek vacant possession.

Mr. Gordon Brown: The Minister misrepresents me.

Mr. Lamont: The hon. Gentleman did say that and it was repeated by some of his hon. Friends. Either he misunderstands, in which case his point has some logic, or he understands correctly, in which case his argument is irrelevant and illogical. The hon. Gentleman must decide which it is.

I assume that amendment No. 233 seeks to ensure that, where a rent officer determines the market rent to be eligible for rent allowance subsidy, if the landlord charges a higher rent the letting will not be treated as qualifying for BES relief. The Opposition are saying that, where the tenant happens to be claiming housing benefit and the landlord is a BES company, a form of rent control should be introduced.

It will not surprise hon. Members that we cannot accept the amendment. We are in the process of abolishing one form of rent control and do not intend to invent another for lettings by BES companies. A key feature of the new assured tenancy regime is that landlord and tenant are free to agree the rent and other terms of the tenancy at the outset. Those other terms might include a rent review clause. If there is such a clause, the tenant will be bound by what he has agreed to.

The Government have undertaken that housing benefit will be available to support the market rents that emerge from the new policy. Claims for housing benefit from private tenants will be scrutinised by rent officers to check that they are acceptable for subsidy purposes using a test based on the market rents being paid by other tenants who are not claiming benefit. There will be no attempt to hold the rents of tenants receiving benefit below market levels. However, some mechanism is needed to avoid collusion between landlords and tenants. As I said, the rent officer's determination will be used for fixing subsidies. He will not normally set a limit on the benefit, which is a matter for the local authority, nor will he fix the statutory maximum rent for the tenancy.

9.30 pm

The level of benefit that the tenant receives will be decided by the local authority. The subsidy decision that underlies it will be a matter for the authority and the rent officer. Those issues will not affect the landlord; he is entitled to recover the rent under the tenancy agreement. If the tenancy agreement has a rent review clause which turns out to be disadvantageous to the tenant because his rent increases faster than the market rate, benefit will not necessarily be payable on the increased rent. But that should not affect the landlord's right to recovery.

Mr. Darling: Does not the Minister accept that the maximum amount of money that the local authority can pay depends on the amount of money that the Government will reimburse? If the local authority pays more than that it is penalised, so it is not true that it is up to the local authority to decide. Its hands are tied by central Government.

To return to my earlier point, what happens if a tenant is charged a rent that is way above his housing benefit? What is he supposed to do, given the shortage of accommodation?

Mr. Lamont: On the first point, it is a matter between the tenant and the local authority, notwithstanding what the hon. Gentleman said about Government support for rent allowance schemes. The relationship between the tenant and the local authority differs from that between the landlord and the tenant.

The tenant must determine what to do if the housing benefit does not cover the market rent. It would be wrong to enshrine in law a provision that no rent can be payable other than that determined by a housing officer. That would be contrary to the purpose of the scheme.

The real point of the debate has been to decide whether we need a revival of the private rented sector. My hon. Friends and I emphatically say yes. It has been in decline in this country for many years.

[*Interruption.*]

The hon. Member for Newcastle upon Tyne, East says yes as though he does not think that there is any purpose in a revival of the private rented sector, but it is overwhelmingly in the national interest. The lack of private rented accommodation is an enormous impediment to the mobility of labour. People are locked into areas of high unemployment, because they are unable to move to where there are jobs. Britain needs to develop a private rented sector, as many other European countries have done.

I agree with Opposition Members that the growth in owner occupation is linked to the decline in the private rented sector. It is to deny common sense and the laws of gravity to suggest that the penal rent and landlord legislation, which Britain has had for generations, has not also played a part. How can we expect people to rent out houses when they are denied a return comparable to that from other investments?

Opposition Members speak as though all tenants were saints and all landlords dragons. My hon. Friends know that many landlords are poorer than their tenants.

[*Interruption.*]

Not all, that is true, but Opposition Members appear to be unaware that the majority of landlords are small

landlords. They are not the people that they are often imagined to be. They do not all manipulate large blocks in north Kensington. Rented accommodation in the inner cities is often in poor repair because landlords cannot afford to maintain the properties. Opposition Members perpetrate the illusion that accommodation can be cheap and in plentiful supply. They talk about tenants being exploited, but it is they who exploit them by perpetrating that illusion. The rented sector has been declining for years. There are about 1½ million people living in privately rented accommodation and if the private sector continues to decline, there will be the problem of rehousing them.

Clearly we need a thriving privately rented sector. The Opposition's main argument against it is the cry of Rachmanism, which is one of those words that is essential to the survival of the Labour party. Rachmanism and all that it stands for is to be condemned thoroughly. Rachmanism is likely when security of tenure and controls on the rent that may be charged mean that the landlord has an enormous incentive to get vacant possession. Abuse is bound to happen if the landlord has no right to occupy his own property, however long the time that passes. When people get a miserable, controlled return on their investment—2 or 3 per cent on vacant possession value; 1 per cent in London—abuses are bound to happen. Controls breed abuses such as we saw in the 1960s and which Opposition Members rightly condemn.

Bad landlords and abuses are less likely if a landlord can get an economic return on his investment and can ultimately have control of his property after he has honoured obligations to his tenant. When a property with vacant possession has a similar value to one that is occupied abuse is least likely. If economic rents are more the norm, there will be less incentive for people to use harassment and the tactics that Opposition Members have described because a property tenanted and a property vacant will have similar values.

The hon. Member for Cardiff, West (Mr. Morgan) gave the game away in his argument. It showed that the Opposition are not really interested in the pros and cons of the argument but only in misrepresenting it. The hon. Gentleman claimed that young people who want to get into the housing market will not be able to do so because BES schemes and landlords will drive them out: landlords will buy all the property and force up house prices. So, on the one hand, Opposition Members say that everyone will go for vacant possession, driving everyone out of their homes to make huge capital gains, and on the other, the hon. Member for Cardiff, West argues that no one will be able to live in a house because they will all be bought for rented accommodation. Which is it?

The Housing Bill has adequate safeguards. If it were not for the attitude taken by the Labour party for generations we might have had a better chance to develop a privately rented housing sector, but the provisions in the schedule are necessary to give that extra incentive to develop the scheme as we all want it.

Mr. Campbell-Savours: I know that the Minister has sat down, but perhaps he will deal with this matter later.

My hon. Friend the Member for Cardiff, West (Mr. Morgan) made an allegation which the Minister dismissed with a smile and said that it was not possible. If what my hon. Friend said happens, will the Minister review the scheme? My hon. Friend's contribution was erudite in that it established a principle that developers may follow. It may affect the ability of young people to acquire property. If my hon. Friend's allegation is proven, what will the Minister do?

Mr. Lamont: The point that I wanted to make was that everything that the hon. Member for Cardiff, West said was inconsistent with the rest of the Opposition's argument. Of course we shall review the scheme after a couple of years, but I prophesy that all the Opposition's fears will turn out to be utterly groundless. If action needs to be taken, we shall not hesitate to take it.

Mr. Gordon Brown: It has been a measure of the fears of all Opposition Members that so many from different parts of the country have spoken about what will happen as a result of the scheme. That is why so many amendments have been tabled for discussion this evening, some of which the Minister has at last admitted are of considerable concern to him too.

I appreciate that the Minister has promised to look again at our amendments on sub-tenancies and parallel trades, so we shall not press those matters to a vote this evening. However, it will be a test of what happens when the Minister offers to consider amendments. I hope that he will write to me quickly so that we can decide how to proceed on Report.

The Minister did not satisfy the Committee on all the other major issues. He did not answer our detailed questions nor the direct question put by one of his hon. Friends. Our argument is clear. The public money going to the business expansion scheme which is about £40 million according to the budget estimate but may be more, would be better spent securing more properties in the rented sector by giving that money to the Association of Metropolitan Authorities housing authorities or housing associations. Conservative Members have been unable during the Committee stage on the Floor of the House or in this evening's debate to deny that ten times as many houses could be started or repaired if that money was given to local authorities.

Our second point is unanswerable. If public money is put into such a scheme, the Government must have the right to lay down proper conditions for its operation. It is incomprehensible why the Government have excluded from the scheme an obligation by landlords to act in a socially responsible way by being signatories to the social landlords' charter. When persons, companies and housing associations buying council houses are subject to that charter—however ineffective—and when the Minister for Housing and Planning described it as a means by which anti-social landlords could be eliminated, why are landlords under the business expansion scheme to be excluded? The Minister has given no reasons, although he has a lever at his disposal in the amounts of public money going to those landlords. When the Minister gave a theoretical explanation, that regulations, red tape and bureaucracy where bad in themselves, he really meant that even when the Government know that circumstances or

[Mr. Gordon Brown.]

activities are unfair, they will refuse to legislate against them because more regulations, red tape and bureaucracy will result. Abuses must not be allowed to take place.

Mr. Butterfill: Does the hon. Gentleman agree that a major difference in principle exists between reassuring tenants of public bodies that their interests will be protected and providing the same degree of reassurance for people who are not yet tenants but who will become part of a private contract between landlord and tenant on freely agreed terms? There is all the difference in the world between those two positions.

Mr. Gordon Brown: The whole question is about the balance of power between the landlord and the tenant. The Government are in a position to protect the tenant and refuse to do so. I see no difference between a public sector tenant and a private sector tenant, because both need protection from irresponsible landlords. The hon. Gentleman's point was raised by his right honourable Friend's question with which the Minister found difficult to cope. The Financial Secretary asked for a guarantee that criminal landlords such as Mr. Hoogstraten would be debarred from benefiting from the business expansion scheme. Despite all the Minister's rhetoric, the answer was no. Mr. Hoogstraten and his friends and people in other parts of the country with similar records will be able to benefit from the tax reliefs available under the scheme, from the rent decontrol, which is the basis of the scheme, and from the capital gains tax exemptions in the shares of the company as the companies are sold.

The concerns of the hon. Member for Bournemouth, West (Mr. Butterfill) require him to vote against the Government's proposals this evening and to support the amendment, which would oblige landlords to undertake to abide by the social landlords' charter.

9.45 pm

Mr. Nicholson: I would not wish to be in my right honourable Friend's shoes if it were found that the person whom he named were benefiting from the business expansion scheme, but I am prepared to abide by my right honourable Friend's assurances.

Mr. Brown: The problem is that the right honourable Gentleman is unable to give the hon. Member for Bournemouth, West those assurances. I shall be happy to give way to the Financial Secretary if he can give the assurances that his hon. Friend seeks. The Minister's silence now and his failure to give a direct answer to the question means that he cannot give the assurances requested.

Mr. Lamont: The hon. Gentleman is ignoring two considerations. First, the Housing Bill contains a considerable strengthening of the laws against what Opposition Members have called bad landlordism. New criminal penalties and civil actions are open to tenants. They are protections against bad landlords.

Secondly, the hon. Gentleman talks as though people can qualify for business expansion scheme relief without making new accommodation available. BES relief is not available for accommodation that is already tenanted. A recipient must make available new property, new supply and more homes.

Mr. Brown: But the Minister does not seem to understand what the debate on the Floor of the House is about. It is about changing the balance between the landlord and tenant to increase the powers available to the landlord. On the question of repossession, which the Minister raised, it is clear that whereas previously it might have been more difficult for a landlord to repossess, it will now be easier for him to repossess the property after five years. Otherwise, it would not be a mandatory reason under which eviction could take place.

The whole process of the legislation and the introduction of these mandatory clauses weakens tenants' rights. The tragedy is that if tenants' rights are made weaker under the Bill, under the business expansion scheme those rights will be even weaker because people will be unable to rely on the social landlords' charter.

I said that I had no intention of detaining the Committee further. The gains to the landlords from these measures are clear—vast sums of tax relief, income tax relief at the outset and capital gains exemptions on their shares as the project concludes. In the middle is rent decontrol which, as the Minister has conceded, will allow landlords to charge any rent that they wish.

There is a huge danger that the public subsidies will not go to provide rented accommodation for migrant workers from the north, as the Chief Secretary said that they would. We have heard little about that aspect from the Minister this evening, which was the chief justification for the scheme. The danger is that we are involved in a programme of state subsidies for fairly expensive flats for executives—perhaps international executives at that—who will use them as second homes when they are in the capital.

Mr. Matthew Carrington (Fulham): I listened to the debate with some interest. The hon. Member for Dunfermline, East (Mr. Brown) will be aware that there is a limit on the capital value of dwellings that can be used for BES. I think that in central London the figure is £125,000. I regret that in central London £125,000 does not buy a great deal of accommodation. In my constituency, which is by no means prime residential land in central London, £125,000 will barely buy a one-bedroomed flat.

Mr. Brown: But the hon. Member for Fulham (Mr. Carrington) forgets that a public subsidy may go to a company that buys a house for £125,000 and then rents it out—for example, to an executive using it as a second home. What can possibly be the argument for giving that public subsidy? If that is the likely result in at least a proportion of the cases where subsidy is involved, how can Conservative Members justify it?

It is difficult to see how the 50,000 homeless in London will benefit directly from the scheme. I should be very surprised if many of them were in business expansion scheme rented properties by the time the Minister conducts his survey after two years. We already know that very few jobs are likely to result from the scheme, and the old argument for public subsidies for BES has now almost disappeared from the Minister's armoury of arguments. Vast sums of public money are going to the scheme; few conditions are applied to the granting of that money, and it could be far better spent in the housing association movement or the public sector.

The tragedy is that the Government would prefer that the private sector did the job inefficiently than that the public sector did it efficiently. That is why we have the business expansion scheme in preference to funding our housing throughout the country in local authorities. I urge my hon. Friends to vote for our amendments against the schedule that is now central to the Bill.

Question put, That the amendment be made:

The Committee divided: Ayes 14, Noes 23.

AYES	
Armstrong, Ms Hilary	Henderson, Mr. Doug
Battle, Mr. John	Ingram, Mr. Adam
Brown, Mr. Gordon	Marek, Dr. John
Brown, Mr. Nicholas	Smith, Mr. Andrew
Campbell-Savours, Mr. D. N.	Smith, Mr. Chris
Darling, Mr. Alistair	Wallace, Mr. James
Griffiths, Mr. Nigel	Worthington, Mr. Tony

NOES	
Arbuthnot, Mr. James	Lamont, Mr. Norman
Boswell, Mr. Tim	Lennox-Boyd, Mr. Mark
Bright, Mr. Graham	Maples, Mr. John
Butterfill, Mr. John	Mitchell, Mr. Andrew
Carrington, Mr. Matthew	Nicholson, Mr. David
Coombs, Mr. Anthony	Shaw, Mr David
Davies, Mr. Quentin	Stern, Mr. Michael
Favell, Mr. Tony	Taylor, Mr. Ian
Forman, Mr. Nigel	Wardle, Mr. Charles
Howarth, Mr. Gerald	Watts, Mr. John
Hunter, Mr. Andrew	Widdecombe, Miss Ann
Jack, Mr. Michael	

Question accordingly negatived.

The Chairman: It has been put to me that Government amendments Nos. 256 and 257 would more appropriately be debated under clause 50. Subject to the agreement of the Committee, I am prepared so to rule.

Mr. Lamont: I beg to move amendment No. 258, in page 123, line 36, leave out "(3)" and insert "(4)".

The Chairman: With this we may take Government amendment No. 259.

Mr. Lamont: Paragraph 3 of schedule 4 places a limit of £5 million on the amount of BES finance that may be raised in any year by a company specialising in letting residential properties. It does that by applying with modification the new section 290A of the Income and Corporation Taxes Act 1988, which is introduced by clause 50. Subparagraphs (2) and (3) make the necessary modifications, but the references therein to subsections of section 290A are incorrect. The amendments insert the correct references. I think that Opposition Members had lighted on the same point.

Amendment agreed to.

Amendment made: No. 259, in page 123, line 39, leave out "(5), (6) and (8)" and insert "(6), (7), (9) and (10)".—[*Mr. Norman Lamont.*]

Amendment proposed: No. 229, in page 124, line 19, at end insert

", and

(c) a company which has been approved by the Housing Corporation and which has formally adopted and implements the Social Landlords Charter, and

(d) a company where its and its qualifying subsidiaries qualifying activites are such that each dwelling-house let in connection with the qualifying activities is so let or available for letting throughout the period commencing with the date when first let to the end of the relevant period.".—[*Mr. Gordon Brown.*]

Question put, That the amendment be made:

The Committee divided: Ayes 14, Noes 21.

AYES	
Armstrong, Ms Hilary	Henderson, Mr. Doug
Battle, Mr. John	Ingram, Mr. Adam
Brown, Mr. Gordon	Marek, Dr. John
Brown, Mr. Nicholas	Smith, Mr. Andrew
Campbell-Savours, Mr. D. N.	Smith, Mr. Chris
Darling, Mr. Alistair	Wallace, Mr. James
Griffiths, Mr. Nigel	Worthington, Mr. Tony

NOES	
Arbuthnot, Mr. James	Lamont, Mr. Norman
Boswell, Mr. Tim	Lennox-Boyd, Mr. Mark
Bright, Mr. Graham	Maples, Mr. John
Butterfill, Mr. John	Mitchell, Mr. Andrew
Carrington, Mr. Matthew	Nicholson, Mr. David
Coombs, Mr. Anthony	Shaw, Mr. David
Davies, Mr. Quentin	Stern, Mr. Michael
Favell, Mr. Tony	Taylor, Mr. Ian
Forman, Mr. Nigel	Wardle, Mr. Charles
Howarth, Mr. Gerald	Widdecombe, Miss Ann
Jack, Mr. Michael	

Question accordingly negatived.

Question proposed, That this schedule, as amended, be the Fourth schedule to the Bill.

Mr. Lamont: We have had a full debate on the schedule, but I should like to say a word about the application of the relief to Northern Ireland. The market for rented housing there is already deregulated to a substantial extent, and so the new assured tenancy scheme will not apply in Northern Ireland. As the BES relief in the Finance Bill is linked to the assured tenancy scheme, it follows that this BES relief would not be available in Northern Ireland. But although Northern Ireland does not have the same shortage of rented accommodation as there is in many parts of Great Britain there is a shortage of good modern rented housing. We therefore propose to bring forward amendments on Report to extend the relief to Northern Ireland. They will include a power to make regulations to set out what kinds of tenancy will qualify. Our intention is that those tenancies will be similar to assured tenancies, both in terms of the type of property and of security of tenure.

[Mr. Lamont.]

We intend to propose another change on Report. Under the Bill as drafted it would be possible for the tenant to be given an option to buy the property, no doubt at a small discount, after the end of the four-year period. There is nothing intrinsically wrong in that, but our aim in giving the BES relief is to try to encourage the long-term provision of rented property. Therefore, we shall table amendments to disqualify a tenancy if there is an option to purchase the property.

Mr. Wallace: I shall not detain the Committee, but in the past two days, the Law Society of Scotland has sent me its comments, two of which are relevant. I do not know whether the Minister has seen them. They relate to the definition of the words "any interest in it" in paragraph 13(4)(c) which, in Scots law, could apply to a superiority. That, I am sure, is not intended. Likewise, "the relevant date" on which an interest is first acquired could, in Scots law, cause confusion as to whether it is when missives are concluded or when a disposition is delivered. Will the Minister look again at these issues before Report so that we may have clarification of Scots law?

Mr. Lamont: I have not seen any of the points that were raised by the Law Society of Scotland. I shall look at them and, if necessary, come back on Report. I shall also be in touch with the hon. Gentleman.

10 pm

Question put, That this schedule, as amended, be the Fourth schedule to the Bill.

The Committee divided: Ayes 21, Noes 14.

AYES

Arbuthnot, Mr. James	**Lamont, Mr. Norman**
Boswell, Mr. Tim	**Lennox-Boyd, Mr. Mark**
Bright, Mr. Graham	**Maples, Mr. John**
Butterfill, Mr. John	**Mitchell, Mr. Andrew**
Carrington, Mr. Matthew	**Nicholson, Mr. David**
Coombs, Mr. Anthony	**Shaw, Mr. David**
Davies, Mr. Quentin	**Stern, Mr. Michael**
Favell, Mr. Tony	**Taylor, Mr. Ian**
Forman, Mr. Nigel	**Wardle, Mr. Charles**
Howarth, Mr. Gerald	**Widdecombe, Miss Ann**
Jack, Mr. Michael	

NOES

Armstrong, Ms Hilary	**Henderson, Mr. Doug**
Battle, Mr. John	**Ingram, Mr. Adam**
Brown, Mr. Gordon	**Marek, Dr. John**
Brown, Mr. Nicholas	**Smith, Mr. Andrew**
Campbell-Savours, Mr. D. N.	**Smith, Mr. Chris**
Darling, Mr. Alistair	**Wallace, Mr. James**
Griffiths, Mr. Nigel	**Worthington, Mr. Tony**

Question accordingly agreed to.

Schedule 4, as amended, agreed to.

Clause 50

RESTRICTION OF RELIEF

Mr. Lamont: I beg to move amendment No. 256 in page 49, line 37, after "with", insert

"the following amendments, namely—

(a) in section 289(12)(b), the substitution of the words 'sections 290A, 293' for the words 'sections 293', and

(b) "

The Chairman: With this it will be convenient to discuss Government amendment No. 257.

Mr. Lamont: The amendments seek to remove a drafting defect. Clause 50 imposes a limit on the total amount of investment in a company that qualifies for BES relief in any year. It does this by inserting a new section 290A in the Income and Corporation Taxes Act 1988. Subsection (4) would reduce the £500,000 limit where the company carries on a trade with other companies at any time within the relevant period, which at present has no definition. In the BES legislation, it has two possible meanings. The amendments are necessary to make it.clear which is to apply.

Amendment agreed to.

Mr. Chris Smith (Islington, South and Finsbury): I beg to move amendment No. 236, in Clause 50, page 49, line 46, at end insert

"and shall only be given after 5 April 1989 if the company and any of its qualifying subsidiaries would not be precluded from being a qualifying company by virtue of section 294 if in that section the word 'half' were replaced by 'one-third' ".

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

No. 235, in page 49, line 46, at end insert—

"(1A) Where a company and each of its subsidiaries is a company whose activities fall within Standard Industrial Classification Groups 2, 3 and 4, Chapter III of this Part shall apply as though section 294 were deleted."

No. 237, in page 49, line 46, at end insert—

"(1A)(a) Where a company raises any amount through the issue of eligible shares after 5 April 1989, no relief shall be available unless the trade, if any, of a qualifying company and of each of its qualifying subsidiaries is an eligible trade.

(b) An eligible trade for the purpose of this subsection is a trade such as is specified in a Schedule to be introduced by Statutory Instruments subject to an affirmative resolution of the House of Commons, such Schedule to have regard *inter alia* to the following factors:

(i) The encouragement of manufacturing industry;

(ii) The enhancement of research and development opportunities;

(iii) The need to achieve a balanced regional dimension; and

(iv) The efficiency of employment enhancement measures in terms of costs per job".

Mr. Smith: We are now discussing the business expansion scheme as a whole rather than its application to the new scheme that the Government intend to implement relative to the provision of rented property.

The Opposition have two principal objections to the BES. The first is that it is not an efficient way of raising risk finance for small companies; the second is that it could be used as a tax shelter for the rich. There is nothing intrinsically wrong—indeed, there is much to welcome—in the principle of using the fiscal system to endeavour to encourage investment in new enterprise. However, the business expansion scheme is not a

terribly good mechanism for doing so. I shall explain why.

On the question of the tax shelter opportunities that are available under the BES, the Government changed drastically the position of the tax shelter aspect with the introduction of the rented property scheme.

It is now almost certain that because the rented property scheme will mean a limit of £5 million rather than £500,000 for the company, and because it will be substantially asset-backed and therefore much less risky than most of the other potential BES investment opportunities, the funds which hitherto have gone into other sectors of enterprise and industry through the BES will in future be directed towards the new property scheme rather than into any other of the possible opportunities. By introducing that property scheme, the Government are introducing a massive distortion. I shall return to that matter because of its importance to the future operation of the scheme.

However, as a tax shelter, the BES does and will remain.

10.5 pm

Sitting suspended for a Division in the House.

10.21 pm

On resuming—

Mr. Chris Smith: Before we suspended for a Division in the House, I was saying that the tax haven nature of the business expansion scheme will remain after the changes which the Government are introducing to provide restrictions on the scheme. For confirmation of that point, where else should I look but in *Accountancy Age* of 24 March. In immediate response to the Budget changes on the business expansion scheme, it contained an article headed in bold letters:

"BES will continue to be attractive as a tax shelter".

What the writer of the article said perhaps reveals more about the attitude towards tax shelter mechanisms among those who employ them than anything else which I have come across in recent months. She wrote:

"Sheltering money is a game and it's fun. And now that Nigel Lawson has abolished forestry tax breaks there are only a few legitimate shelters left—enterprise zones, pensions (long-term and not as exciting) and"

—this is the key—"BES." Clearly, BES remains a prime tax shelter.

Earlier, I spoke about how the scheme will be distorted by the Government's rented housing proposals. That view is reinforced later in the article which quotes Kevin Barker, the joint managing director of Johnson Fry which, of course, is the United Kingdom's leading sponsor of BES issues. Kevin Barker said:

"We will be concentrating a lot of time on assured tenancies to the exclusion of smaller companies."

That will be the effect of the introduction of the assured tenancy scheme under the BES—a much more attractive tax shelter proposition than any mainstream BES enterprise. It will focus attention on that rather than on the other traditional occupations which might be promoted in some circumstances by some BES proposals.

We have several considerable reservations about the operation of the BES as a generator of investment finance for small business. The Government are fond of citing the Peat Marwick report.

Mr. Lamont: Is this on the amendments?

Mr. Smith: It is on an amendment and I shall deal specifically with the amendments in a moment, Mr. Hunt.

The Peat Marwick report, which stands high in the Government's regard, deals only with the first year of the scheme's operation. That is crucial consideration which the Government continually fail to acknowledge. Many aspects of the scheme that the Peat Marwick report found relatively sound and successful have changed over the years as the nature of takeup under the scheme has changed. The amendments seek to tackle those changes.

Amendment No. 236 seeks to change the asset base rule for BES companies from a limitation on assets to a figure of one half to a limitation of a figure of one third. Amendment No. 235 would give a deliberate boost to the manufacturing trades which could be promoted under the business expansion scheme by removing entirely the limit of one third for manufacturing trades. Amendment No. 237 seeks to instruct the Secretary of State to establish a list of activities that will qualify for BES relief. We specifically tell the Secretary of State that in drawing up that list he must have regard to a number of important considerations. These are:

"(i) The encouragement of manufacturing industry;

(ii) The enhancement of research and development opportunities;

(iii) The need to achieve a balanced regional dimension; and

(iv) The efficiency of employment enhancement measures in terms of costs per job.".

We specifically list those criteria because they are aspects on which the business expansion scheme is falling down at present.

It is perhaps opportune that this debate comes only a few days after the Small Business Research Trust published its analysis and study of the operation of the business expansion scheme. Unlike the Peat Marwick report, it did not simply look at the first year of the scheme. It examined the scheme from its inception until the present day. The Small Business Research Trust report is extremely revealing and discloses a number of serious failings of the scheme. For example, the report says that the growth in prospectus issues over the past few years has been considerable and that something like 70 per cent of the finance invested through the scheme in 1985–86 was in companies that raised more than £500,000.

[Mr. Smith.]

The clause contains a specific provision—the limit of £500,000—to tackle precisely that problem and it is likely that the number of prospectus issues, rather than fund issues, will decline as a result. That will not necessarily be the case for the property scheme, but it will for other parts of the BES.

We welcome the establishment of a limit, but the Government have not done enough to tackle the other problems that the Small Business Research Trust throws up in its study. First, the report says that

"the Scheme has not assisted significant numbers of high-risk businesses".

On the whole, the businesses started up by the BES in recent years have tended to be asset-backed and low risk and have not fallen into accord with the spirit of the scheme as it was first established in 1983.

Secondly, the proportion of total finance—not the number of companies—invested through the BES in the manufacturing sector has declined from around one third in 1983–84 to under a quarter in 1985–86.

10.30 pm

The final tables in the report, which bring the figures up-do-date for the year 1987–88, and the industrial distribution of companies show that in categories three and four, the principle manufacturing categories, the number of investee companies as a percentage of the total in category 3 was 7 per cent, and in category 4 it was 5 per cent. In terms of the amount invested, the picture is even worse. The amount invested in category 3 was 2 per cent, and in category 4 it was 1 per cent. Therefore, a grand total of 3 per cent of the overall amount invested in 1987–88 went to the categories relating to manufacturing industry.

Most of the funds have gone to construction—28 per cent; wholesale and retail distribution and hotels and restaurants together have received 42 per cent. That is where the BES money has gone. Opposition Members do not believe that that is necessarily a good way to use taxpayers' money as an incentive for enterprise.

Mr. Campbell-Savours: I have not read that report, but I wonder whether many of these schemes are being supported because they are heavily asset backed. The scheme was originally set up and, as I understand it, still operates, to break the relationship between the entrepreneur and the investor. Perhaps a scheme could be devised to bridge that gap without letting through an avalanche of rogues and people who want to cheat the system, so that we could change that relationship to favour the riskier investment, which is what my hon. Friend and I want.

Mr. Smith: My hon. Friend makes a valid point. Indeed, that point was made by the Small Business Research Trust study. It says that that is a rigid rule in the scheme which divorces the investor of funds from the management of the enterprise that is established and, arguably, that can act to the detriment of the enterprise itself. The study argues for a much more hands-on approach for the investor. There are obvious dangers in that and I would not necessarily embrace that immediately without strong safeguards being introduced for operating that hands-on approach. My hon. Friend's point is extremely important.

Mr. Campbell-Savours: I have not spent long in Committee but earlier this evening the Minister made a statement about the need to link private funds with public funds in the sense that the taxpayer was investing his funds and the linkage of the two made for a better package than simply public sector investment.

In this case, could there be some regional framework—that will not help my hon. Friend whose constituency is in London—within tax law to help companies in certain parts of the United Kingdom perhaps with a more flexible arrangement to govern the operation of this scheme which will also meet the objectives to which I referred before and about which my hon. Friend has expressed quite natural reservations?

Mr. Smith: Again, my hon. Friend anticipates a point made by the Small Business Research Trust. It, too, has raised the point about regional patterns of investment. If the scheme were operated more on a regional basis, it would be more effective and would improve the risk-taking nature of the enterprises involved.

Mr. Graham Bright (Luton, South): The hon. Member for Islington, South and Finsbury read out some percentages and said that a considerable amount of the money invested went into construction, hotels and so on. Does he agree that when such activities are analysed, they represent considerably more than £500,000? The figures run into millions of pounds. Some hotels have gobbled up as much as £18 million. The restriction proposed in the clause would swing that percentage back. Does the hon. Gentleman agree?

Mr. Chris Smith: The hon. Gentleman clearly has not looked at table 5.1 in the Small Business Research Trust study.

Mr. Bright: No, I have not seen it.

Mr. Smith: It is extremely interesting and I recommend it to the hon. Gentleman. It shows that his point is partially right. The balance below the £500,000 limit between manufacturing and hotel, catering and service industries is more in favour of manufacturing than it is above the £500,000 limit, but there is still an imbalance. Even below the £500,000 mark a considerable amount goes into hotels, catering and similar activities.

Mr. Bright: Does the hon. Gentleman agree that the percentage distortion is so great because above the £500,000 mark the amount of cash is considerably higher than that? That is my point. If it were restricted, there would be a better redistribution below the £500,000 mark. That is what distorts the figures at present.

Mr. Smith: It will not remove the distortion entirely.

Mr. Bright: I accept that.

Mr. Smith: That is one of the reasons why amendment No. 237 goes further than the Government, who propose the £500,000 limit. We support that but we want to go further and include a specific promotion of manufacturing industry in our suggestions for improving the scheme.

The hon. Gentleman ignores the fact that for the rented property scheme, the limit of £500,000 will not apply. The limit will be £5 million. That will have an immense impact on people trying to decide which scheme to invest in.

Mr. Quentin Davies (Stamford and Spalding): Would the hon. Gentleman care to enlighten the Committee about the economic principle on which he bases his assumption that distribution, hotel and other service activities are inherently less desirable than manufacturing?

Mr. Smith: I base my assumption on the eminently sensible approach to our economic life which argues that it is right to have a balance between manufacturing investment and investment in other activities. The present balance attained by the business expansion scheme is not right.

If the hon. Gentleman thinks that the wine bars, the wine companies, the helium gas-filled balloon to be sent across the Atlantic—all of which have been financed through the business expansion scheme—are enterprises worthy of being financed and supported by taxpayers' money, we shall have to disagree.

The Chairman: Order. We cannot now have a general debate on the entire business expansion scheme. I hope that the hon. Gentleman will limit his remarks to the amendments before the Committee.

Mr. Chris Smith: I shall, of course, accord with your ruling, Mr. Hunt. I must not allow Conservative interventions to tempt me into transgressing the rules of debate.

Our amendments seek to address the problems which are associated with the business expansion scheme and which are highlighted in the Small Business Research Trust study. I have already referred to the significant increase in asset-backed low-risk enterprises and the balance which at present tends to be against manufacturing rather than in its favour.

The research study throws up two further points. The first is that the scheme is relatively expensive in terms of employment promotion on a cost-per-job basis. The report says that there is

"an increase in the cost-per-job (which even in 1983–84"—

at the very start of the scheme—

"was higher than that for other small firm schemes)."

Clearly, in terms of job creation, the position was bad in 1983–84 in relation to cost per job, but it has been getting worse since, and in our amendment No. 237 we seek to direct the Secretary of State's attention to the problem.

However, the worst aspect of the business expansion scheme is the way in which it has operated in favour of the south-east and against other regions. One has only to look at the figures for BES investment in the south-east. In 1985–86, the amount invested in the south-east, in percentage terms of the total amount invested through BES, was 72.1 per cent—that amount was invested in just one region, the south-east. In 1987–88, 62 per cent went to the south-east through prospectus issues, and in the same period 46 per cent went to the same region through fund issues. So it is clear that an enormous percentage of BES funding goes to companies in the south-east of England.

The south-east of England benefits not only in terms of the overall proportion: it gains a net increase of BES funding; there is a net flow of funds. More people are investing in the south-east from outside the south-east through the BES than are investing in their own regions.

So it is evident that many problems are associated with the business expansion scheme. It is expensive in terms of cost per job; it is biased against manufacturing and in favour of service industries; it is grossly biased on a regional basis and—

Mr. Campbell-Savours: In his reading of the report, has my hon. Friend been able to identify the reasons for the concentration of BES resources in the south-east of England? Is it linked in any way to property prices and the concentration of wealth, or is it linked to higher incomes? There must be some reason for it.

Mr. Smith: It relates partly to higher incomes, because higher-income earners tend to be concentrated in the south-east, and that means that they will produce more investment funds through the BES. However, that does not explain the net inflow of funds from outside the area. The way in which BES funds seek out the least risk is the opposite of what the scheme originally intended. As the scheme now operates, the funds seek out the lowest risk, and I suspect that it will inevitably lead the funds more towards the south-east than towards other parts of the country.

10.45 pm

Mr. Shaw: I make just one brief point. While the small Business Research Trust report, and other reports, have hinted that there have been regional problems, the amendment will cure many of those problems by limiting it to £500,000. I am sure that the hon. Memberr would recognise that the Small Business Research Trust report contains a number of suggestions about how limiting it to £500,000 will help not only the regions but the smaller risk investments. The table in the report which deals with the funds shows that they have a better record of investing in manufacturing industry than others.

I should like the hon. Member to reflect on the following point. When he talks about cost per job he is out of date; no studies have yet been carried out of which I am aware of the tax that successful companies

[Mr. Shaw.]

have paid. Many of these companies have been trading for only one, two, three, four or five years. One company in which I am involved will have paid more in total taxation to the Exchequer this year than it received in tax relief under the business expansion scheme. The net cost per job will be negative.

Mr. Smith: I always respect the hon. Gentleman's experience of the business expansion scheme as he has been involved in so many. His point about successful companies may well be right. But the overall pattern at present belies the picture that he painted. When the hon. Member suggests that the £500,000 limit would go some way to cure the regional problem he ignores the figures in table 5.2 in the Small Business Research Trust study which clearly demonstrate that a higher proportion of those issues over £500,000 go to the south-east. Of prospectus issues over £500,000, 66.5 per cent go to the south-east and 54.3 per cent of fund or scheme investments go to the south-east.

The figures for issues under £500,000 show that 63.2 per cent of prospectus issues and 47.3 per cent of fund or scheme investments go to the south-east. Although there is a marginal difference and a marginal improvement on the regional imbalance when the £500,000 limit is applied it does not solve the problem.

Mr. Campbell-Savours: Will my hon. Friend give way?

Mr. Smith: I am sorry, but I must get on. Although we welcome the fact that the Government have moved towards establishing a limit we do not believe that that by itself will cure the problems, especially the problems of regional and manufacturing imbalance within the business expansion scheme at present. I commend the amendments to the Committee.

Mr. Lamont: Although there is one point in the amendments tabled by the hon. Member for Islington, South and Finsbury (Mr. Smith) which I shall look at, I do not accept the general premise and philosophy behind them. As my hon. Friend the Member for Stamford and Spalding (Mr. Davies) pointed out, the amendments seem to assume that investment in one sector of the economy is better than investment in other sectors. Although I am prepared to admit that it is not something to be wildly applauded because there have been so many asset-backed investments, the fact that there have been investments in the service sector is not to be regretted. That is why I cannot accept the thrust of the hon. Gentleman's amendments.

Amendment No. 236 would tighten the existing land and buildings restriction so that only one third, instead of one half, of a company's net assets could take the form of land and buildings. There is no evidence that the restriction needs to be tightened. Furthermore the £500,000 limit is likely to have a dramatic impact on the amount of asset-backed companies, as I am sure my hon. Friend the Member for Dover (Mr. Shaw) will agree. However, the hon. Gentleman may have the kernel of an idea in amendment No. 235, which seeks to prevent the existing land and buildings restriction applying to a company that carries on manufacturing activities. Part of the amendment deals with fixed plant as opposed to other plant. The hon. Gentleman may have had in mind extractive industries, such as the chemical industry, where plant is fixed and the asset value may be high.

I do not want to deal with the problem by taking the standard industrial classification and identifying good and bad activities. That would be a wrong approach, but I want to consider the problem that has been identified in terms of fixed plant to see whether there is another way to approach it. It is a difficult problem. I have studied the amendment tabled by the hon. Member for Islington, South and Finsbury and if he is prepared to withdraw that amendment from the three in this group, I shall consider it although I may not be able to do anything before Report.

The hon. Member for Islington, South and Finsbury has spoken at length and has quoted the Small Business Research Trust. He also made several points about the business expansion scheme. I do not want to detain the Committee because it is late, but the hon. Gentleman concentrated on several aspects and I want to make one point in response to his arguments.

A point that the hon. Gentleman missed and which was acknowledged by the Small Business Research Trust is that a main benefit of the business expansion scheme has been to make people in the City, in the institutions and the merchant banks, think about unquoted companies. They did not do that ten or 15 years ago. Of course there may have been several asset-backed investments, but the cultural change has been of enormous import. That is manifested not only in the amount of growth companies—the Small Business Research Trust acknowledges that many growth companies have been financed by the BES—but by the growth of the venture capital industry outside the BES. That is what it is all about.

The purpose is not to create many pensioner small businesses that are dependent on finance from the BES and supported by tax relief. The purpose of introducing the BES is to create a climate in which people invest in companies outside the normal quoted securities and not only in the Marks and Spencers and the ICIs of the small companies quoted on the stock exchange. There have been many changes in the unlisted securities market and the third market as well as the growth of the venture capital industry, which is now bigger in this country than in any other country in Europe. That is another reason why we can afford to lower the limit to £500,000: Other institutions and other people will pick up the job.

My hon. Friend the Member for Dover (Mr. Shaw) pointed out that in so far as the point made by the hon. Member for Islington, South and Finsbury applies, the proportion of manufacturing companies below £500,000 is far higher than the figures that the hon. Gentleman quoted, which were largely for prospectus issues. For all those issues, the figure is over 20 per cent for manufacturing. As my hon. Friend the Member for Dover said, below £500,000 the proportion of manufacturing is much greater.

The criticisms made by the hon. Member for Islington, South and Finsbury, and echoed by the Small

Business Research Trust, will, as my hon. Friend the Member for Dover said, be met by the £500,000 limit. That is one reason for bringing the proposal forward. The hon. Gentleman is scathing about the business expansion scheme. He seems to forget that, when we extended the scheme a few years ago and introduced the capital gains exemption that he bitterly criticised today, the Leader of the Opposition welcomed the proposals. The words "business expansion" somehow conveyed the right meaning to the Leader of the Opposition.

I do not deny that some of the points made by the hon. Member for Islington, South and Finsbury have force. Of course they do. However, the hon. Gentleman should acknowledge the good work of the business expansion scheme. The cap that we seek to introduce will deal with some of the other points that he raised.

Although I cannot accept amendments Nos 236 and 237, I shall consider one of the points raised by amendment No. 235.

Mr. Campbell-Savours: I wish to press the case for a regional basis for modifying the scheme. Has the Minister given further thought to that so that the scheme may have greater regional emphasis in its application?

Mr. Lamont: The problem with the regional dimension—as with the enterprise allowance—is that the take up reflects the culture in different regions of Britain. If there are fewer start-ups in the north, or the north-east, that reflects the fact that, traditionally, there are fewer entrepreneurs and small businesses in those areas. It is interesting that that is beginning to change.

The hon. Member for Newcastle upon Tyne, East (Mr. Brown) knows better than I that there is evidence that, in the north-east, the number of start ups has increased, and is dramatically better than it has been for many years. Attitudes in different regions are significant, so we are limited in what we can do. However, the cap that we shall introduce will encourage more small and manufacturing projects in the regions. That was impressed on us and is one of the reasons for the change. My hon. Friend the Member for Dover knows about local funds. Again, such funds will be much more interested in the smaller projects below £500,000. I cannot guarantee to solve the problem raised by the hon. Member for Workington (Mr. Campbell-Savours) but a limit on investment should take some investment to other areas, away from the concentration in the south. That is not only my interpretation—the hon. Member for Islington, South and Finsbury will acknowledge that other people, including the Small Business Research Trust, suggest that. If the hon. Gentleman will not press amendment No. 235, I shall consider at least the spirit of it.

Mr. Chris Smith: At this late hour, given the extremely constructive manner of the Financial Secretary's response, it would be churlish of me to do anything other than to beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

11 pm

Mr. Lamont: I beg to move amendment No. 252, in page 51, line 8, leave out "(a)".

The Chairman: With this, it will be convenient to take Government amendment Nos. 253 and 254, amendment No. 16, in page 51, line 17, at end insert—

"(c) it consists of operating ships which satisfy the requirements mentioned in paragraphs (b) and (c) of subsection (6) of section 297."

and Government amendment No. 255.

Mr. Lamont: There are two sorts of company for which we thought it right to have a limit of £5 million instead of £500,000: one is companies letting residential property; the other is companies engaged in ship chartering. Clearly, a limit of £500,000 would have been of little or no use to companies chartering ocean-going ships. Because of the current market conditions, they may still find it difficult to raise the larger amounts of equity finance. The hon. Member for Newcastle upon Tyne, East (Mr. Brown) knows about that. It was in response to representations from the Labour party and from industry that we conceded this point originally.

However, the General Council of British Shipping has suggested that the £5 million limit should also apply to companies which operate their own ships. So far, the only substantial use that has been made of BES for shipping is by a ship chartering company, so we decided to extend the higher limit to ship chartering companies only. But, in principle, there is not reason why the £5 million limit should not also apply to companies operating their own ships. Therefore, we propose to make that change. By pure coincidence, amendment No. 16, tabled by my hon. Friend the Member for Croydon, South (Sir William Clark), seeks to do the same.

Mr. Chris Smith: I shall not advise my hon. Friends to oppose this group of amendments. But we wish that the Government had taken a more sympathetic interest in Britain's Merchant Navy on a regular basis than just once in this amendment.

Amendment agreed to.

Amendments made: No. 253, in page 51, line 8, at end insert "operating or".

No. 254, in page 51, line 10, leave out from "craft" to "those" in line 16 and insert

"and—

(a) every ship operated or let by the company carrying on the trade is beneficially owned by the company;

(b) every ship beneficially owned by the company is registered in the United Kingdom;

(c) throughout the relevant period the company is solely responsible for arranging the marketing of the services of its ships; and

(d) the conditions mentioned in section 297(7) are satisfied in relation to every letting by the company.

(7A) Where—

[Mr. Chris Smith.]

(a) any of the requirements mentioned in paragraphs (a) to (c) of subsection (7) above are not satisfied in relation to any ships; or

(b) any of the conditions referred to in paragraph (d) of that subsection are not satisfied in relation to any lettings,

the trade shall not thereby be precluded from being a trade to which that subsection applies if the operation or letting of those ships, or, as the case may be,".

No. 255, in page 51, line 31, at end insert

" 'let' means let on charter and 'letting' shall be construed accordingly;".

No. 257, in page 51, line 38, leave out

"the provisions set out in subsection (1)"

and insert—

"(a) in paragraph 2(7), for the words 'paragraphs 5' there had been substituted the words 'paragraphs 3A, 5'; and

"(b) the provisions set out in subsection (1)(b)".—[*Mr. Norman Lamont.*]

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

Mr. Andrew Mitchell (Gedling): I do not intend to detain the Committee for a great length of time, but I want to probe the Minister about how he has arrived at this limit of £500,000 and to press him on a number of points to see whether there is any ground for change in the future.

I stand four square behind the Minister's points on abuse and I have considerable sympathy with some of the matters raised by the hon. Member for Islington, South and Finsbury (Mr. Smith). However, I am worried that £500,000 may be too low for the sectors that the Government want to help and that were behind amendment No. 237 proposed by the Opposition concerning manufacturing and distribution.

I recognise that the Minister has received representations, including the report by Peat, Marwick, Mitchell on the £1 million limit. Although the BES schemes are comparatively young, trade studies are already coming through on the results of BES schemes and other venture capital amounts which were invested in Consett. They show the low cost to public funds per job employed there.

I should declare an interest, because I worked for many years for Lazard Brothers and I am still retained by them. I want to refer specifically to the experience of a Lazard Brothers subsidiary, for which I never worked, called the Development Capital Group. It is a widely respected group within the venture capital industry and is run by experienced ex-industrial managers. It is the largest BES manager of funds and is among the three largest venture capital managers. It is also interesting to note that the disposition of these funds is at variance to the normal, which is approximately two thirds in the south east and the London area and one third in the regions. The investments of these firms are the other way round—two thirds in the regions and one third in the south east and the London area.

An analysis of the 68 companies in which the fu[redacted]—approximately £36 million—have been invested shows that 61 per cent were in the manufacturing and distribution sectors and nearly three quarters were in individual amounts in excess of £500,000, all solely or in partnership with other BES funds, which collectively employ more than 1,100 people. I am worried that the imposition of a £500,000 limit would have prevented such investments. From my analysis of the disposition, it is clear that, if the limit had been set at £750,000, about 64 per cent would have been able to proceed.

I wish to make one specific observation. The BES schemes offer very attractive tax treatment. They are now becoming more mature. There is effectively 40 per cent tax relief on the way into the schemes and 40 per cent tax relief through capital gains tax exemption on the way out.

For the next year, will my right honourable Friend the Minister consider beginning to remove the capital gains tax exemption when an investment is sold and simultaneously increasing the £500,000 limit? That might be the appropriate balance. I welcome his comments on the specific examples that I have given.

Mr. Lamont: I am grateful to my hon. Friend for raising that subject, which has been mentioned by various hon. Members. Clearly, we can debate whether the appropriate level is £500,000 or £750,000, but there is no science involved, as proved by our previous debates. We wished to escape the predominance of the asset-backed investment and move towards the types of investments advocated by the hon. Member for Islington, South and Finsbury (Mr. Smith). The evidence is that that happens with smaller investments. Although the funds make investments in individual companies in excess of £500,000, that is above average. The latest figures—admittedly for 1986–87—show that companies raising finance exclusively through funds have been at an average of £330,000.

I referred in our previous debate to the development of the venture capital industry. Its average investment in 1987 was about £560,000. That shows that companies that have attractive projects above the £500,000 limit have an opportunity that they did not have before to raise money.

As my hon. Friend the Member for Gedling (Mr. Mitchell) said, the limit may have an adverse effect on the prospectus issues. I hope that he will not take it amiss if I observe that there may be grounds for cutting the costs of prospectus issues. We do not need to take them for granted. My hon. Friend has raised a legitimate concern. Based on our knowledge of funds and of what the venture capital industry is capable of doing, I have explained why the figure of £500,000 was the right one. It was urged on us by a number of bodies. I assure him that we shall keep the figure under review. We want the funds to prosper as they play an important part in the market. If the effect of the change is too adverse, we shall reconsider.

Question put and agreed to.

Clause 50, as amended, ordered to stand part of the Bill.

Clause 51

APPROVED INVESTMENT FUNDS

Mr. Shaw: I beg to move amendment No. 246, in page 52, line 4, leave out "90" and insert "70".

At this late hour, I do not wish to incur the wrath of my colleagues by speaking for too long. However, I know that they and, indeed, all members of the Committee will appreciate that many of the smaller fund managers and those with experience in the regions have been pressing for such a proposal for some time.

I should make it clear that I have been involved in fund management. I launched two BES funds—one regionally and one nationally. Probably everyone knows that I am a director of one or two BES companies.

The amendment would delete the reference in the clause to 90 per cent and replace it with 70 per cent. Some might wonder about the significance of that. The clause would allow tax relief to be obtained after the end of the financial year—the tax year—in which the fund received its money from investors but might not have fully invested in companies. The investment process is difficult. For those hon. Members who do not have experience of it, I should say that it can take up to six months for a BES investment to be made from the moment that the entrepreneur walks through the door and requests money. It is therefore extremely difficult in such circumstances if tax relief is unavailable and fund managers are working against time.

The amendment is significant because it has long been requested by fund managers—not the larger ones, but the smaller ones and those with experience of regional funds. The amendment is supported by the authors of the Small Business Research Trust report, which was mentioned earlier. As the report shows, the smallest investments have the highest risks; they are the most complicated and difficult and take longer to come to fruition. That point is referred to in the report. In particular, page 5 of the report states:

"The proposal in the March 1988 Budget to allow fund managers an extra six months from 5 April to invest at least 90 per cent of the amount raised may be too short a period to have a significant effect on fund activity. Moreover, the provision only applies to approved investment funds and so does not benefit small local funds which tend, for size and cost reasons, to operate as managed schemes."

My amendment relates to small and regional funds and I hope that the Minister will consider it and its possible benefits. I believe that, if the amendment were accepted, there would be limited, if any, tax loss. Indeed, now that income tax rates have been stable for some time, it is likely that there would be no tax loss.

The problems of small regional funds may be summarised as follows. Often, in the regions, businesses are not incorporated—they are not limited companies; they are often partnerships and unincorporated. Numerous legal problems arise which lengthen the timescale to get the companies in a form in which BES investment can take place.

The professional advice available in the regions is often not as good as it might be in London—not because of lack of competence but simply because of lack of experience of dealing with the BES in those areas. That again means that it takes more time for investments to take place.

In my experience, entrepreneurs in the regions have shown a lack of understanding of equity finance. That is because, for years, equity finance was not available and they had to rely on loan finance. All those factors contribute to the time difficulty of completing investments. In that respect, the amendment would help.

Hon. Members may wonder why a figure of 90 per cent is unacceptable because it is a concession. Unfortunately, the concessions which have been squeezed out of the Inland Revenue for the BES over the years have always taken two years—two bites of the cherry—and I had hoped that after all the years that we had struggled, this concession might come in one big bite. I acknowledge that the concessions have been of help and that many jobs have been created and much investment made under the business expansion scheme. The reason that 90 per cent is unacceptable is that only 10 per cent is left. Anyone with experience of managing a fund will know that only five or six investments are made out of a fund. Any more would not be manageable from the viewpoint of the fund's managers.

11.15 pm

By definition, therefore, each investment must be one-fifth or one-sixth of the total fund. The ability for only 90 per cent of the fund to be invested and 10 per cent carried forward is no real concession. If my figure of 70 per cent were used, and for the smaller, region-based funds, two investments were carried forward outside the six-month period, it would be no great tragedy or loss to the Inland Revenue, but there would be a significant impact on regional and small funds.

My amendment would help the regions and the smaller funds. Since the announcement of the concession in the Budget, I have not been aware of any regional funds that are to start up. I suggest to my right honourable Friend the Minister that this concession needs to go just a little further, with the Revenue allowing a slightly bigger bite of the cherry than hitherto.

Mr. Lamont: The clause is intended to—

[*Interruption.*]

It is important to ensure that there is a concession before my hon. Friend asks for a bigger one, which he has done.

Clause 51 gives an improved fund more time in which to find suitable companies to invest in by giving the investor his tax relief by reference to the date on which the fund closes, provided that at least 90 per cent of the amount invested in the fund is invested in the BES company within six months. This does not mean that the investor gets his tax relief before the fund has

[Mr. Lamont.]

invested its money, which appears to have been the misunderstanding of a number of people. Emphatically, that is not so. The investor will get his relief by reference to when the fund closes, for that year. This means that a fund could close on 5 April, the end of the tax year, and the managers would have until 5 October to invest at least 90 per cent of the money raised.

That change and the changes that we made last year for the carryback of investment by the investor were very much designed to meet the problem of the end-year bunching that applies to many BES funds. There has been a complaint that because taxpayers are not aware of their own position until late in the year, they do not have to decide to invest in BES funds until the end of the year, and there is a tremendous problem for the managers in investing the fund within the tax year. Last year, we introduced the six-month carryback to deal with that. The amendment would contribute to that.

Six months is a long time for fund managers to find suitable investments. My hon. Friend the Member for Dover (Mr. Shaw) said that all the investments that the fund would make were greater than 10 per cent and that it was wrong to leave only 10 per cent, which is not equal to any one investment, and that therefore this headroom was of no use.

However, that is not the way in which we regard the 10 per cent. It is not there for another investment that might be made beyond the six months. It is there because, clearly, the investments of the fund do not necessarily fall neatly into 10 per cent, 15 per cent or 20 per cent categories. It was agreed that there might be a margin of uninvested cash, and 90 per cent does not mean that the fund is not fully invested. Another way of putting it would be to say that we are defining "fully invested" as 90 per cent rather than leaving an opportunity for yet another investment.

I understand the point made by my hon. Friend, who has considerable experience not only of BES but of the operation of funds in the regions, which all members of the Committee wish to encourage. What my hon. Friend said should be treated with respect. But I do not wish to act upon it this year. My hon. Friend wants everything in one bite and not two, but I made the concession on the carry-back last year and on the 90 per cent, and I wish to see how that operates. However, I hear loud and clear what he says.

Mr. Shaw: The Minister has taken on board some of my points. I hope that he will note the two key ones.

For small funds and small company investment, it is sometimes necessary, from the moment a fund is raised and closed, for 18 months to be available for that fund to fully invest. It helps if the tax relief can be backdated to the tax year in which the fund was raised. Therefore, my amendment may not provide the sole answer, because the whole of the following tax year should be available as an investment period for smaller funds as well as the year in which the fund is raised.

Although I am willing to withdraw the amendment and acknowledge that there may be two bites at the cherry and that I shall have the opportunity to press the point next year, I hope that the Minister ensures that he receives regular reports in the Treasury on the number of small regional funds started this year. If none are started, or very few, by the time next year's Finance Bill is in preparation, I hope that he insists that his civil servants draft a clause along the lines of my amendment.

I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 51 ordered to stand part of the Bill.

Further consideration adjourned.—[*Mr. Lennox-Boyd.*]

Adjourned accordingly at twenty-three minutes past Eleven o'clock till Thursday 16 June at half-past Four o'clock.

THE FOLLOWING MEMBERS ATTENDED THE COMMITTEE:

Hunt, Mr. John *(Chairman)*
Arbuthnot, Mr.
Armstrong, Ms
Battle, Mr.
Boswell, Mr.
Bright, Mr.
Brooke, Mr.
Brown, Mr. Gordon
Brown, Mr. Nicholas
Butterfill, Mr.
Campbell-Savours, Mr.
Carrington, Mr.
Coombs, Mr. Anthony
Darling, Mr.
Davies, Mr. Quentin
Favell, Mr.
Forman, Mr.
Griffiths, Mr. Nigel
Henderson, Mr.
Howarth, Mr. Gerald
Hunter, Mr.
Ingram, Mr.
Jack, Mr.
Lamont, Mr. Norman
Lennox-Boyd, Mr.
Maples, Mr.
Marek, Dr.
Mitchell, Mr. Andrew
Morgan, Mr.
Nicholson, Mr. David
Shaw, Mr. David
Smith, Mr. Andrew
Smith, Mr. Chris
Stern, Mr.
Taylor, Mr. Ian
Wallace, Mr.
Wardle, Mr. Charles
Watts, Mr.
Widdecombe, Miss
Worthington, Mr.

PLOP

Inland Revenue

Policy Division
Somerset House

FROM: MRS E FLETCHER
DATE: 14 JUNE 1988

MRS R CHADWICK
APS/PAYMASTER GENERAL

FINANCE BILL: CLAUSE 67 - PAYROLL DEDUCTION SCHEME FOR CHARITIES

1. I attach a revised Speaking Note to replace the one previously supplied as part of the Note on Clause 67. There is a small change in paragraph 12 (which previously gave the impression that Minister had announced the introduction of joining the scheme by telephone, whereas the Inland Revenue gave notice of this change) and the number of schemes have been up-dated to mid-June figures.

2. There has been very little reaction to Clause 67. Apart from the factual reports in the Press shortly after the Budget CAF and the Chartered Association of Certified Accountants welcomed the doubling of the limit to £240. Charities VAT and Tax Reform Group said it provided little real help since the scheme had proved to be a flop.

MRS E FLETCHER

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cc PS/Chancellor
PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Mr Corlett
Mr Stewart
Mrs Fletcher
PS/IR

BOARD OF INLAND REVENUE

PART II SPEAKING NOTES (NOT FOR CIRCULATION)

GENERAL NOTE

Introduction

4. The payroll giving scheme has been running for just over a year now. The scheme enables employees to make donations to charity direct from their wages or salary, and get tax relief on their gifts. This clause doubles, to £240 a year, the amount which an employee can give from the start of the current income tax year, 6 April 1988.

5. The scheme has been widely welcomed, particularly by charities, who recognise its potential to increase their funds.

6. Over 2700 schemes have already been set up by employers, and I hope other employers will follow suit. We have already made it available to some 435,000 civil servants and arrangements are being made for a further 161,000 to join in.

7. Clearly it would be unrealistic to expect the scheme to reach its full potential immediately. It must take time to build up, as more and more people come to realise that it offers a very simple way of giving regularly and painlessly from their earnings to charities of their choice - and obtaining full tax relief.

8. I hope charities will encourage their supporters to make full use of the scheme.

Reason for increase

9. Although the average donation made per employee last year was well within the existing limit, some charities made representations to us that the limit was too low and should be much higher. They explained that there was a significant number of people who were giving the maximum amount allowed, and wished to give even more. We have been pleased to be able to meet these requests. Doubling the limit to £240 will mean that charities will gain. And it demonstrates, again, the Government's commitment to the voluntary sector and to the payroll giving scheme in particular.

BOARD OF INLAND REVENUE

DEFENSIVE NOTES

Limit should be higher

10. There has to be some limit on the amount the Exchequer contributes by way of tax relief. £240 is a generous donation for most employees. The limit has been increased twice since the scheme was first announced and we shall continue to keep it under review.

Slow take up of scheme?

11. It is true that the scheme has got off to a somewhat slower start than we should have liked. There is no shortage of employers willing to make the arrangements available to their employees. Some 2,700 schemes were in existence by mid-June, but the take up among employees so far is a little disappointing.

12. But I am confident that the scheme is going to be a success, as it becomes better known. That is why we have shown our confidence in it. It is the first time individuals have been able to make donations to charity, and get tax relief, without having to do anything more

formal than sign a form authorising their employer to make the deductions from their pay and pay them over to an agency for the charity or charities of their choice. Employees can join their employer's scheme simply by making a telephone call to a payroll agency. This should encourage more people to contribute, especially where there is a nationwide appeal. And to make it easier for employees they can now, if they wish, choose a consortium, made up of different charities, to receive all or part of their gift. It could hardly be simpler.

Better publicity?

13. As with all forms of fund-raising the public need to be made fully aware of the fact that they can give to charity in this way, and how they can give. Most charities are well organised when it comes to asking for donations to be made by deed of covenant. I hope they will be able to give the payroll giving scheme the same publicity. The increase in the limit which we are proposing enables each employee to give £20 a month or £4 a week. If the scheme is taken up widely, charities stand to benefit considerably.

Government should publicise scheme

14. The Government has provided the opportunity to tap a potentially enormous source of new funds. It is now primarily up to charities to exploit this to the full by publicising the scheme and encouraging their supporters to join in.

Reduction in basic rate reduces tax repayments to charities

15. Slightly reduced repayments are the inevitable result of a reduction in the basic rate. But reductions in income tax rates since 1979 leave people more to give to charities if they wish. Tax repayments to charities have increased steadily over the years. The total amount repaid in the year to 30 September 1987 was about £350 million, about £150 million of which was in respect of deeds of covenant.

No general VAT relief for charities?

16. VAT matters are not relevant to this clause. However, there is a wide measure of VAT

relief for specialised goods and services used by charities in caring for the disabled and many of their purely voluntary activities are outside the scope of the tax. It is estimated that their average VAT burden is about 1-2 per cent of total expenditure. A general relief from VAT would, however be expensive in revenue terms, difficult to administer and benefit most those charities spending most irrespective of the purpose and nature of their expenditure. It would also be in breach of our obligations under the EC Six Directive on VAT.

/BACKGROUND NOTES

53/2/LPD/3751/004

cc PS/CHANCELLOR
PS/CST PS/FST PS/PMG
MR CULPIN MR GILHOOLY
MR MICHIE
MR TREVETT C&E
PS/C&E
PS/IR.

Treasury Chambers, Parliament Street, SW1P 3AG

Sir Peregine Rhodes, KCMG
British Property Federation
35 Catherine Place
LONDON
SW1E 6DY

14 June 1988

Dear Sir Peregrine

CLAUSE 16 FINANCE (NO 2) BILL

Thank you for your letter of 3 June about this clause.

This new penalty provision replaces the previous complicated automatic third test for the serious misdeclaration penalty. It will not be automatically applied whenever the de minimis thresholds of £100 or 1%, whichever is the greater, are exceeded. The tests are minimum figures only and when exceeded Customs will first consider whether the nature of the errors justifies the issue of a warning letter, or the imposition of a penalty. In no circumstances will a penalty be imposed without the case first being referred to Customs' Head Office. In short the penalty will be imposed only the most careless, bordering on reckless traders, who persist in making significant errors even after a formal warning.

You have expressed concern about the retrospective nature of the penalty. No error in a prescribed accounting period prior to Royal Assent either can or will be penalised. At the very least there will normally have to be errors in two prescribed accounting periods after Royal Assent before a penalty may be imposed. However, errors occurring before Royal Assent may be taken into account for the issue of a warning letter. This is because of the length of time between the majority of control visits and the objective of improving the accuracy of returns by the very few who already persistently disregard their VAT obligations.

You have said that experience of "reasonable excuse" provides very limited protection. I cannot agree that this is true and suggest

you are being misled by the few cases that reach the VAT Tribunal. In fact, Customs have accepted reasonable excuse in some 21,000 cases, and either not imposed a penalty (including default surcharge) or withdrawn the penalty assessment. The operation of reasonable excuse has therefore worked well and coupled with the provision for voluntary disclosure should ensure that only the most negligent are penalised under this new provision.

Finally I can assure you that the operation of this penalty will be closely monitored and kept under close review together with the serious misdeclaration penalty.

Yours sincerely

Peter Lilley

PETER LILLEY

53/2/LPD/3751/003

cc PS/CHANCELLOR
PS/CST PS/FST PS/PMG
MR CULPIN MR GILHOOLY
MR MICHIE
MR TREVETT CTE
PS/CTE PS/IR.

Treasury Chambers, Parliament Street, SW1P 3AG

J W Hardy Esq
President
The Institute of Taxation
19 Cobham Road
Leatherhead
SURREY
KT22 9AU

14 June 1988

Dear Mr Hardy,

CLAUSE 16 FINANCE (NO 2) BILL

Thank you for your letter of 2 June in which you expressed concern about this clause.

This new penalty provision replaces the previous complicated automatic third test for the serious misdeclaration penalty. It will not be automatically applied whenever the de minimis thresholds of £100 or 1%, whichever is the greater, are exceeded. These tests are minimum figures only and when exceeded Customs will first consider whether the nature of the errors justifies the issue of a warning letter, or the imposition of a penalty. In no circumstances will a penalty be imposed without the case first being referred to Customs' Head Office. It will only be imposed on the most careless, bordering on reckless traders, who persist in making significant errors even after a formal warning.

I can assure you that the operation of this penalty will be closely monitored and kept under close review together with the serious misdeclaration penalty.

Yours ever

Peter Lilley

PETER LILLEY

INLAND REVENUE
CENTRAL DIVISION
SOMERSET HOUSE

FROM: D DENTON
DATE: 14 June 1988

PS/FINANCIAL SECRETARY

GOVERNMENT COMMITMENTS FOR REPORT

Appended, as requested, is a list of the items for which Ministerial approval has already been given (prior to today) to bring forward amendments/new clauses at Report.

D. Denton

D DENTON

cc. Principal Private Secy
PS/CST
PS/Paymaster General
PS/Economic Secretary
Mr Culpin
Mr Gilhooly
Ms C Evans
Mr Cropper
Mr Jenkins (OPC)
Mr Isaac)
Mr Painter) for info
Mr Beighton)
Policy Directors
Mr Calder
Mr Cleave
Mr Hall (Sols)
Asst Secretaries on F Bill
Mr McManus
Mr Fraser
Mr Denton
Mrs Hupman
PS/IR

Appendix

FINANCE BILL GOVERNMENT AMENDMENTS ETC - MINISTERIAL COMMITMENTS FOR REPORT

(a) Amendments

Clause 35 - Annual payments	: Extend provision to apply to payments by Scottish partnerships.
Clauses 49 and 50 and Schedule 4 - BES	: Extension of relief for letting of private residential property to Northern Ireland.
	: Extending £5m limit for ship-chartering companies to companies which operate their own ships.
	: Preventing tenants being given an option to buy the property.

(b) New Clauses

1. CGT : To enable election, for all pre-1982 assets, for gains to be computed by reference to 1982 values.

2. CGT : To give some benefit from rebasing in cases where asset acquired between 1982 and 1988 and tax payment was deferred on that occasion (holdover, rollover etc).

Inland Revenue

Policy Division
Somerset House

FROM: A C JARVIS
14 June 1988

PAYMASTER GENERAL

BENEFITS-IN-KIND: THIRD PARTY ENTERTAINMENT

CLAUSES 46-48 FINANCE BILL

1. You may have already seen the attached articles in today's and yesterday's Times about the hospitality provided for firms entertaining clients during Wimbledon fortnight. The Opposition may refer to this during this evenings Committee stage proceedings on Clauses 46-48 of the Finance Bill.

2. One point mentioned in yesterday's article which may be seized on is that hospitality firms charge businesses up to £850 per head for food, drink and a men's final ticket. This may be an extreme example but it is just the sort of benefit which could be exempted from income tax by the Finance Bill proposals. No matter what the level of hospitality the argument still holds true that the recipient is unlikely to know the actual value of the benefit he receives from being entertained whether at Wimbledon or at a Rugby Union International at Twickenham. Similarly the host (or the hospitality firm) could not apportion costs fairly between the guests. Although the hospitality firm might charge £850 per guest at Wimbledon (or the £285 quoted for Twickenham) this is just an average cost. Not all guests will fully partake of everything on offer. Some may only be there to watch the tennis, others will take more than their fair share of hospitality.

---

cc PS/Chancellor
PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Mr Cropper
Mr Tyrie
Miss Sinclair

Mr Isaac
Mr Lewis
Miss Rhodes
Mr Elliot
Mr I Stewart
Mr A Parker
Miss McFarlane
Mr Jarvis
PS/IR

3. Today's article quotes an estimated £500 million as the annual turnover of companies providing this sort of hospitality. We cannot substantiate this figure. Our previous speculative estimate was £100m giving a revenue yield if liability could be enforced of up to £40m. But in practice it has not been possible to collect much tax under the present provisions. The cost in terms of yield is therefore negligible.

4. The point to make here, however, is that the cost of providing entertainment is not allowed as a deduction to the provider in calculating his taxable business profits. This disallowance of the costs of entertainment will extend to overseas customers if the House approves Clause 68. Moreover Schedule E tax will not be due on the full turnover figure. Many of those being entertained would not anyway be liable to Schedule E. For instance, foreigners not resident here, or the self-employed.

5. The reasons for the Government's proposals are set out at paragraphs 12-14 of the Notes on Clauses 46-48, and these apply equally well to hospitality provided by third parties at Wimbledon.

A C JARVIS

Wimbledon final ticket prices soar to £900

Hospitality firms fuel black market

By Howard Foster and John Goodbody

TIMES. 13/6/88.

The claim by a leading hospitality company that up to 150 umpires are involved in providing "under the counter" Wimbledon tickets at inflated prices has highlighted the phenomenal growth in black market ticket prices for the event.

This year has seen one of the biggest price increases ever. Tickets for the men's singles final costing £25 have already changed hands for up to £900. Advertisements in *The Times* seeking tickets have doubled since last year. Some touts offer holidays in exchange for good seats.

Some touts selling tickets in the streets around the courts will make £20,000 during the Wimbledon fortnight, which begins next Monday. They are not acting illegally. The only offence of which they might be guilty is obstruction.

The Times has examined the entire ticket system and uncovered allegations that umpires are selling their Centre Court tickets against their association's rules. *The Times* has also been offered Centre Court tickets from an allocation given to the Lawn Tennis Association, another clear breach of official rules.

This year is the hardest ever for those wanting to obtain a Wimbledon ticket on the black market, for a number of reasons.

A rapidly expanding section of the market has contributed to an escalation in prices so great that signs are emerging that the black market ceiling may soon be reached. That market is the unofficial corporate hospitality industry, which has been trying without success to gain the official recognition of the All England Lawn Tennis and Croquet Club for the past 10 years.

The 1988, Wimbledon fortnight will see up to 15 of these companies taking over sports halls, car parks and council parks close to the courts with their "villages" of marquees. They charge business people up to £850 a head for food, unlimited drink and a ticket for the men's final.

These companies are under signed agreement to obtain prime position seats for their clients, who are often entertaining valuable contacts.

As the number of hospitality companies grows, so does the number of touts, and once the companies have taken their allocation, there are fewer black market tickets for the public.

"We don't like the hospitality companies because they are out to corner the market and will fix the ticket prices themselves", one tout said. "At the moment, we are their main source of supply. They don't like us but they can't do without us."

Mr Chas Wheeler, of Business Entertainment Services, part of Britain's second biggest hospitality group, blames the system of ticket allocation for the high prices. "We have to pay for our tickets from the ticket agencies like anybody else and that means paying silly prices.

"We have tried asking the All England Club for an allocation from the public ballot, in return for which we would pay a sum for the benefit of tennis, but they want to keep things the way they are.

"Now, for the first time, I have seen signs that the prices are becoming too high. We have had people this year telling us they will not come to Wimbledon because, for the money, they could afford to take clients to two other major sporting events. This is killing the goose that lays the golden egg for the touts."

The allocation system involves the distribution by the club of Number 1 and Centre Court tickets to many organizations and individuals, including the Lawn Tennis Association, the umpires, players and the debenture holders. The latter pay £6,250 for a ticket on each day of the championships over a five-year period.

The All England Club also provides tickets to 44 leading British companies with tents in the grounds. The Keith Prowse organization is the only hospitality company authorized to receive a ticket allocation at face value, having handled tickets for the club since 1924.

One of the two big areas where the black market operated until 1982 was in supplying the demand from foreign visitors. Since then, the All England Club has used its long-standing relationship with Keith Prowse to provide the company with tickets as part of a package offered to foreigners. That eliminated the black market demand in that particular area, but it also reduced the number of tickets available to touts, raising prices.

Another reason for the rise in black market ticket prices was the careful checking of applications to go into the public ballot for tickets. Members of the public now have to request application forms, where before they could simply collect handfuls from the club. These are checked by club officials, who weed out multiple applications by checking for similar handwriting. The odds against getting a pair of tickets for some days are estimated at 20-1.

In 1985, good forgeries appeared for the first time and many people had to check whether they had originals or counterfeits. As a result, many tickets were traced to their source, an embarrassment to officials who had sold their tickets against the rules. This plugged another traditional source of black market seats and pushed prices up again.

In 1986 the new ticket manager at the club, Mr Peter Lovewell, ended the granting of tickets to some traditional sources, further restricting supplies.

Finally, all tickets are now issued in May instead of February and March, leaving the black market to scramble for them in the three weeks before Wimbledon begins.

Tomorrow: The siege of Wimbledon.

TIMES 13 JUNE 1988

TIMES

14 JUNE 1988

£500m backyard hospitality industry: 2

Big business is set to boom on Wimbledon's fringes

By Howard Foster and John Goodbody

The fortress-like All England Lawn Tennis and Croquet Club, with its concrete and barbed-wire perimeter walls, is under siege by an "army", complete with tents and provisions, ready to breach the defences of one of the most exclusive events in the social calendar.

From the opening of Wimbledon Fortnight next Monday, up to 15 unofficial companies involved in the wining and dining of thousands of business clients will be setting up camp in car parks, sports fields and even possibly back gardens, all unable to operate within the All England Club itself.

This growing industry has an estimated annual turnover of £500 million from big British sporting events, and has helped to push up Wimbledon ticket prices by removing several thousand from the black market-place.

The number of these firms appearing at the 1988 Wimbledon tournament is larger than ever, and the pressure to supply tickets to important clients months in advance can cause considerable problems. Guests at one unofficial hospitality company threw themselves on the mercy of the All-England Club last year after tickets failed to materialize.

Mr Chris Gorringe, chief executive of the All-England Club, said: "We get tired of people coming to us after being let down by the unofficial corporate hospitality firms. They operate totally outside our organization.

"The sad thing is that none of the money these people are taking goes back into the game of tennis. After costs, our takings go back into the game."

> None of the money these people are taking goes back into the game of tennis

One of Britain's bigger advertising agencies confesses to misgivings about using the services of one unofficial hospitality company that put its guests in a marquee in the back garden of a residential area last year. Neighbours made plain their objections.

A senior executive for the agency said: "We had a million pounds' worth of clients and there we were feeling that at any moment the neighbours might start causing a fuss. It is not something we would take a chance on again."

The most publicized corporate hospitality débâcle recently involved a company called Maceworth. It failed to provide tickets for almost 400 clients who paid £285 each to watch the England v Wales Rugby Union international at Twickenham, with refreshments.

Maceworth, which has run a hospitality event at Wimbledon before, told *The Times* that "other commitments" prevented the company from providing a service this year.

One company, which has used its own detached house close to the All-England Club, is expected to entertain 1,200 clients at a local sports ground provided by Merton Borough Council this year.

Mr Marcus Evans, managing director of Associated Promotions, angered neighbours by allowing his clients to use the gardens of his house in Somerset Road. The council supported the neighbours' objections but, to defuse the situation in 1988, it offered land in Wimbledon Park as an interim measure.

The only hospitality company to benefit from allocations of tickets sold at face value direct from the All-England Club is Keith Prowse, which caters for a large number of foreign visitors. However, it is not allowed within the gates of the club, pitching its tents in parkland across the road.

It is the aim of the larger unauthorized hospitality firms to displace Keith Prowse or, at the very least, to persuade the club to part with some of its face-value tickets to bring down the price of hospitality for the client.

Mr Charles Wheeler, of Business Entertainment Services, said: "We wrote to the club and asked if we could have a specified number of public ballot tickets on the basis that we would pay money into a fund to be used for British tennis.

"The club said that it had to be seen to be letting the public have tickets. We need hundreds of tickets and we have to pay the inflated prices just like anyone else. If the Americans come over, they will pay anything. The more of us there are, the more we have to pay."

Seedings, page 42

D. John Ogren
Chairman and Managing Director

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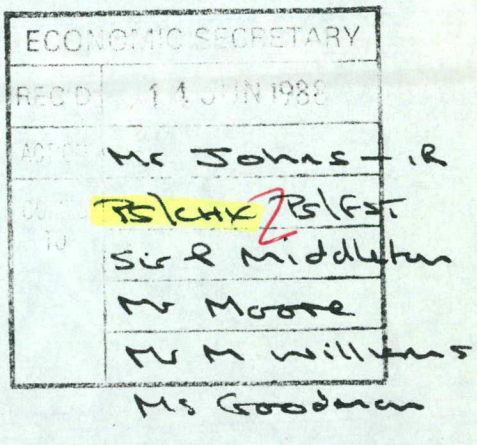
14 June, 1988



Mr. Peter Lilley, MP
Economic Secretary
The Treasury
Parliament Street
London, SW1P 3AG

Dear Minister,

It is our understanding that you plan to amend Clause 129 of the Finance Bill to increase the proposed Southern Basin oil allowance to 125,000 tonnes per chargeable period.

We thank you for improving the terms and appreciate that any amendment at this stage in the legislative process represents a significant action by Government. However, based on reports that this is the only change that you plan, we must with respect tell you that it is an inadequate modification.

From a Conoco point of view, our six fields committed since 31 March 1982 continue to be severely impaired:-

	£ Millions	
	NPV (10% Real)	Net Cash Flow
Versus Pre-Budget at;		
100,000 tonnes	-44	-196
125,000 tonnes	-26	-133

In addition to Conoco, the overall impact on industry continues to be strongly negative. I refer to the UKOOA letter dated 13 May 1988, with its graphical attachment. Future developments, in aggregate, remain negative and committed fields are still impaired by more than £100 million. This is in spite of the fact that, based on the 23 May meeting between UKOOA, Department of Energy and Treasury, there appeared to be little disagreement on the committed fields.

Continued/..

DIRECTORS: G.D. Achenbach, C.L. Bare, G.W. Edwards, F.E. Ellis, I R Kemp, D.J. Ogren, S.M. Stalnecker (All USA), W.S. Atkinson, P.B. Buckroyd, I. Gray, T. Moore, D. McGeachie, J.C. Symon, J.R. Wallace, G.E. Watkins, D. Watts

Registered in England No. 524868

Overall, these circumstances can only imply a conscious decision to increase tax take during this period of continuing low oil prices. This creates the altogether unacceptable position that investor confidence is seriously shaken while new developments are discouraged and the history of constructive government and industry dialogue is undermined.

We urge you to reconsider your position on Clause 129. From our perspective, to be acceptable the 125,000 tonne allowance must be accompanied by a moving forward of the effective date to 31 March 1988. We would appreciate an opportunity to discuss this alteration with you or your office.

This letter is being copied to the Minister of State for Energy.

Yours sincerely,

D. John Ogren

DJO/gmp

14 JUN 1988

UK OFFSHORE OPERATORS ASSOCIATION LIMITED

3 Hans Crescent, London SW1X 0LN
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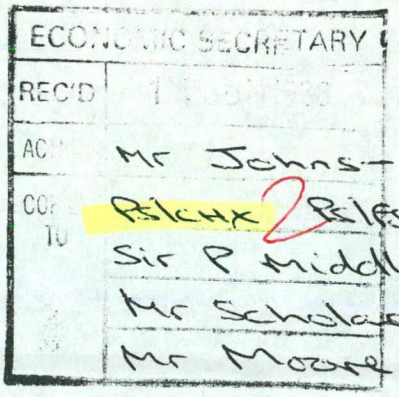

Miss Sinclair
Mr M Williams
Ms Goodman
Miss Hill
PS/IR.

Peter B. Lilley, Esq., MP
Economic Secretary
HM Treasury
Parliament Street
London SW1P 3AF

14 June 1988

Dear Economic Secretary,

We appreciated the opportunity of being able to meet you yesterday, but I have to advise that we are most disappointed with the Government amendment to the Finance Bill which has been tabled today.

You will know from our representations that we and our Members went to considerable depth to inform you of the adverse impact of the Budget proposal on our financial position and on industry confidence, specifically with regard to the post 1982 existing developments. Our recommendation to restore the oil allowance to 160,000 tonnes per chargeable period represented the minimum level consistent with your objective of fiscal neutrality. Even at this level a number of our Members would suffer. We are particularly disappointed because we believe that a positive stimulus would have been in the interests of both industry and Government.

The unprecedented effort our Members have put into supporting our case is a measure of their strength of feeling on this matter; it is therefore very disappointing that so little cognizance seems to have been taken of our views. Nevertheless, we have been grateful for your willingness to hear them.

We urge that you give Clause 129 further consideration. We are copying this letter to the Minister of State for Energy, The Rt. Hon. Peter Morrison.

Yours sincerely,

Keith Taylor

K.H. Taylor
President

cc The Rt. Hon. Peter Morrison MP

Inland Revenue

Policy Division
Somerset House

FROM: P A MICHAEL
DATE: 14 June 1988

1. MR PITTS 14/6.

2. FINANCIAL SECRETARY

FINANCE BILL: CGT REBASING

1. This note seeks Ministers' agreement to bring forward a technical amendment at Report Stage to remedy an oversight in the drafting of the CGT rebasing provisions. I am sorry that we did not spot this originally.

Background

2. Under the provisions of the Bill, rebasing will be available where a person disposes of an asset on or after 6 April 1988 which they held on 31 March 1982. Rebasing will also apply where the person making the disposal did not own the asset on that date but who acquired it on a specified no gain/no loss transfer from someone who did. The most common types of no gain/no loss transfer are between husband and wife and among companies within the same group, but there

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cc. PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Culpin
Miss Sinclair
Mr Cropper
Mr Jenkins (OPC)
Mr Isaac
Mr Pitts
Mr Cayley
Mr Hamilton
Mr Michael
PS/IR

are various other existing provisions which provide for similar treatment. These provisions are listed in two places in the Bill and operate for both rebasing and (in the case of disposals under the post-Budget regime) computation of indexation on the March 1982 value.

The Problem

3. It has just been brought to our attention by the Co-operative Union Ltd that the list of no gain/no loss transfers for these purposes is not quite complete. Specifically, it does not include a rather obscure provision which provides a no gain/no loss rule on mergers involving Industrial and Provident Societies. In looking at this we have discovered three other obscure no gain/no loss provisions (dealing with disposals by the Housing Corporation and housing associations) which are also omitted. Prior to instructing Parliamentary Counsel before the Budget we undertook a search of the Statutes for no gain/no loss provisions, using the standard private sector computer program for this sort of thing, but the computer failed to pick these provisions up.

Conclusion

4. It is reasonable to assume that unless the Bill is amended, those taxpayers concerned will be adversely affected. To put the matter right would mean amending the Bill in two places: the amendments would total about ten lines and be purely technical. Because time is short, we have today instructed Parliamentary Counsel on a contingency basis and we would be grateful for Ministers' approval to make the changes on Report (when we shall have other Government amendments on capital gains aspects). Once again, I am sorry to trouble you with this.

PAM

P A MICHAEL

British Property Federation

35 Catherine Place, London SW1E 6DY
Telephone: 01-828 0111
Facsimile: 01-834 3442

15 JUN 1988

From the Director General
Sir Peregrine Rhodes, K.C.M.G.

14 June 1988

FINANCIAL SECRETARY
REC. 15 JUN 1988
ACTION MR. CAYLEY IC.
COPIES TO PPS, MR CULPIN
MR. CROPPER
MR. TYLER
PS IC.

ECONOMIC SECRETARY
REC'D 15/6
ACT FST

Peter Lilley Esq MP
Economic Secretary
Treasury
Parliament Street
London SW1P 3AG

FINANCE (NO 2) BILL: CLAUSE 91

The Federation was encouraged by the Chancellor's announcement in his Budget speech that he intended to rebase the calculation of capital gains tax to 31 March 1982. The implication was that the opportunity was being taken to eliminate the need to use 6 April 1965 valuations so simplifying a complicated and time consuming set of rules enacted 23 years ago. However, when we received the Inland Revenue's press release it became apparent that the computations would be more complicated than before. This is because a new set of rules is to be grafted on to old rules which remain in force.

In detail we are disappointed that, given the aim of simplication, the changes will not eliminate the following:-

1. The process of comparison between a gain or loss computed by reference to one set of rules with that computed by reference to another. The present proposals introduce a third set of rules by which a comparison with the others must be made.

2. The need for valuations to be agreed with the Inland Revenue as at 6 April 1965. Given the time that has elapsed since that date it is not surprising that our members are finding increasingly that such agreements are difficult to achieve. Even those astute enough to have commissioned professional valuations in 1965, which would previously have been generally accepted, are now finding that they are rejected by District Valuers who frequently view the valuations in the

light of developments since. Often the Valuers were not practising in 1965 and have no first-hand knowledge of the conditions prevalent at that time. Where there are no 1965 valuations, the information available is frequently scanty. This makes a 1965 valuation today highly subjective.

3. The need to make reference to complicated provisions when making calculations, e.g. paragraph 11 of Schedule 5 of the CGT Act 1979.

The new proposals both preserve the old rules, and add to them to bring about the following restrictions:-

(a) neither a gain nor a loss should be augmented;

(b) a loss should not be turned into a gain, nor a gain into a loss;

(c) neither a gain nor a loss should be created where none existed.

We feel strongly that while restrictions are desirable, it is unsatisfactory to link these to, and so perpetuate a set of rules whose use is becoming increasingly difficult. We suggest that the restrictions should, instead, be expressed in terms of the real gain or loss made by the owner of an asset, irrespective of how long he has owned it. Most owners will be aware of the extent of any real gain or loss more readily than of that computed under the tax legislation.

We understand that you will be proposing a new clause at Report Stage which will introduce a blanket election allowing all pre-1982 assets to be treated as if they were acquired on 31 March 1982. We understand that the election is intended to cover all chargeable assets owned by the electing party (together with its subsidiaries, in the case of a group of companies). We do not think that this would result in the simplification which is your aim, or eliminate the need to make assessments of valuation as at 1965. The inclusion of large numbers of properties, in many cases owned for long periods, and other assets such as shares in subsidiaries, will mean that the potential tax consequences of election might be considerably higher than the saving in administration.

We therefore strongly urge that, as an alternative, the provisions in the Bill should be amended to the effect that any chargeable gain is limited to the real gain and that any allowable loss should be limited to the real loss.

... The Annex to this letter sets out a possible form of amendment to Clause 91 which we invite you to consider. In our view the principles resulting from the proposals in the Finance Bill would be neutral in tax terms. Neither the Revenue nor the taxpayer would be prejudiced. The same applies to our suggested alternative under which both the Revenue and taxpayers would benefit from the elimination of the need to look further back than 31 March 1982, except to the original cost.

PEREGRINE RHODES

ANNEX

CLAUSE 91 AMEND TO READ

"(3) sub-section (2) above shall apply with the proviso that:-

(a) a gain computed under that sub-section shall not exceed the gain, if any, computed by reference only to original cost and

(b) a loss computed under that sub-section shall not exceed the loss, if any, computed by reference only to original cost.

(4) Where in the case of disposal of an asset the effect of sub-section (2) above would be to substitute a loss for a gain (computed by reference only to original cost) or to substitute a gain for a loss (computed by reference only to original cost), it shall be assumed in relation to the disposal that the asset was acquired by the person making the disposal for consideration such that, on the disposal, neither a gain nor a loss accrues to him.

(5) In this section, references to "original cost" mean the original cost of acquisition together with any enhancement expenditure allowable under S.32 (1) (b) of the Capital Gains Tax Act 1979."

Britoil

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Fax 041-225 5050
Telex 777633

Dial Direct to 041-225 .....

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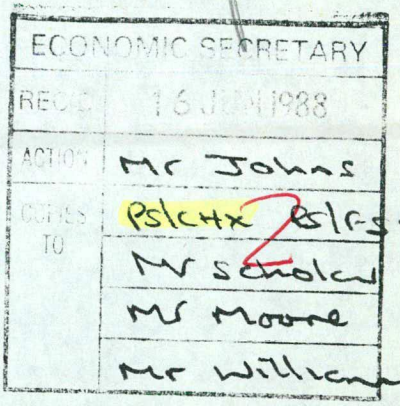

15th June 1988

Mr Peter Lilley
Economic Secretary to the Treasury
Treasury Chambers
Great George Street
LONDON
SW1

Dear Mr Lilley

I thought you would be interested in seeing a copy of a letter which we have just sent to all Members of Parliament with an interest in energy matters, on the subject of the royalty and PRT changes recently put forward in relation to southern basin gas fields. PS/IR

We are concerned that the measures proposed in the Finance Bill adversely affect the economics of individual gas fields, leading to a reduction in project value. This applies to fields which we are considering for development in the future, but also for fields developed from 1982 onwards on which Britoil and its partners have already made considerable commitments of investment funds.

You will be aware that there have been a number of discussions between our staff and your officials, as well as representations by UKOOA. We welcome the amendment to Clause 129, announced on June 14th, which increases the oil allowance to 125,000 tonnes per chargeable period, but would reiterate that this falls far short of what is required.

Yours sincerely

W J Saint
Chief Executive

J. E. GORTON

TELEPHONE
01-920 6456
(SWITCHBOARD 01-920 8000)

BRITANNIC HOUSE,
MOOR LANE,
LONDON, EC2Y 9BU

15 June 1988

FINANCE BILL - SOUTHERN GAS BASIN FISCAL REGIME

The Government's proposed changes to the tax regime for gas field investments are of great concern to BP as a result of their impact on our Britoil portfolio.

In separate legislation the Government proposes to abolish the royalty levy on new gas fields, a measure which has our full support. In order to pay for this measure, clause 129 proposes a reduction in oil allowance to offset against petroleum revenue tax (PRT). Our concerns are twofold. Firstly, the increase in PRT from this measure is to be derived principally from fields committed between 1982 and 1987, thereby penalising companies such as Britoil: during this period Britoil and their partners committed over £2,000 million to the development of seven gas fields, the profits from which have been seriously eroded by the drop in gas prices resulting from the oil price collapse in 1986.

Secondly, we believe that the proposed reduction in oil allowance over-compensates for the abolition of royalty and that there will be a substantial net penalty to Britoil and its Southern Basin gas fields. The objective of the measures was to encourage the development of more gas fields, but we believe that the impact will have the opposite effect and unless significantly modified will deal a severe blow to the industry's investment confidence which will impact adversely on future activity.

In discussions on this issue, officials have acknowledged that the differences in perceptions of the impact of their proposals are attributable partly to differences in forecasts of prices but also partly to the Government's use of out of date or inaccurate data.

The industry proposal is that the level of oil allowance should be set at a minimum of 160,000 tonnes per 6 month period (compared to the existing level of 250,000 tonnes and the level of 100,000 tonnes proposed in clause 129). I understand that the Government is tabling an amendment to Clause 129 which would increase the oil allowance to 125,000 tonnes. While I welcome this as a move in the right direction, the amount proposed still falls far short of what in our view is required.

We would urge you to support the industry case. We should be pleased to furnish any further information you may require.

Yours sincerely,

Background Information for Members of Parliament

1983 Fiscal Changes

From 1983, the Government abolished Royalty for all new fields except those onshore and in the Southern Basin. On that occasion, far from being reduced, the oil allowance was doubled, from 250,000 to 500,000 tonnes per chargeable period (or from 5 million tonnes to 10 million tonnes in total).

These changes acted as an unequivocal incentive for new developments. This is evident from the figures for new field development consents outside the Southern Basin immediately prior to and after the fiscal changes.

Development Approvals

1979	4
1980	3
1981	0
1982	3
1983	5
1984	6
1985	8
1986	5
1987	6

This is a particularly good result in view of the fact that oil prices were falling from 1982. The stimulus was partly the direct effect of the 1983 fiscal changes, especially the removal of Royalty which is a non-profit-based tax that can make viable projects uneconomic. It was also the indirect effect on industry confidence of dealing with a Government that recognised the deterioration of industry prospects, and saw the need for new incentives to maintain the pace of development.

UKOOA Representations since 1983

Since 1983, the industry has been making representations that the Southern Basin should not be excluded from the beneficial effects of the tax changes which applied to the rest of the North Sea, based on the following arguments:-

a) Extending new field terms to the Southern Basin could help fill the impending gas supply gap through the 1990s from indigenous sources.

b) The existence of different tax regimes for new developments in the Southern Basin and elsewhere discriminates economically against Southern Basin activity and distorts the allocation of resources.

c) The harsher tax regime in the Southern Basin is a hindrance to the development of the smaller, high-cost gas fields that make up a significant portion of the new finds in that area. Royalty is a regressive tax, being non-profit-based, and therefore it has a more adverse effect on marginal fields.

Since the oil price collapse in 1986, gas prices have been substantially eroded, increasing the proportion of Southern Basin fields in the marginal category. In 1988, the industry argued, the time was ripe for an imaginative incentive to be given, such as the successful boost that was given to fields outside the Southern Basin five years earlier.

The 1988 Budget Proposals

In the 1988 Budget, the Government accepted the industry's argument that Royalty represents an unnecessary hindrance to new developments in the Southern Basin. To compensate for the cost of eliminating Royalty, they propose to reduce the oil allowance from its present 250,000 tonnes to 100,000 tonnes per chargeable period (or from 5 million tonnes to 2 million tonnes in total) which increases the Petroleum Revenue Tax payable. This would make the Southern Basin oil allowance one fifth of the level which applies to new fields elsewhere, increasing rather than eliminating the discrimination against Southern gas fields. These proposals affect not only future developments but all Southern Basin fields given development consent after April 1982.

UKOOA Members' Response

UKOOA has learned from consultations with its members that only 5 of the 37 members consider themselves better off as a result of the Budget - and then only marginally. The impact on already-committed post-1982 fields is of the greatest concern to the industry: operators estimated the reduction in the remaining net present value (NPV) of these fields (at 10% real) to be £216 million compared with the £60 million which was the Government's official estimate of the cost to industry. Impact on cash flow - the funds that would be used to finance new developments - was estimated by industry to greatly exceed the NPV figure.

As to future fields - the target of the Government's help - UKOOA estimated that the impact here would also be negative. Figures provided by 24 member companies suggested that the NPV of future fields in which they had an interest would be reduced in aggregate by some £83 million. Here again the negative impact on cash flow, a key, decision-infuencing factor, was many times larger.

Summary of Industry's Arguments

In summary, the industry's arguments are :

a) It is mistaken to 'rob Peter to pay Paul', i.e. to reduce the profitability of committed fields to help pay for the needed removal of a fiscal disincentive to the development of future fields.

b) It is unprecedented in the history of UKCS taxation for the Government to raise the tax burden in an era of falling prices.

c) The reduction of industry confidence in the tax regime will force companies to increase their economic thresholds for future oil and gas developments to compensate for additional fiscal risk.

d) Fiscal encouragement has worked before. We see a need for the fiscal regime to continue to be encouraging, especially at a time when oil and gas prices are low. The 'supply side' benefits of a well chosen incentive could mitigate or offset the anticipated reduction in Government take.

UKOOA Recommendation

In order to achieve the substantial benefit for future fields which was anticipated by the Government, an oil allowance of 200,000 tonnes per chargeable period would be needed. However, to achieve the overall balance between committed and future fields implicit in the Government's proposal, an oil allowance of 160,000 tonnes would be appropriate. This level would leave the committed fields in an approximately neutral NPV position in the aggregate, although a number of our members would continue to lose.

2nd June 1988

Inland Revenue

The Board Room
Somerset House
London WC2R 1LB

FROM: MISS A P LEES
DATE: 15 June 1988

PRIVATE SECRETARY TO THE FINANCIAL SECRETARY

INVESTMENT TRUSTS: LETTER FROM JOHN BUTTERFILL MP

1. Mr John Butterfill wrote to the Financial Secretary on 24 May on two points raised by the Association of Investment Trust Companies (AITC) - letter attached. We expect the Financial Secretary will want to write straightaway to Mr Butterfill as he has put down a Finance Bill amendment to Clause 109 (reflecting the second point), and may still do so on the other (Clause 108).

2. On the first point - that PEPs should not discriminate against investment trusts - we have drafted the reply along the lines we have been using since 1986 to defend the restriction. But the Financial Secretary has asked us and FIM (your note of 26 May) to review a number of options for extending PEPs, and this could well involve looking again at the position of investment trusts. The reply, therefore, does not entirely close up the possibility of a change.

Definition of Investment Trust

3. The second of AITC's points concerns the definition of investment trust companies in the Taxes Acts. This point is being handled by Mr Spence and Mr Bolton. The following paragraphs have been supplied by them.

---

cc PS/Chancellor of the Exchequer
Miss Wallis (MCU)
Mr Nelson
Mr Hewitt
Mr Gropper

Mr Corlett
Mr McGivern
Mr Spence
Mr Kuczys
Mr Bolton
Mr Walker
PS/IR
Miss Lees

4. Investment trusts are exempt from capital gains provided they satisfy the statutory tests in Section 842 of the Taxes Act 1988 (previously Section 359 of the Taxes Act 1970). As Mr Chappell explains, one of the conditions for the CG exemption is that the company's income must derive wholly or mainly from shares or securities. The Revenue's long standing practice is to regard this condition as satisfied if no more than 30 per cent of the company's income arises from other sources. We think that this is a generous interpretation of the statutory test, allowing investment trusts quite a bit of leeway.

5. AITC's complaint concerns futures and options, particularly forward currency arrangements, which do not fall within the expression "shares or securities". Consequently, income deriving from these sources has to come within the 30 per cent leeway.

6. AITC's basic concern is that if a large proportion of a trust's holdings of futures and options is treated as income for tax purposes (rather than as a capital gain) then this might - in extreme circumstances - use all the 30 per cent lee-way and take the proportion of income from shares and securities below the 70 per cent requirement. It is worth emphasising at this point that, unlike the Association for Futures Investment (some members of which saw you on 13 June), AITC does not complain about the basic proposition that the return on options and futures is taxable as income if the institution is trading in them. The investment trusts are not creating any difficulties on this score. Their only concern is on the potential knock-on effects of the tax treatment of futures and options on their CG exemption. Hence the proposition (in Mr Butterfill's amendment to Clause 109) that the "70 per cent of income" test should be widened to cover income from options, futures etc, as well as income from shares and securities.

7. If there were a real risk that investment trusts would lose their CG exemption on this count, we would recommend

remedial legislation (though we doubt whether the formula in Mr Butterfill's amendment is the right one). But on present evidence, the possibility of practical problems seems remote. This point figured in AITC's 1988 budget representations and was discussed in detail at a meeting with Revenue officials on 27 January at which Mr Chappell was present. As already noted, AITC's most immediate concern has been forward currency transactions. These are the subject of a revenue statement of practice, prepared in close consultation with AITC and issued shortly after the 27 January meeting. AITC said at the meeting that they welcomed the statement of practice and were hopeful that it should remove most of their problems in this area. Matters were, therefore, left on the basis that AITC would come back with further representations for a change in the law if, in the event, these hopes were disappointed.

8. Consequently, it is surprising that AITC should now be pushing for amendments in this year's Finance Bill and Mr Butterfill has, in fact, now tabled 2 amendments to clause 109. Accordingly, we suggest that you should write to him explaining why you cannot support the amendments. Hopefully, he will withdraw them. But, we will, of course, offer full briefing for use in debate.

MISS A P LEES

NOTE

I have just had a telephone call (unsolicited) from the Secretary of the Association of Investment Trusts. He had seen Mr Butterfill's amendment to Clause 109, and felt - as he put it - he needed to explain why they were now suggesting an amendment to the legislation whereas they had previously agreed that the right course was to see how the guidelines worked out, and to make representations for legislative change only if there proved to be practical problems. He said that, as Clause 109 offered a vehicle for an amendment, they thought it worth trying for a legislative solution now, rather than take the risk (however remote) that it would turn out to be a practical problem in future which needed a legislative solution (which would have to compete for Finance Bill space with other matters). AITC recognised it was unlikely that Ministers would legislate in this year's Finance Bill. If Mr Butterfill was told by the Financial Secretary that legislation this year was not on the cards, but got assurances that the point would be kept under review, that would be quite enough to satisfy AITC. He volunteered that if FST took this line in debate on the amendment they would advise Mr Butterfill not to press the point any further. My contact also volunteered the thought that if Mr Butterfill said - in the light of anything he had from FST before Clause 109 was debated - that he was inclined to take his amendment off the order paper then they would advise him this was quite all right by them.

I have revised Mr Bolton's draft of this part of the letter to Mr Butterfill in the light of what the Secretary of the Association said to me. It should help to ensure that there is a smooth run on this particular amendment to Clause 109 - and it may even persuade Mr Butterfill to take it off the order paper.

I R SPENCE

PS The FST may want to take out the last sentence of the first paragraph of the draft letter.

FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

June 1988

John Butterfill Esq FRICS MP
House of Commons
LONDON
SW1A OAA

Thank you for your letter of 24 May about the tax points raised with you by Mr Chappell on behalf of the Association of Investment Trust Companies. You asked whether it would be productive for you to put down amendments on these points for Committee. For the reasons set out in the rest of this letter, I do not feel able to meet either of these points in this year's Bill. I see that you have in fact put down an amendment to Clause 109 on the second point you raised - the tax definition of investment trusts. I leave it to you to decide whether or not it would be productive to leave your amendment on the order paper for Committee, in the light of what I have to say on this point.

First, he suggests that the Personal Equity Plan (PEP) Regulations should be amended to allow investment trusts to qualify as a PEP investment without any special restriction.

What he has in mind, I think, is to remove the existing restriction on investments in investment trusts and to allow such investments up to the maximum limit of £3000 a year (as they are allowed to do for UK equities generally).

The main aim of the PEP scheme is to encourage direct ownership of shares in UK companies. Although investment trusts are quoted companies in their own right they cannot provide the same relationship which is provided by a PEP Manager between the investor and the companies in which his funds are invested. Moreover, many investment trusts do have holdings in gilts and foreign companies, and distinguishing in the PEP regulations between those investment trusts with holdings only in UK equities and others would add an unwelcome complication. It was these considerations we had in mind when we built into the PEP scheme the restriction on investment in investment trusts.

I would not, therefore, be in favour of an amendment to the Finance Bill along the lines suggested. That said, we do review the PEP limits each year, and I shall certainly bear

in mind the Association of Investment Trusts Companies' views during our next review.

The second point which concerns Mr Chappell is the present definition of investment trusts for tax purposes, on which you have put down your amendment to Clause 109.

One of the conditions that an investment trust has to meet to qualify for tax exemption on its capital gains is that its income must be wholly or mainly derived from shares or securities. In practice this test is satisfied if 70 per cent of its income is from this source. This gives 30 per cent lee-way for income from other sources. As Mr Chappell says, a trust's return from investment in futures and options may (to a lesser or greater extent) rank as income for tax purposes. His concern is that the income from this source might be large enough to use up all the 30 per cent lee-way, and depress the proportion of the trust's income from shares and securities below the 70 per cent requirement. In that event, the trust would fail to satisfy the statutory test for investment trust status, and would lose its exemption on its capital gains.

I can say straight away that I would be quite prepared to consider a change in the statutory test for the definition of investment trusts if it became apparent that there was a real risk of investment trusts losing their entitlement to CG exemption in the way that Mr Connel fears. However, as matters stand, it seems unlikely there will be any real problem in practice. I base this view on the outcome of the detailed discussions Mr Chappell and his colleagues from the Association of Investment Trusts have had with the Revenue.

The starting point for these discussions was the industry's concern - entirely understandable - for clarification about the circumstances in which the return on futures and options would rank as income rather than as a capital gain. To the extent that the return is a taxable gain there is, of course, no problem. As Mr Chappell explains, the main problem area was the treatment of forward currency transactions. After discussion with the Association, the Revenue published a Statement of Practice on this subject. It is also the intention to produce further guidelines, on the tax treatment of options and futures generally, as soon as consultations are complete. The Association are a party to these discussions.

The Association expressed the view that, with these clarifications of the law, they were reasonably confident that most of the difficulties would be removed in practice. There was a concern, nevertheless, that some investment trusts might inadvertently fail to satisfy the tests because of unexpected fluctuations in income. The Revenue have, however, covered this point in the Statement of Practice.

They have said they would be prepared to review cases where there had been isolated and minor infringements of the statutory tests as a result of forward currency transactions being treated as producing income rather than capital gains.

Against this background, I am a little surprised that the Association should now be seeking amendments to the legislation before the guidelines have been tested in practice. As I am sure you would understand, I do not think it would be right to contemplate a legislative change until it is evident that there is a practical problem, and that legislative action is the only remedy for it. However, I can assure you that the application of the guidelines will be closely monitored to see whether they are producing a satisfactory result. The Inland Revenue have already told the Association that they will be very ready to discuss matters with them if there are difficulties with the practical application of the guidelines. If, against expectations, it proves that there are real practical problems which can only be resolved by legislation, then I can assure you I would be quite prepared to consider it.

I hope these assurances are helpful - and I would, of course, be very happy for you to pass them on to Mr Chappell and his colleagues at the Association of Investment Trusts.

NORMAN LAMONT

2715/2

CONFIDENTIAL

PS/CHIEF SECRETARY

FROM: MRS T C BURNHAMS
DATE: 15 June 1988

cc: PS/Chancellor
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary

Mr Culpin
Mr Gilhooly
Miss Evans
Mr Jenkins P.Counsel

Mr Denton IR

Mr Geddes C&E

FINANCE BILL: NEW CLAUSES

As requested I attach a list of all new clauses tabled to date. At present it looks as if there may be only two further clauses to add to the list of Government new clauses for Standing Committee. The Inland Revenue hope to be able to bring forward a clause to relax the rules for foreign earnings deductions for seafarers and another to amend the S.350 Charge for unauthorised unit trusts * at the Committee Stage. It may be however that it will not be possible to bring them forward until Report.

2. You also asked for advice on the order the clauses should be taken. Of the Government new clauses the one that is likely to be contentious is NC 29 - VAT on spectacles and hearing aids. It would be logical in relation to the order of the Bill and advantageous because of its sensitivity to deal with this clause first. I assume the Economic Secretary will handle this clause.

3. As to the order, there appears to be no natural order of precedence. As the clauses cover disparate subjects it may be most convenient to group them according to the "responsible" Minister but roughly in the same order as the different sections of the Bill. The order would be as follows -

NC 29	VAT on spectacles etc	EST
NC 32	Restrictive undertakings	FST
	[Seafarers	FST]
	[Unauthorised Unit Trusts	FST]
NC 36	Gains from settled property	FST
NC 31	Disposal of assets etc	PMG
NC 34	Jurisdiction of General Commissions	PMG
NC 32	Post consolidation amendments	?

TERESA BURNHAMS

* under consideration by FST

NEW GOVERNMENT CLAUSES

Already Tabled

NC 29 **VAT on Spectacles etc**

The new clause gives effect to a ruling of the ECJ that goods supplied by medical and allied professions may be exempted from VAT only if they are minor and indissociable from the services of medical ease. Its main effect will be to apply VAT at the standard rate to spectacles, contact lenses and hearing aids.

NC 31 Deemed disposal of assets on company ceasing to be liable to UK tax

The new clause is a necessary complement to Clause 99. It imposes a similar charge on unrealised gains when a company takes its assets out of the scope of the UK tax system, not by migration but by becoming resident in anothers country for double taxation treaty purposes.

NC 32 **Consideration for certain restrictive undertakings**

The new clause removes the present favourable tax treatment of payments to employees under restrictive covenants entered into with their employers. In future, such payments will be treated as if they form part of ordinary pay and payments will be deductable in the calculation of thc employer's taxable profits. It will apply to covenants entered into on or after 9 June.

NC 33 **Post Consolidation Amendments**

The new clause corrects errors in the Income and Corporation Taxes Act 1988. Some of the errors derive from pre-consolidation amendments made by the Finance Act 1987. There will also be a new schedule of amendments.

NC 34 **Jurisdiction of General Commissioners**

The new clause allows taxpayers to agree with their tax offices that appeals and other proceedings will be brought before General Commissioners other than those indicated by the Taxes Management Act. Follows consultation procedures.

NC 36 **Gains arising from certain settled property**

To prevent avoidance of higher rate CGT by non-discretionary Trusts through the use of settlements in which the settlor or his spouse has an interest.

Non-Government New clauses already tabled

NC 1	Profit-related pay	Beith/Wallace
NC 2	Mortgage interest relief	Beith/Wallace
NC 3	Independent taxation of pensions	Beith/Wallace
NC 4	Definition of a covenanted payment to charity	Beith/Wallace
NC 5	Bad debt relief	Sir W Clark
NC 6	Relief for expenditure on eligible securities	Beith/Wallace/Kennedy
NC 7	Accession Tax	Beith/Wallace/Kennedy
NC 8	Small scale Bingo	Watts and 13 others
NC 9	Relief for interest paid by personal reps	Butterfill and 8 others
NC 10	Additional loans to pay loan interest	Butterfill and 8 others
NC 11	MIRAS on 9 and 10 above	Butterfill and 8 others
NC 12	VAT gaming machines	Watts and 12 others
NC 13	Benefits in Kind threshold 1988/89	Sir W Clark/Sir M Fox
NC 14	Amendment of Sch 23 ICTA 1988	Sir W Clark/Sir M Fox
NC 15	Amendment of S 393 ICTA 1988	Butterfill/Riddick
NC 16	First year allowances for ships	Sir W Clark
NC 17	Replacement of a ship (roll-over relief)	Sir W Clark
NC 18	Earnings from work done abroad	Sir W Clark
NC 19	Relief for technical education and development	Sir W Clark/Beaumont Dark
NC 20	VAT zero rating	J Smith and 5 others
NC 21	Corporation tax deductions	J Smith and 5 others
NC 22	Anti avoidance	J Smith and 5 others
NC 23	Total reliefs (No 1) [£10,000]	J Smith and 5 others
NC 24	Total reliefs (No 2) [£20,000]	J Smith and 5 others
NC 25	Total reliefs (No 3) [£30,000]	J Smith and 5 others
NC 26	Restriction on reliefs [basic rate]	J Smith and 5 others
NC 27	NHS lottery	Barnes
NC 28	Removal of obstacles to employee ownership	I Taylor and 5 others
NC 30	Tax relief on company cars *	Shersby
NC 35	Woodlands (amendments to Inheritance Act 1984)	Arbuthnot/Boswell/Hurst
NC 37	Share options	Sir W Clark

* considered in SC 9 June

Inland Revenue

Policy Division
Somerset House

FROM: H B THOMPSON
DATE: 15 JUNE 1988

Mr Thompson's minute below draws attention to a flaw in the legislation. This works in favour of some taxpayers, to the disadvantage of others. It needs to be put right. The question is when. Deferring until next year would give longer to devise a more precise remedy and you might get away with not much tax loss; but there can be no certainty of either, and if the loophole were exploited, you would be criticised. There will also be those who are caught by an excessive withdrawal of indexation when the flaw works to the taxpayer's disadvantage. I incline to putting it right this year. DH 16/6.

1. Mr Pitts
2. Financial Secretary

FINANCE (NO 2) BILL - SCHEDULE 8

INDEXATION AND GROUPS

1. My note of 6 June sought your authority to table an amendment to clarify the meaning of a provision in Schedule 8. I am sorry to have to tell you we have found another, potentially more serious, flaw in the Schedule. This note asks whether you wish to introduce an amendment on the point or defer action (albeit at some risk of tax loss), either until next year or until abuse actually develops.

BACKGROUND

2. Schedule 8 counters arrangements by which groups of companies can use the capital gains indexation allowance to create large artificial capital losses by clothing intra-group lending in particular legal forms.

---

cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Mr Scholar
Mr Culpin
Miss Sinclair
Mr Cropper
Mr Jenkins (Parliamentary Counsel)
Mr P J Davies (Parliamentary Counsel)
Mr Isaac
Mr Painter
Mr Cleave
Mr Pitts
Mr Beighton
Mr Hamilton
Mr Cayley
Mr Thompson
Mr K Brown
Mr Gordon
Mr Gill
Mr T R Evans
Mr Denton
PS/IR

3. Paragraph 1 of the Schedule denies the indexation allowance on the repayment of a "debt on a security" to a linked company - that is, a company in the same group or an associated company. Paragraph 3 has corresponding but more complicated provisions for disposals of linked company shares.

THE FLAW

4. The flaw in the provisions is easiest seen by considering cases where there has previously been an exchange of shares for debt, or debt for shares, as part of a company reconstruction. Sections 78 and 85 of the Capital Gains Tax Act 1979 then come into play. Their effect is that the accrued gain on the old holding is transferred to the new holding, for taxation when the new holding is disposed of. As part of the mechanics for this, the new holding is deemed to have been acquired on the date - perhaps long before - when the old holding was acquired.

5. The problem arises when sections 78 and 85 shift gains which accrued on shares that are not caught by Paragraph 3 to a debt caught by paragraph 1, or vice versa. It arises because the new asset retains its true identity even though it is burdened with gains that accrued on a different type of asset and is treated as acquired when they were acquired.

6. In the first situation, the asset on which Paragraph 1 bites is a debt on a security. It did not itself come into existence until the time of the exchange, and it may be argued that indexation should be denied only for the period from that date until subsequent disposal - that is, for the period of its actual existence as a debt. But the wording of the paragraph also denies indexation for the inherited gain from the time the companies became linked - which may go back to the original acquisition of the shares. This is likely to be criticised as overkill.

7. In principle, the same applies when new shares caught by Paragraph 3 are given in exchange for "innocent" shares. But here the problem can be solved administratively. This is

because all disallowance of indexation under Paragraph 3 is to be on a "just and reasonable" basis. That method was adopted for Paragraph 3 (but not for Paragraph 1) to get round share pooling problems.

8. In the reverse situation a gain that accrued on an old debt, to the disposal of which Paragraph 1 would normally apply, has been transferred to new, innocent shares. The disposal of the shares escapes Schedule 8, and receives an indexation allowance (dated back to the time the debt was created) which it would not have had if the asset had either kept its original identity as debt or had not been given a fictional acquisition date. The same effect occurs when "innocent" shares are given in exchange for "tainted" shares; and here the "just and reasonable" provision in Paragraph 3 does not help.

POSSIBLE AMENDMENTS

9. The first situation (the putative overkill) could be remedied by amending the provisions so that Paragraph 1 denied indexation for the period after the actual creation of the debt only. But precisely targeted legislation might not be straightforward. It would be necessary to draft so that the amendment did not interfere with Paragraph 3 when shares within that paragraph were exchanged for debt. Subject to the views of Parliamentary Counsel - whom we have not yet consulted - this might mean falling back once more on the potentially controversial "just and reasonable" disallowance device.

10. The reverse situation requires disallowance of the indexation allowance on otherwise "innocent" shares for the period during which the inherited gains accrued on a "tainted" debt or shares . This would be more complex, and would almost certainly mean relying on "just and reasonable" disallowance for debt as well as shares.

THE NEED FOR ACTION

11. The first, overkill, situation is probably not urgent. We think it has been spotted by Linklaters and Paines, whose enquiry about the effect of the legislation drew our attention to it, and may therefore attract attention in Committee. But the situation need not arise in new company reconstructions - the creation of a debt on security can be avoided. For past reconstructions the case for saying there is an overkill is not clear cut. There could certainly be cases where large gains that accrued on "innocent" shares are shifted to "tainted" debts and so stand to lose the indexation allowance. It may however be argued that those who have arranged their affairs so that accrued gains are shifted onto a form of security ripe with avoidance possibilities do not deserve much sympathy; and that unless strong pressure for early action develops the point might well be left over for the time being. But if the point is raised, it will add fuel to the criticism of the clause as being, in a sense, "retrospective".

12. The reverse situation carries a risk of large tax losses. Suppose a group has set up the debt on a security device against which the provisions are aimed. The debt remains in existence for some time in order to build up an "indexation" period. At present, the device is brought to fruition simply by repaying the debt. That is a disposal, and Schedule 8 defeats the device by denying indexation. Now suppose that when the group is ready to harvest the device, it first exchanges the debt for newly issued shares. Apart from section 78, that would be a disposal of the debt. The gain - normally nil - would come into charge, and Schedule 8 would bite to prevent indexation from turning it into an allowable loss.

13. But section 78 intervenes. There is no disposal at the time of the exchange. The group now disposes of the replacement shares. As they have not appreciated there is no gain. And since they have only just been created, there should be no indexation allowance. But because section 78 treats them as

having been acquired when the debt was acquired, the disposal qualifies for an indexation allowance from that time. By inserting the extra step, the artificial indexed loss is obtained after all.

14. There are strong arguments for acting now to block this loophole:

- it may carry almost as much potential loss as the main device, which could enable many hundreds of millions of pounds of indexed losses to be created, and certainly more than the point discussed in my note of 6 June;

- it is possible that the loophole is already know to some advisers, and it would not look well to introduce legislation this year which well-advised people were able to walk round because of a defect;

- even if the loophole has not been spotted, it would be right to block it before it is;

- if the "overkill" point was raised in Committee and it became necessary to legislate for it on Report, the loophole would have to be dealt with at the same time. This could lead to charges of either ignorance of the full impact of the legislation or failure to mend a serious known flaw until pressed; perhaps both.

15. Against that, it may be said

- when the issues were weighed last October, it was thought that the extra cost to the Exchequer of deferring the legislation now in Schedule 8 until 1989 was unlikely to be very great; and there is no reason to change this view;

- the necessary capital reconstruction, involving conversion of loan stock or redeemable preference shares into ordinary shares, would not be straightforward;

- we have some defences: the existence of the underlying loan or the artificiality of the inserted step might make the scheme vulnerable;

- further action against past exchanges might be sensitive: the measure is already under attack as retrospective;

- the strong nature of the provision as it now exists may deter creation of new debts or redeemable preference shares to take advantage of the loophole;

- debts or redeemable preference shares created now to take advantage of the loophole will anyway need time to mature.

CONCLUSION

15. We shall be glad to know whether you wish to bring forward an amendment on the topic, and if so whether you are content to adopt the "just and reasonable" approach for both aspects. If you wish to bring forward an amendment we shall need to instruct Parliamentary Counsel urgently, and even so it may not now be possible to act until Report stage. If not, we shall be glad to know whether you wish us to pursue the matter as a Starter for next year, or whether you would prefer us simply to monitor the position with a view to bringing forward legislation if and when abuse actually develops.

H B THOMPSON

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Standing Committee A

FINANCE (NO. 2) BILL

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

Ninth Sitting
Thursday 16 June 1988

CONTENTS

CLAUSES 52 to 62 agreed to, some with amendments.
SCHEDULE 5, as amended, agreed to.
CLAUSE 129, as amended, agreed to.
CLAUSE 130 agreed to.
Adjourned till Tuesday 21 June at half-past Four o'clock.

Members who wish to have copies of the Official Report of Proceedings in Standing Committees sent to them are requested to give notice to that effect at the Vote Office.

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not later than

Tuesday 21 June 1988

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Standing Committee A

Thursday 16 June 1988

[MR. JOHN HUNT *in the Chair*.]

Finance (No. 2) Bill

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

Clause 52

PERSONAL PENSION SCHEMES: COMMENCEMENT.
1987 c. 51

4.30 pm

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

Mr. Nicholas Brown (Newcastle upon Tyne, East): Even in the great and searing symphonies of Shostakovich there are quieter moments. I suspect that that is also true of Finance Bills, and this sitting may be one of our more placid. Pensions do not, perhaps, have the same high political profile as abuses of the business expansion scheme, but we have important points to make.

The theme of our remarks and inquiries to the Financial Secretary relate directly to the need for firm protection for the consumer. Such protection is all the more necessary with a sophisticated product. The arrangement of pension affairs is probably the most detailed and important set of financial arrangements that the ordinary citizen makes in his or her life.

The average citizen, with no specialist knowledge, is entitled to protection and certainty. That is all the more important if choice is expanded. Our fear is that the clause may not give consumers sufficient safeguards. On that point, I wish to press the Financial Secretary for some reassuring comments that will provide certainty before—and not after—some terrible scandal emerges.

We have had some awful warnings. Indeed, on Monday the House debated the difficult set of circumstances that now pertain to the firm of Barlow Clowes. That state of affairs should not have arisen. The fact that that group is in difficulties relates directly to the question of regulation—the nub of our reservations about the clause. The Government have appointed an investigator to look into the Barlow Clowes mess and I hope that he gets on with it quickly. However that does not excuse previous incompetence and neglect.

Briefly, the problem is this. Until March 1985, Barlow Clowes' main activity seems to have been dodging taxes by manipulating gilt-edged stock—bond washing. I shall have more to say about washing later. Bond washing was outlawed in 1985, but Barlow Clowes continued to offer a gilt-edged bond with a high rate of interest, income tax free and with no reduction in capital redemption. Given those implausible circumstances, what on earth were the regulatory authorities doing? How on earth could any professional, considering that set of parameters, expect the operation to work in practice? Yet, nothing was done, and investors were left to make their own judgments. The chickens have come home to roost.

Is the Government's attitude that investors and purchasers of pensions be left to make their own judgments? It is unfair for the Government to expect ordinary citizens and investors, such as the purchasers of pensions, to make their own judgments without any guarantee that basic minimum standards, enforced by the Government, have been met.

Mr. John Butterfill (Bournemouth, West): Does the hon. Gentleman accept that the Government introduced a detailed system of regulation through the Financial Services Act 1986? But in creating some of the self-regulatory organisations that are envisaged by that Act, which the Labour party supported in its Committee proceedings, FIMBRA—the Financial Intermediaries, Managers and Brokers Regulatory Association—has had many teething troubles to overcome. Given the all-party support for the establishment of that SRO, it is a little churlish of the hon. Gentleman to take that attitude.

Mr. Nicholas Brown: I have not finished my remarks yet and I am sorry that the hon. Gentleman accuses me of churlishness. The Opposition are not alone in thinking that the hon. Gentleman is really good value. He is substantially right in what he says. It is right that the principles behind the Financial Services Act 1986 have all-party support. Later, I shall acknowledge what the Government have done, so the hon. Gentleman's accusation is a little premature.

Our problem is that we are unsure whether what has been done is sufficient to reach the goals for which we all aim in principle. We want adequate protection for the consumer and the opportunities for abuse to be limited. The fourth IDS Bulletin on pensions, issued in December 1986 says:

> "there is a danger of employees being subjected to high pressure sales techniques to persuade them to buy personal pensions—but there will be no rational basis for comparing rival claims and there is a great risk of money purchase schemes failing to produce the benefits people have been led to expect."

That anxiety is expressed not just by me, but by pensions professionals. I hope that the Minister can respond to that.

Such worries are expressed not just by specialists and the Opposition—I do not claim to have specialist knowledge—but by Lord Young who was quoted in the press recently as saying that the provisions of the Financial Services Act 1986 will require review. I am sure that his view is based on a similar approach to mine.

Mr. Butterfill: Does the hon. Gentleman agree that the disclosure changes, for which Conservative and Opposition Members pressed during the Committee stage of the Financial Services Act 1986 and which have now been implemented by Lautro are welcome

[Mr. Butterfill.]

because they enable investors to make a more informed choice?

Mr. Nicholas Brown: Yes. The hon. Gentleman's role in that is much commented on in the general literature on the subject. I support him in his campaign for the disclosure changes and I am pleased that the Government eventually acceded to his request.

But will those changes be enough to provide sufficient safeguards for ordinary, individual citizens when they decide on those issues? I hope that the Financial Secretary can respond to that complicated problem. Those are difficult decisions for people who have no specialist knowledge and who are entitled to clear statutory protection. They are particularly entitled to protection from misleading and over-persuasive advertisements. Although I do not claim to have specialist knowledge of pensions, I have some knowledge of advertisements.

The background that I share with the hon. Member for Fylde (Mr. Jack) was bound to emerge sooner or later. While has was working for Proctor and Gamble in Newcastle, trying to bring the merits of that excellent produce, "Daz", to the attention of a wider public, I was in the office, but along the corridor, trying to bring to the attention of a slightly different public the merits of that superior product, "Ariel". Later, I transferred to a product known as "Lenor", which provided housewives with a softness and freshness that they had never known before. That was the loving touch of new Lenor. Excellent though that product was—particularly in its marketing in those early days of its launch—it was slightly more expensive than the products of its competitors in the market.

The Chairman: Order. We are discussing personal pensions schemes, not personal freshness schemes.

Mr. Nicholas Brown: You are absolutely right, Mr. Hunt. but I was about to say that I am afraid that the same thing may happen with personal pension schemes.

Those who wish to advertise products must comply with detailed regulations. Will the Financial Secretary say when those regulations are to be enshrined in law and how they are to be enforced? Can those who wish to sell such schemes advertise generously and widely now, without being subject to the detailed regulations that are just around the corner? We are afraid that the residual impact of unregulated advertising may remain with us until much later.

We are also worried abut the application process that is described in the clause, and whether it has been properly scrutinised. We are concerned that unauthorised unit trusts could slip through the scrutiny mechanism, if only temporarily, Can the Financial Secretary describe how the scrutiny mechanism works in practice, and assure the Committee that it involves more than the mere scrutiny of a form that the applicant has filled in?

Finally, will the Government give an assurance about the arrangements for compensation funds? We have no quarrel with them regarding well-established areas, but in newer areas that are not currently covered by the Government's compensation fund arrangements, proper arrangements must be made and the Government must take responsibility for ensuring that the regulatory authorities insist that proper compensation arrangements are in place. It would be a disgrace if citizens who trust us to provide legislative safeguards for their affairs were let down because the general principle—which we all support—was not made law or put into practice by a Government who have some crimes to their name in other, similar areas.

4.45 pm

Mr. Doug Henderson (Newcastle upon Tyne, North): Reading the clause for the 50th time to try and understand the details left me somewhat unsettled by its contents. I thought that my uncertainty was such that there might have been an amendment to help me express my fears and reservations. It is a pity that that is not the case. However, I hope that in this stand part debate it will be possible to make some points and to pose a few questions.

It is widely known that the Opposition did not support the Government's changes to pension schemes. Although some aspects may be acceptable, the general trend of the clause moves away from protecting poorer and low paid people and those with less job security. We have been through these arguments before and it is unnecessary to repeat them.

The Opposition recognise the need to delay the Government's implementation of the provisions for six months because of the number of uncertainties which have arisen. I am doubtful whether six months is long enough. Perhaps the Financial Secretary will be able to assure us that it is adequate. However, I feel that there will be some difficulties.

The basic reason for the delay is that section 62 of the Financial Services Act 1986 relating to compensation was not in force early enough to enable the changes in pension plans to go ahead. We now know that that scheme will be in place in the autumn. Regarding the implementation date of the new pensions plans, if someone opts for a new scheme from 1 July and something goes wrong with the pension fund, what will happen between that time and the time when the compensation scheme becomes applicable? What will happen to people offered a pension fund by a company which is linked to the company which is in difficulties and has been in the news this week? Will there be automatic compensation for people who expect a pension based on their commitment and their contribution? Will the Government have something special to cover that? We need a specific answer to those questions.

We welcome the fact that insurance companies, unit trust companies and other institutions which might offer a pension in future are required to be registered by authorised organisation. I think that that provision is supported by all members of the Committee.

However, there are difficulties for people who are currently considering whether it is in their interest to opt for a private pension scheme. I know from people I have talked to in the industry that a number of

companies have improved their company scheme to try to persuade the existing employees who are members to retain their rights within that scheme. If one result of the changes in pensions is improvements in company schemes—albeit probably for the higher paid employees—that is welcome. I am sure that the Government can cite a number of cases where that has happened. But alarmingly, the very opposite has occurred in some circumstances.

There is a lot of confusion about the new pension scheme provisions. All of us—apart, perhaps, from the hon. Member for Bournemouth, West (Mr. Butterfill)—are probably confused by the various pension schemes available. Someone considering whether to take out a private pension must be confused.

There is an interesting example concerning Legal and General which, as members of the Committee know, is a highly reputable organisation which will manage pension schemes or provide individual pensions. However, Legal and General is trying to bribe its staff to opt out of the company pension scheme by offering, surprisingly, pay increases of between 5 and 10 per cent—depending on the age of employees—if they opt out of the scheme and make their own private provision with the company of their choice.

One reason why the company has felt it necessary to bribe its employees is that it wishes to get ahead while there is still some confusion. That is unfair to its employees; if I were one I should wish to know more about the details of the new pensions contracts. At present I would not know whether I would get compensation if I signed up with a company that got into financial difficulty after July.

This afternoon my hon. Friend the Member for Newcastle upon Tyne, East (Mr. Brown) demonstrated his detailed understanding of the advertising industry. My hon. Friend the Member for Leeds, West (Mr. Battle) is nodding approvingly. It is nice to see old comrades co-operating. I understand that the delay in bringing about the advertising code was a principal reason for the six-month deferral of the new pension scheme. We now know that the code will not come into force until 1 July.

I should like to ask the Financial Secretary whether the final contents of the code are agreed and whether they could be subject to further modification. Have the various schemes that have now registered and sought authorisation incorporated that advertising code into the literature that they are preparing to attract pension investors?

I think that it is unfair for people, employees of Legal and General and others, to be pressed without time for thought to decide on what in most cases is irrevocable. The scheme lays down the financial provision for much of the rest of their life, and certainly for their later years. If we are seeking to tidy up pension arrangements, to make proper provision and to ensure that cowboys are kept out of the industry, it would be better to include that advertising code in statute. We should have a period when companies can offer new pension schemes based on the new advertising code. At the end of six months, perhaps a year, the new pension arrangements—many of which will make an impact for many years—could be introduced at the same time as the tax relief provisions.

The Government are rushing a little. I understand their reasons for wanting to get on and get the job done without undue delay. However, they are seeking to jump the gun by introducing the new scheme before the compensation payment arrangements are in force and before the advertising code is applicable to companies that will be offering pensions.

It would be interesting to know how many firms have registered, showing that they would be wishing to offer insurance, and how many have been approved by the various bodies which have been given the task under the Financial Services Act 1986 of approving those pension companies. It would also be interesting to know how many other applicants are expected—how many parts of the industry have held back a little and perhaps will come into the business when they know what the compensation provision is and what the advertising code says. Many people are thinking about setting themselves up as a financial institution offering pension schemes, but they are biding their time until they see how things develop.

As my hon. Friend the Member for Newcastle upon Tyne, East said, we are talking about consumer choice. If people are to have maximum choice, they should be able to invest their money to obtain a pension in some of the other financial companies that will want to move into the business. A period of a year would enable that choice to be offered.

I do not want to take more of the Committee's time than is necessary, but it would be useful to defer clause 52 to allow more time, so that consumer choice and protection can be given top priority. Perhaps my fears are unfounded and the Financial Secretary will reassure me, but I detect that some Conservative Members have those same fears.

Mr. Alistair Darling (Edinburgh, Central): Although the clause is technical, it enables the Committee to have a useful discussion about the provision of pensions, bearing in mind, Mr. Hunt, your injunction to stay in order.

I speak as one of the younger members of the Committee. For many people of my age the problem of a pension is not urgent. Unless the retirement age is reduced substantially, I do not anticipate drawing my pension in the immediate future. One or two members of the Committee are probably in the same boat.

For many people the provision of a pension is taken for granted. That is especially true for younger people who assume that when they retire at 60 or 65 they will be provided for. It is odd that some young people express concern about the plight of pensioners and say, "Isn't awful that Mr. and Mrs. so and so have such a little to get by on," but they do not equate their situation with that of the pensioner couple because they cannot envisage what it will be like for them in 30, 40 or 50 years' time. That is a tragedy not from the point of view of those flogging pensions but for the country generally. People do not realise the changes that the Government have introduced to the state pension.

In 1978 when the state earnings-related pension scheme came into effect, many people said, "Oh good,

[Mr. Darling.]

that means that we shall get a good pension when we retire". Leaving aside whether or not that is true—certainly SERPS was a great improvement rather than nothing being done—I am not sure that people realise that the Government have changed SERPS and that men under 43 and women under 38 will not get what they might have thought they were entitled to. They will have to rely on the basic state pension. If anyone of my age has not done so, I urge them to find out how much the basic state pension is because it is not very much. If people have to rely on that alone, they will be in desperate trouble in their old age.

It is an indictment of this country that we are the third lowest of the EEC countries in our provision of old-age pension. The Government may say that we should consider not only the state pension, but all the other benefits—to quote Government spokesmen—to which people are entitled. If all the other benefits are considered, our provision is possibly worse than in other EEC countries. Old people relying on the basic state pension find it difficult to make ends meet. An elderly constituent of mine said graphically when told that her housing benefit had been cut, "I can afford to live for only another four years, after which my savings will be used up". It is an indictment of this country that in this day and age thousands of people are in that position.

The Government's philosophy is that we should not rely on the basic state pension except for special needs. I resent the mentality that argues that those who can put money by and who have good pension schemes can make provision for their old age, but for the rest it will be like the old Poor Law—there will be something there, but not much.

5 pm

The Government have a duty to tell people their plans. Advertising campaigns have been mentioned. One or two are aimed at people in work, and probably in good work, who are doing well under the Government and can look after themselves, but there is no advertising to warn those who may be in and out of work or on low wages, or who have part-time jobs—they make up a substantial proportion of the population—what lies in store for them in their old age. No wonder. That is probably the last thing that the Government want to tell them. The conditions that the Government have engineered are partly responsible for that miserable state of affairs.

I hope that the Minister will spell out the changes in last year's Finance Act and the social security legislation that reduce entitlement, especially for the younger generation who may not realise what lies in store. About 10 million people are not in pension schemes. What will be done to help them? It is all very well to help those who manage to help themselves, as the Government constantly do, but the bulk of the population find it increasingly difficult to make ends meet in their old age.

The Government recognise that the elderly population is increasing and that the number of pensioners at the beginning of the next century will be substantially up on the present number. That is why the Government changed SERPS. They did not identify the problem and set about dealing with it positively, but said, "There is a problem. It will cost too much, so let's make sure that people don't get that much and so save money. Let those who can make their own arrangements."

There is a philosophical difference in that the Labour party believes that the state should provide a decent pension that enables people to live with dignity in their old age, whereas the Conservative party believes that although there should be a fall-back position to enable a person to have a decent standard of living in old age, one should make one's own arrangements on a private basis. I readily accept that the cost of SERPS would be a significant factor in determining the money that the Government would have to raise over the years, but the balance is wrong and people will be left in an awkward position.

Even those who are in occupational schemes, or who will shortly go into them, will find that the Government are changing the rules on opting out. People are not fully aware of the options, or of the consequences of opting out or entering the money contracts or whatever scheme the Government introduce. It is no use the Government saying, "Let's rely on the salesman." Thanks to the Financial Services Act 1986 his best advice need only include what his own company has to offer.

The Chairman: Order. The hon. Gentleman is going wide of the clause. I remind him that clause 54 is about occupational pension schemes. Clause 52 is highly technical and deals mainly with commencement. Although I have listened with interest to the hon. Gentleman's remarks, I am not sure that they relate directly to the clause.

Mr. Darling: I beg your pardon, Mr. Hunt. I was about to leave the subject of occupational pensions. The clause may be technical, but the technicalities have been brought about because of the complications that I outlined.

Although the clause is technical, it underlines a problem that will haunt us in years to come. People are not aware of the minefield that the Government have laid, through which they must find their way. Will the Minister, who is considerably older than I am and who is likely to draw his pension sooner than I shall, consider the prospects of a younger person who looks forward to that with some dread?

The Financial Secretary to the Treasury (Mr. Norman Lamont): If the hon. Member for Edinburgh, Central (Mr. Darling) starts talking about my age, I shall start talking about his education. The hon. Member for Newcastle upon Tyne, East (Mr. Brown) compared his speech with a Shostakovich symphony—an entirely apposite comparison, of course. We discovered that Shostakovich can have some very jolly bits in it; I am not sure that the same is true of the Financial Services Act but none the less, hon. Members seem to wish that subject to dominate the debate.

Under last year's Finance Act, the new regime for the personal pension should have come into effect on 4 January 1988, but there were difficulties in the timetable for implementing the Act. The hon. Member for Newcastle upon Tyne, East rightly said that if someone takes out a money purchase personal pension scheme, he not only does not have the security of a Government scheme but he does not have the elements of assurance and security that there are in belonging to a large occupational scheme. He is wholly at risk and is devoting all, or a large part of, his life savings. Therefore, it is right that investor protection should be considered and it was in the light of that that we postponed the start date for the new regime.

The start date for the new personal pensions has consequences for the retirement annuities tax regime because that was going to be phased out at the same time as the personal pensions were increased, so clause 52 also provides for a similar deferral for retirement annuity contracts so that new contracts can continue to be made and premiums qualify for relief up to the end of June.

The safeguards that apply to personal pensions are extremely important and are provided for under the Financial Services Act. The hon. Gentleman wondered what the safeguards are and it is worth spelling them out before I refer to implementation.

Financial concerns and investment advisers are required to obtain authorisation from the self-regulating organisation if they are to carry on investment or advisory business. Before the self-regulating organisation grants authorisation, the firm will be thoroughly screened to ensure that it is fit and proper to trade. Once authorised, firms must trade according to good conduct rules, give informed advice with full knowledge of the client's circumstances and show due skill and diligence. If the rules are breached, there will be disciplinary measures and remedies, including compensation to be available to the client. Also as part of the investor protection are rules on advertising, cooling-off periods, commissions and compensation.

Mr. Rhodri Morgan (Cardiff, West): Does not the Barlow Clowes case demonstrate that although the Government have abolished SERPS, they certainly have not abolished twerps?

Mr. Lamont: Barlow Clowes has absolutely nothing to do with what we are discussing. Barlow Clowes is not a pension manager, but it was thoroughly predictable that the Opposition would drag it into the debate. It is just a pity that the case does not involve anyone with a name like Hoogstraten. That would have been even better. How lucky the Opposition were last week to have a man who sounded like a street in East Berlin or a Dutch football team to drag across their rhetoric.

Mr. Nicholas Brown: I am grateful to the Financial Secretary for giving way and allowing me to make my probably equally predictable intervention. Surely the example that we have cited is relevant to our debate today, because if it tells us anything, it tells us about the failures of Government to regulate properly in the financial sector. That is the substance of the clause that we are discussing.

Mr. Lamont: I think that it would be advisable not to go too far into the Barlow Clowes case, but the Financial Services Act is not yet in place. It is easily demonstrable that the strengths or weaknesses of the Government's proposals and regulation can hardly be proved or tested by reference to Barlow Clowes. As the Opposition seem determined to ignore the fact, I shall state yet again that Barlow Clowes is not a pension manager.

Mr. Butterfill: Does my right honourable Friend also recollect that deposit-based pensions and the regulations surrounding their advertising, which worry the Opposition, are not included in the Financial Services Act, because deposit-based pension schemes were not deemed to be investments for the purposes of the Act? I do not recollect any Opposition Member suggesting that they should be.

Mr. Lamont: I was going to mention deposit-based schemes and my hon. Friend has made a relevant point.

The hon. Member for Newcastle upon Tyne, East wondered how far the investor protection requirements were in place. The relevant provisions of the Financial Services Act are almost all in place, but I shall spell out to what extent they are not. Almost all will be in force by the new personal pensions start date in particular. On 29 April it became a criminal offence to undertake investment management or give investment advice without authorisation. Other detailed rules, such as cooling-off periods, are scheduled to coincide with the personal pensions start date on 1 July. The compensation scheme for authorised personal pension unit trusts, about which the hon. Gentleman asked, should be in place by August. Compensation for deposit-based personal pension schemes, to which my hon. Friend the Member for Bournemouth, West (Mr. Butterfill) referred, will be covered by compensation arrangements under the banking and building society legislation. Insurance companies already have arrangements and unit trust personal pensions will be covered by the end of August for the purposes of compensation. Other provisions and safeguards already apply to unit trusts.

The hon. Member for Newcastle upon Tyne, East asked about unauthorised unit trusts. They cannot establish a tax-approved personal pension scheme. He referred to the code of advertising practice, which deals with such matters as forecasts and projections of benefits that can mislead the public. Although they are not exactly part of the Financial Services Act, they are very important. That code will be in place by 1 July.

5.15 pm

Personal pension schemes can be established only by select categories of institution—an insurance company or friendly society; an authorised unit trust; a building society or pension company associated with it; a banking institution or one of its subsidiary holding companies. None of those categories includes Barlow Clowes, which the hon. Gentleman cited as an example

[Mr. Lamont.]

of an organisation that might cause problems in the market.

I agree that investor protection is very important, because many people's savings are involved. However, the provisions of the Financial Services Act, apart from the one exception that I gave, are in place. Having postponed the start date once, it would be an enormous mistake and unnecessary and regrettable to postpone it again. The development of personal pensions is keenly awaited, and will help to fill a gap.

The hon. Member for Edinburgh, Central (Mr. Darling) voiced some reservations about private versus state provision. That makes for a familiar political debate, but even he would accept that if we are to have an element of private pension provision we must not confine it to those who are fortunate enough to work for companies with occupational schemes. There are also people who intend to move around from company to company during their working lives. Personal pensions will give them greater mobility and help them to avoid the problems that come from having occupational pensions preserved on moving jobs. I believe that the start of personal pension schemes is to be welcomed. I appreciate the worries of Opposition Members about investor protection, but I am satisfied that the Financial Services Act has reached a state that makes it right for us to go ahead with personal pensions as originally intended.

Mr. Nicholas Brown: I am afraid that I am not sufficiently reassured by the Financial Secretary's remarks, although he has gone some way to meet our anxieties.

It is important that the Committee underscores the need for investor protection, and so I shall sound a warning note by forcing a Division.

Question put, That the clause stand part of the Bill:

The Committee divided: Ayes 24, Noes 12.

AYES

Arbuthnot, Mr. James	Lamont, Mr. Norman
Boswell, Mr. Tim	Lennox-Boyd, Mr. Mark
Bright, Mr. Graham	Lilley, Mr. Peter
Butterfill, Mr. John	Major, Mr. John
Carrington, Mr. Matthew	Maples, Mr. John
Coombs, Mr. Anthony	Mitchell, Mr. Andrew
Davies, Mr. Quentin	Nicholson, Mr. David
Favell, Mr. Tony	Shaw, Mr. David
Forman, Mr. Nigel	Stern, Mr. Michael
Howarth, Mr. Gerald	Wardle, Mr. Charles
Hunter, Mr. Andrew	Watts, Mr. John
Jack, Mr. Michael	Widdecombe, Ann

NOES

Armstrong, Hilary	Ingram, Mr. Adam
Battle, Mr. John	Marek, Dr. John
Brown, Mr. Nicholas	Morgan, Mr. Rhodri
Campbell-Savours, Mr. D. N.	Quin, Ms Joyce
Darling, Mr. Alistair	Smith, Mr. Andrew
Henderson, Mr. Doug	Smith, Mr. Chris

Question accordingly agreed to.

Clause 52 ordered to stand part of the Bill.

Clause 53

PERSONAL PENSION SCHEMES: OTHER AMENDMENTS

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

Mr. Nicholas Brown: May I underscore the reputation for churlishness that I seem to be acquiring among Conservative Members by saying in the most truculent and belligerent way possible that I have no quarrel at all with the third part of clause 53, and strongly support the Government on the first part of the clause. Indeed, the clause—it embraces company directors who were not previously covered by such legislation—is the sort of thing which the Labour party might have called for, so the comrades' Financial Secretary is to be supported. The Financial Secretary appears to be wondering what clause we are considering and I can tell him that it is clause 53. If he likes, I will steer the Bill through the House for him if he would like to change places. That will come in time.

In relation to clause 53(2), which will create wider confusions and difficulties, I ask why the alteration is being made in this way. The clause makes a significant change in that it facilitates an individual remaining a member of a contracted-in occupational scheme but enables him to take the benefit of a DHSS rebate and the incentive payment into a personal pension. I understand that without the change anyone in a contracted-in scheme would lose the incentive payment but the measure is a bizarre and clumsy way of seeing that they get it. The Committee is entitled to an explanation of the Government's approach. The Financial Secretary should explain, too, how the Government justify their previous stance.

Mr. Lamont: The clause has two proposals. The first, minor proposal exempts the personal pension scheme from additional rate tax, as it would apply to trusts. Secondly, and more importantly—this will interest the hon. Member for Newcastle upon Tyne, East (Mr. Brown)—it provides better terms in certain circumstances for members of occupational pension schemes who wish to contract-out of SERPS. It is not generally possible for occupational pension scheme members to participate in a personal pension at the same time. For topping-up purposes there are additional voluntary contributions but personal pensions are seen as complete alternatives to occupational schemes. That is because of the fundamental differences in the tax regimes for occupational and personal pensions. The clause will give the pension scheme members who do not wish to leave their employer's scheme the opportunity to contract out of SERPS on an individual basis through a personal pension scheme. The scheme itself will be contracted-in; the member of the pension scheme may wish to contract-out but without having to give up membership of his own scheme. Personal pension scheme rules should, in such cases, not permit contributions to the individual's account other than minimum contributions paid under the social security legislation. That is to say, the money that will be paid into the personal pension scheme will be the contracted-

out rebate. No other funds will be payable into the personal pension schemes but that would not prevent an individual from topping up his occupational pension within the normal limits, either by additional contributions or by contributing to his own free-standing AVCs.

The hon. Member asked why we were introducing such a proposal. We are doing so to widen choice because there are those who would like to contract-out of SERPS but who do not want to risk losing the benefits of the scheme to which they already belong. There is no good reason why they should not be permitted to do so and why people should not be permitted to create personal pension schemes of that kind. I hope that the proposal will be welcomed.

Question put and agreed to.

Clause 53 ordered to stand part of the Bill.

Clause 54

OCCUPATIONAL PENSION SCHEMES

Mr. Nicholas Brown: I beg to move amendment No. 278, in page 54, line 4, leave out paragraph (c).

This is a probing amendment. The clause relates to the Inland Revenue code of practice, which is now established as law. I understand that the Inland Revenue found the legislative framework too tight to deal with what are certain extraordinarily complex matters. To give itself more discretion, the Inland Revenue sought legislative sanction to discard certain rules by regulation. The clause seeks to give the Inland Revenue the power not just to discard existing rules but to change them and to make new regulations.

The Opposition do not wish to undermine the Inland Revenue in carrying out its important functions, but we must be sure that the Financial Secretary can justify the changes. That is all the more important because the changes take away parliamentary scrutiny of these matters by vesting the authority to change the rules in the Inland Revenue board rather than in Parliament. The Financial Secretary must justify what is being done, although we do not necessarily oppose it in principle.

Mr. Lamont: Clause 54 introduces a revised regulation-making power for dealing with the transitional difficulties arising from certain changes there were made in the Finance Act 1987. Hon. Members may recall that we made various changes to benefit limits, particularly the rate of accelerated accrual permitting maximum pension benefit only after 20 years, accelerated accrual of lump sums only to the same extent that pension benefits enjoy that accelerated accrual, and a limit of £150,000 on the tax-free lump sum.

When we introduced all those changes it was important to safeguard the position of people in existing pension schemes. We also had to have transitional arrangements to cover the situation of a person who might have been a member of a pension scheme before Budget day last year but whose pension arrangements were altered, either because the company was taken over and the scheme was amalgamated with another company scheme or the scheme was subsequently altered or reconstituted in some way. I think that the hon. Member would accept that the changes that we applied last year ought to apply to new schemes and new members of existing pension schemes so as to avoid retrospection. It became apparent that the original powers were not drawn widely enough to allow the regulations to protect existing pension scheme members from losing their right to the former rules, so no regulations have yet been made under those original powers.

Schedule 23 of the Taxes Act 1988 is unusual in that it overrides the rules of pension schemes. As the hon. Gentleman said, pension schemes are extremely diverse in form and structure and it is not necessarily easy to anticipate all the possible effects. It is therefore desirable that the regulation-making power should allow sufficient flexibility to deal with all deserving cases which may come to light. Paragraph (c), to which the hon. Gentleman referred, must be considered in that light. It is a sweeping-up provision, commonly included in regulation-making powers. None the less, the complexity and diversity of the subject means that the provision is necessary to help resolve problems that may not easily be foreseen. The provision is particularly directed at transitional arrangements when companies are taken over or other changes occur in the company's pension scheme which adversely affect existing members.

5.30 pm

Mr. Nicholas Brown: The Financial Secretary has explained the Government's reasoning on operating practice and fairness. Having heard his explanation, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 54 ordered to stand part of the Bill.

Clause 55

LUMP SUM BENEFITS PAID OTHERWISE THAN ON RETIREMENT

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

Mr. Nicholas Brown: The clause deals with tax exemption on retirement lump sums, and the extension of that to a period just following retirement. The clause sets a ceiling of £150,000 as the tax-free limit, but sets it out as a limit per policy. Do the Government intend that tax-free ceiling to apply per policy, which that is what the Bill will mean if it is enacted, or is that an anomaly which the Government will correct on Report? If it is not an anomaly, the Committee must ask who will benefit.

The only possible beneficiaries will be those who can afford the sort of retirement pension schemes and policies that offer £150,000 tax-free lump sums on retirement. Those sound like expensive schemes. If people can purchase more than one and get the £150,000

[Mr. Nicholas Brown.]

tax-free lump sum on each policy, the beneficiaries will be those whom my hon. Friend the Member for Wrexham (Dr. Marek) describes as the "super-rich"—or if they are not super-rich when they start paying into the schemes they certainly will be afterwards.

In fairness, should not everything be taxed as income after the first, and only, £150,000 tax-free lump sum, if such tax-free lump sums are to be retained? How many such policies can a person have with a tax-free lump sum from each? Do the Government think that a person who is infinitely able to afford it should be able to benefit from an infinite number of policies? That is surely absurd.

Mr. Lamont: The hon. Gentleman has raised an interesting point—I found it interesting, anyway—even if it is not wholly valid. I shall try to explain why his fears are somewhat exaggerated, although I will certainly reconsider the matter.

Under the legislation introduced last year, it will in future generally be impossible for someone to receive a lump sum on retirement in excess of £150,000. For occupational schemes, the limit generally applies, as the hon. Gentleman said, to the total of lump sums due from the various employers' schemes to which a person may have belonged during his career. It is the responsibility of the final employer to take account of lump sums from previous service in calculating what can be paid. For personal pensions, the limit applies individually to each arrangement, as the hon. Gentleman correctly identified. There are practical reasons for that and they are the same as the reasons why the tax relief on personal pension schemes operates differently for personal pension schemes and for occupational schemes. It is limited by reference to benefit for personal pension schemes and by the amount that one can contribute for occupational schemes.

There are strong practical reasons why the limit applies individually on personal pensions. There is no one in the same position as the final employer for occupational schemes who can take account of the lump sums from other arrangements and, if necessary, cut back on the lump sum. If someone has entered into many personal pension arrangements, no one pension provider can take an overall view. Moreover, we have tried to keep the administrative requirements for personal pensions as simple as possible. That means that one personal pension provider may not know of the existence of others.

It is theoretically possible that someone could build up a number of lump sums through personal pension arrangements, which may come to £150,000. The amendment seems to try to subject any excess over £150,000 to tax. That does not avoid all the practical difficulties. It would be necessary to check in every case whether the £150,000 limit was exceeded and to collect tax on that excess. What the hon. Gentleman fears is unlikely to arise in practice.

As I said, there is a distinction between the personal pension and the occupational regimes. The only limit on the available tax reliefs for occupational schemes is on the benefits payable on and after retirement—the two thirds rule. There is no limit on the total contributions that may be paid. There is a limit on employee contributions, but not on those of employers. It is important that the cap on lump sums is applied to aggregate benefits. One of the reasons why we acted last year was that we thought that people were putting money into occupational schemes in great quantities in the last years of their career and getting large amounts tax free.

For personal pensions, there is a control on the level of contributions. The limit is 17½ per cent of salary for the under-50s and a little more for older contributors. Few people contribute right up to the Revenue limit. Moreover, not more than 25 per cent of the total fund accumulated by retirement date may be taken as a tax-free lump sum. It is unlikely that many people could accumulate lump sums totalling as much as £150,000 because of the limit on contributions and because the lump sum that may be taken as tax free is lower. As personal pensions are just about to start, it will be many years before that danger becomes real.

I have noted what the hon. Gentleman said and I am grateful to him for highlighting the problem. It is unnecessary to reply before Report, but we shall consider whether we should make changes.

Mr. Nicholas Brown: I am grateful to the Minister for agreeing to re-examine the issue with a view to capping ultra-excessive generosity to the super-rich, to whom my hon. Friend the Member for Wrexham referred. Any Government commitment on that is welcome. To underscore our seriousness and to make our view abundantly clear before we have a chance to study what the Financial Secretary has said on the matter, I seek to divide the Committee.

Question put, That the clause stand part of the Bill:—

The Committee divided: Ayes 23, Noes 11.

AYES

Arbuthnot, Mr. James	Lennox-Boyd, Mr. Mark
Boswell, Mr. Tim	Lilley, Mr. Peter
Bright, Mr. Graham	Major, Mr. John
Butterfill, Mr. John	Maples, Mr. John
Carrington, Mr. Matthew	Mitchell, Mr. Andrew
Coombs, Mr. Anthony	Nicholson, Mr. David
Davies, Mr. Quentin	Shaw, Mr. David
Forman, Mr. Nigel	Stern, Mr. Michael
Howarth, Mr. Gerald	Wardle, Mr. Charles
Hunter, Mr. Andrew	Watts, Mr. John
Jack, Mr. Michael	Widdecombe, Ann
Lamont, Mr. Norman	

NOES

Armstrong, Hilary	Ingram, Mr. Adam
Brown, Mr. Gordon	Marek, Dr. John
Brown, Mr. Nicholas	Quin, Ms Joyce
Campbell-Savours, Mr. D. N.	Smith, Mr. Andrew
Darling, Mr. Alistair	Smith, Mr. Chris
Henderson, Mr. Doug	

Question accordingly agreed to.

Clause 55 ordered to stand part of the Bill.

Clause 56

ASSESSMENT AND COLLECTION

Mr. Lamont: I beg to move amendment No. 191, in page 54, line 24, leave out "to this Act".

This is a minor drafting amendment, which removes some redundant words from clause 56(1). Later I shall seek to explain what clause 56 is about, which is a more important point.

Amendment agreed to.

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

Mr. Nicholas Brown: I shall seek to redeem my reputation for churlishness, which the hon. Member for Bournemouth, West (Mr. Butterfill) has given me, as brazenly as possible, given the encouragement that I am now receiving from the Financial Secretary.

I support what I understand to be the broad thrust of the clause, which seeks to roll up interest, income and gains, and insists that underwriting losses are offset against them in total. I should like to make two points. First, it appears that there is nothing to prevent annual capital gains exemption—currently £5,000—being deducted before it is added to profit. Will the Financial Secretary tell me whether that is an anomaly or the Government's intention?

5.45 pm

Secondly, if net losses are available to an underwriter under the tax rules, should they not be limited to those that can be offset at basic rates?

Mr. Lamont *rose—*

Mr. Brown: Brazen it out!

Mr. Lamont: The purpose of clause 56 is not quite as the hon. Gentleman describes. It is more far reaching.

Clause 56 and schedule 5 introduce a considerable reform in the administrative arrangements for assessing and collecting income tax from Lloyd's members. Clause 59 makes consequential amendments but the new arrangements are the outcome of extensive consultations with Lloyd's and, although they have no revenue effect, they benefit administratively both Lloyd's and the Revenue.

The present system is extremely complex. It gives rise to successive delays for the Revenue, and its problems are reflected in corresponding problems for Lloyd's and there can be considerable delays in obtaining repayments of tax when it incurs losses. The complexity of the system imposes enormous compliance costs on Lloyd's, its agents, accountants and the members themselves.

The need for simplification has become urgent in the light of the rapid increase in Lloyd's membership, and the legislation on reinsurance to close premiums, which will involve more detailed scrutiny of syndicate tax computations. If nothing were done, the position would become more difficult.

The new arrangements will produce a simpler, more effective system for taxing Lloyd's members. It will match the tax arrangement to the way that Lloyd's itself operates in practice. In doing so, it will cut down the number of separate tax calculations which bedevil the present system.

The first change made by the new system, which is dealt with in clause 56, means that all Lloyd's members' incomes from underwriting activities will be charged to tax under case 1 of schedule D as income from the underwriting trade. At present this treatment applies to underwriting profits and losses. It does not apply to the Lloyd's members' syndicate investment income which is a member's other source of income from his underwriting activity.

This change in the basis of assessment does not alter the tax liability, but it will bring the two together. Assessing both streams of income will be a major simplification.

Schedule 5, introduced by clause 56, deals with the responsibilities of syndicate agents. The machinery is designed to ensure that agents provide the information about syndicate profits and losses which is needed to determine the tax liability of individual members. The main feature of the machinery in the schedule is that it will introduce effective machinery for establishing the amount of taxable profit and loss made by the syndicate.

The agent will be responsible for making a return of the taxable profit or loss and he will be responsible for appeals against the inspector's determination of that profit or loss.

Mr. D. N. Campbell-Savours (Workington): Why is this change being made?

Mr. Lamont: The change is for administrative reasons. It does not affect tax liability. It is for the convenience of the Revenue and Lloyd's members and about arrangements for the collection of tax.

A feature of the machinery is that it will make the syndicate agent responsible for making a return of the taxable profit or loss. The syndicate agent will be given legal responsibility for what he already does in practice. At present the agent submits tax computations, deals with the inspector's questions and discusses any points of dispute. These responsibilities are inevitable because the agent is the only person in a position to exercise them. At present he has no legal authority or responsibility for the process. In theory all responsibilities belong to the individual syndicate members, even though in practice they have no way of exercising them, which is nonsense.

The syndicate agent will also be responsible for making a payment on account of basic rate tax on the syndicate profit. This is a simplification and rationalisation of the existing system. At present the agent makes a payment on account for syndicate investment income, but he does not do so for the underwriting profit. His different treatment of the two sources of income is a major reason for the complexity of the present system.

Under the new arrangement, the syndicate agent will make a payment on account of basic rate tax on both sources of income taken together. The system will be straightforward for the agent.

Mr. Campbell-Savours: The liability remains the same, but might it affect the time when payments are made to the Revenue? Might it lead to a deferment of a year on one component in the new aggregate?

Mr. Lamont: It has all sorts of effects on timing both ways, but it will not specifically create a cash flow loss for the Revenue. I assure the hon. Gentleman that the provision is being introduced for administrative reasons.

Mr. Campbell-Savours: They always are.

Mr. Lamont: And very much at the behest of the Revenue.

The last component is assessment of tax on individual members. Under the new system a member will be assessed on his aggregate profit for all his syndicates six months after the agents have made their payment on account of basic rate tax. The assessment will cover both basic rate and higher rate liability. It will take account of any adjustments made to syndicate profits or losses since the agent put in his tax computation. The change will also be a major simplification.

The hon. Member for Workington (Mr. Campbell-Savours) asked about capital gains. I am happy to respond because I intended to discuss them. The changes in the administrative arrangements do not affect the treatment of Lloyd's members' capital gains. The existing administrative arrangements for dealing with Lloyd's capital gains work satisfactorily and there is no need to change them.

It is true that Lloyd's members' capital gains from premium trust funds are treated differently from those of other financial traders. Lloyd's members' capital gains fall within the individual capital gains code, whereas other financial traders' gains are subject to income tax as part of their income. This is the aspect about which the hon. Gentleman for Workington asked. The arguments for and against bringing the tax treatment of Lloyd's members' gains into line with that of other financial traders were considered in the pre-Budget discussions with Lloyd's. It was decided to leave the present arrangement unchanged, but the point will be kept under review for the future.

I apologise for spelling out the provision in more detail than may have seemed necessary, but these are time-consuming and, from Lloyd's point of view, important matters. They have taken a long time to resolve and it was important to get them on the record.

Mr. Nicholas Brown: I am grateful to the Financial Secretary for the concession on the last point. As for the rest, I am afraid that the excitement may have been too much for me, so we shall not press a Division.

Question put and agreed to.

Clause 56, as amended, ordered to stand part of the Bill.

Schedule 5

UNDERWRITERS: ASSESSMENT AND COLLECTION OF TAX

Amendments made:

No. 192, in page 128, line 2, after "and," insert "(c)".

No. 193, in page 128, line 2, after "profit,", insert "containing".

No. 194, in page 128, line 35, leave out "(b)" and insert "(c)".

No. 195, in page 129, line 13, leave out "(a)".

No. 196, in page 129, line 17, leave out "(a)".—[*Mr. Norman Lamont.*]

Mr. Lamont: I beg to move amendment No. 197, in page 130, line 46, leave out from "(a)" to "section" in line 49.

The Chairman: With this it will be convenient to take Government amendment No. 198.

Mr. Lamont: The amendment corrects a drafting defect in the rules extending the normal time limits for late assessments on Lloyd's members. The extension of the time limit in paragraph 8(2)(a) of schedule 5 goes further than intended. The amendment corrects this defect.

Amendment agreed to.

Amendment made: No. 198, in page 130, line 53, at end insert

"and

(b) in the case of a variation, an assessment which gives effect to the determination as varied shall not be out of time if it is made within one year of the date of the variation.

(3) sub-paragraph (2)(b) above shall not apply in the case of a variation under paragraph 4(3) above which is made later than six years after the end of the closing year.".—[*Mr. Norman Lamont.*]

Question put and agreed to.

Schedule 5, as amended, agreed to.

Clause 57

REINSURANCE: GENERAL

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

Mr. Campbell-Savours: I should like to ask a question of the Minister about the clause, especially about proposed new subsection 450(4)(b) of the Taxes Act 1988, which is given in subsection (1). Will he explain what the positon was hitherto?

Mr. Lamont: I shall certainly require advice to know what the immediate predecessor of paragraph 4(b) was, but while waiting for that clarification I am happy to tell the hon. Member for Workington (Mr. Campbell-Savours) what the clause is about.

The clause corrects a minor anomaly in the special tax rules dealing with insurances policies known as

stock loss policies, taken out by Lloyd's members to insure themselves about possible losses. The payment of the insurance premium is deductable for tax purposes. If a loss occurs, the Lloyd's member's receipt of the insurance money is correspondingly treated as a taxable receipt. A sensible result would be for the taxable receipt to come into account for tax purposes in the same year as the loss that gives rise to the payment to the member under his insurance policy.

In most circumstances the existing rules give that result. However, they give a different, irrational result where a Lloyd's syndicate is running on. The hon. Member for Workington is familiar with that situation, where one or more accounts is kept open beyond normal closing date. For example, a 1979 syndicate might still be open in 1987 instead of the 1979 syndicate having closed its account by paying a reinsurance to close premium in the normal way at the end of 1981. 1981 is just a date that I have chosen as an example.

In those circumstances, a loss arising in 1987 will be taken into account for the 1985 underwriting year. As the hon. Member for Workington knows, Lloyd's operates on a three-year basis. This is a sensible result, given the way in which Lloyd's operates commercially.

The problem with the present rules is that the insurance moneys received would rank as a taxable receipt for the 1979 year of assessment, because that is the year in which the insurance premium was paid. The new rule will correct the mismatch and ensure that the tax charge on the receipt of the insurance premium occurs in the same year as the tax relief for the loss that gave rise to the payment of the insurance money. So the mismatch in the timing of receipts and losses for tax purposes will be removed, and members of running-off syndicates will be treated in the same way as other Lloyd's members.

My explanation has already covered the hon. Gentleman's question about the present position under subsection (4)(b) of the Taxes Act 1988. I apologise for being unable to identify the precise point in the words of the legislation, but the clause is fairly uncontroversial and clear.

Question put and agreed to.

Clause 57 ordered to stand part of the Bill.

Clause 58

REINSURANCE TO CLOSE

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

6 pm

Mr. Nicholas Brown: In supporting the main thrust of the clause and the scrutiny by the Inland Revenue of reinsurance to close premiums, I should like to raise an important issue. In the light of recent damaging scandals that have beset Lloyd's, it is difficult to see how even this Government could have done other than introduce closer scrutiny of those arrangements by the Inland Revenue. In assessing what is fair and reasonable in allowing a reinsurance premium to close, when will the Government deal with the computing of outstanding liabilities on a discounted basis? The issues are complex to those who have no background in the insurance industry, but it is the view of the Labour party that insurers should make proper and adequate provision for unexpired risks. Indeed, the whole Committee will accept that they would be wrong not to do so.

However, insurers should have regard to the present value of the liability. If they cannot resist the temptation to take an exaggerated view of the risk rather than let the money go to the Inland Revenue, it is the duty of the Inland Revenue to ensure that the taxman's due is obtained by the taxman rather than retained by the industry. The investment of premium income is an integral part of the insurance business. That obvious point must be taken into account when calculating the original sum necessary to cover the remaining risk, because naturally income will be generated.

Another matter that concerns us is the possible abuse of the special reserve funds as a tax avoidance mechanism. In principle, the matter is the same as the one to which I have just referred: there is the same scope for misuse, and I press the Financial Secretary on the Government's intentions in closing such options.

Mr. Lamont: On the special reserve fund, we have left the position as it is. The hon. Gentleman obviously thinks that the special reserve fund is an anomaly and should not be allowed—

Mr. Brown: The Financial Secretary is misrepresenting my position. I am not saying that a special reserve fund is an anomaly that should not exist at all. But it should not be a mechanism that can be used for tax avoidance. That is a slightly different point.

Mr. Lamont: I wholly misunderstand the hon. Gentleman's point. The special reserve fund is there to give members of Lloyd's some tax privileges and exemptions from tax in respect of the special liability that they have as members of Lloyd's. I am not sure how such a fund can be abused. The main issue about the special reserve fund is whether it should have been enlarged. That has been the subject of past representations from some members of Lloyd's. We rejected those representations because we took the view that members of Lloyd's were major beneficiaries of the general tax cuts in the Budget. Therefore, there was no case for enlarging the privileges of special reserve funds.

The hon. Gentleman also asked about discounting. All I can say is that under the present law, the legal position on discounting is under consideration. But I cannot go further than that.

Clause 58 is the main clause affecting Lloyd's in this year's Bill. The clause modifies the effect of the legislation that we introduced last year. It gives relief from the effect of the reinsurance to close legislation to Lloyd's members who leave syndicates. The provisions also produce simpler, fairer treatment for those who continue their syndicate membership. Those proposals

[Mr. Lamont.]

have been fully discussed with Lloyd's members and their comments have been taken into account.

Neither of the changes affects in any way the basic purpose of the reinsurance to close legislation, which was to ensure that the tax deductibility of RIC premiums was put on a proper basis in a way that was effective but also fair to Lloyd's members. The test for tax deductibility is that the premium shall be tax deductible to the extent that it represents a fair and reasonable assessment of the value of the liabilities transferred by the year 1 syndicate to the year 2 syndicate that takes on the responsibility for meeting those liabilities. That formula, which fully protects the interests of the Exchequer, was arrived at after detailed discussions with Lloyd's members. It fully met their concern that the criteria for tax deductibility should take account of the special features of Lloyd's business.

Mr. Campbell-Savours: When the Minister says that the formula fully protects the interests of the Exchequer, am I wrong in presuming that there is an Exchequer cost to the clause? I should have thought that there was.

Mr. Lamont: There might be over a period of time, but it would be almost negligible.

I should like to explain how the clause operates. It deals with the only aspect that caused concern last year, which my hon. Friend the Member for Croydon, South (Sir William Clark) raised directly with me in debates on the Bill. He said that in some respects existing rules would produce unfair results. I have come to the conclusion that he had a point. The problem that my hon. Friend referred to stems from the fact that the payer of a premium in year 1 receives a tax deduction for it, and the person who receives that premium in year 2 has a taxable receipt. It follows that if £100 of a premium is disallowed for tax purposes under the legislation, the payer of the premium will be taxed on that same sum and the recipient of the premium in year 2 will get a corresponding credit reducing his taxable receipts.

The present rules produce an equitable result if a person continues his syndicate membership and has the same share of the business in one year and the second year. The problem is the mismatch between the taxable receipt and the deductibility if the person in the syndicate leaves. The person in the second syndicate then receives the full benefit of the credit.

As my hon. Friend the Member for Croydon, South pointed out, the present rules provide an unsatisfactory result for members who leave the syndicate. They can also produce an unfair result for continuing members whose share of the syndicate business changes between years 1 and 2. In practice, most members of Lloyd's are in that position. I understand that it is very common for shares to alter. The member who reduced his share in the year 2 syndicate would find that his credit for year 2 was smaller than his tax disallowance for year 1, so he would pay too much tax. Correspondingly, the member with an increased syndicate share for year 2 would have a bigger credit for that year than his tax disallowance for year 1.

Our solution is simple. A member who leaves a syndicate will not be affected by the RIC legislation. He will receive a full tax deduction for the premium that he pays for year 1. Correspondingly, there will be no credit in year 2 for his successor who receives the premium. That means that those who join syndicates in year 2 will not receive an unwarranted advantage in tax terms at the expense of those who have left.

The solution for continuing members is to ensure that the credit that they receive in year 2 will always be the same as their RIC premium disallowed for year 1. The one will offset the other. That is why I told the hon. Member for Workington that there will be deductibility in one case and a taxable receipt in the other. There will be no significant effect on the yield from the RIC proposals that we put forward last year. Ninety per cent of Lloyd's members continue their syndicate membership anyway, so this issue is at the margin, although it caused a considerable degree of controversy in our debates on the Floor of the House last year.

Question put and agreed to.

Clause 58 ordered to stand part of the Bill.

Clause 59

MINOR AND CONSEQUENTIAL AMENDMENTS

Amendments made: No. 199, in page 56, line 17, leave out from "(1)" to end of line 19 and insert

"for paragraph (a) there shall be substituted—
'(a) for the assessment and collection of tax charged in accordance with section 450 (so far as not provided for by Schedule 19A);
(aa) for making, in the event of any changes in the rules or practice of Lloyd's such amendments of that Schedule as appear to the Board to be expedient having regard to those changes;';"

No. 200, in page 56, line 37, leave out from "17" to "and" in line 39 and insert

"for paragraph (a) there shall be substituted—
'(a) for the assessment and collection of tax charged in accordance with preceding provisions of this Schedule (so far as not provided for by Schedule 16A to this Act) ;
(aa) for making, in the event of any changes in the rules or practice of Lloyd's, such amendments of that Schedule as appear to the Board to be expedient having regard to those changes;';"—[*Mr. Norman Lamont.*]

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

Mr. Nicholas Brown: Very briefly, the clause deals with administrative arrangements for the assessability of Lloyd's names. The arrangements are very complex and although the full weight of the parliamentary Labour party's research facilities has been bought to bear on these matters, we have not been able to catch the Government doing anything so outrageous that we can make a fuss about it, so I shall not.

Question put and agreed to.

Clause 59, as amended, ordered to stand part of the Bill.

Clause 60

DISPOSALS OF OIL LICENCES RELATING TO UNDEVELOPED AREAS

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

Mr. Chris Smith: We come to the issue of oil licences. It might be helpful if my remarks, which are primarily directed to clause 60, also encompassed some of the aspects of clauses 61 and 62. We have no fundamental objections to those clauses, and I shall not ask my hon. Friends to divide the Committee. The clauses relate primarily to block swaps within the North sea and the tax treatment of such arrangements.

6.15 pm

Swaps have happened even under the present tax regime. The most spectacular in recent times has been in relation to block 22/11 in the North sea where Enterprise organised simultaneous swaps with Conoco, Chevron and Britoil and scooped the lot as a result. It drilled in some 280 feet of water and found one of the largest fields discovered for many years. I believe that it yielded some 175 million barrels of indicated recoverable reserves. That was good news for Enterprise and good news for the development of the North sea as a whole. The key point, however—especially in relation to these provisions—was that Enterprise was aware of the geology. It predicted the find rightly when the companies which had originally owned shares of that particular block did not and it was already close by in the south-east Forties field, so its new well was right in the heart of its existing infrastructure. The other companies did not have the same confidence, insight or ease of access to put in their wells and discover that large field.

A swap mechanism that enables expertise, knowledge of geology and insight into the conditions for potential fields to be swapped at the same time as blocks of the North sea are swapped can operate in a worthwhile manner. It has been spectacularly successful in the example that I have given. The provisions that we are discussing make the tax treatment rather lighter in such circumstances and, on the whole, that is something that we want.

The Economic Secretary to the Treasury (Mr. Peter Lilley): Clause 60 introduces a new capital gains relief for licence disposals, as the hon. Member for Islington, South and Finsbury (Mr. Smith) has said. It originates from the discussions that followed last year's Finance Bill when I said that the possibility of introducing some form of roll-over relief for gains on work programme farm-outs at the exploration phase where no cash profit was realised would be considered and discussed with the industry. We had very helpful discussions with the industry in the subsequent months which led us to introduce a clause which goes somewhat wider in three respects than the promise that I made to the House last year. In particular, we have moved from offering roll-over relief, or some form of it, to a proposal that goes further than that. Instead of simply deferring the capital gains charge payable, liability to capital gains is almost entirely removed.

The second aspect of my statement last year was that the change would be related simply to work programme farm-outs. Those are transactions where, instead of handing over cash for a share in a licence interest, the farmer-in undertakes to carry out a programme of exploration and appraisal drilling in the licence block concerned. In the ensuing discussions, however, it emerged that much the same considerations applied to swaps of one licence interest for another where both related to undeveloped acreage. Such swaps equally involve no cash profit. They are undertaken to rationalise holdings of licence interests and should likewise result in increased exploration. The removal of the capital gains relief provided by the clause has therefore been extended to licensed swaps of the kind that the hon. Member for Islington, South and Finsbury described.

The third widening of the promise is that we have moved from relating it to pure work farm-outs and pure licence swaps where no cash changes hands because we recognise that in the highly complex world of the North sea there are transactions which do not take that pure form and where there is a mix of a work programme and a monetary consideration. We have introduced arrangements whereby such hybrid cases can be coped with and the capital gains treatment related to corresponding aspects of the deal.

In all respects, the new relief provided by the clause will apply to past as well as to future disposals as a number of cases from previous years are still open. In the light of the uncertainty about their proper treatment under existing law, the clause will enable all past cases qualifying for new relief to be settled without any capital gains tax liability arising so far as the work programme or licence swap element is concerned.

I expect the element of relief provided by the clause to entail an Exchequer cost of only about £5 million a year. In so far as the relief leads to more exploration and development, as I hope that it will, costs should over time be more than recouped. I commend the clause to the Committee.

Question put and agreed to.

Clause 60 ordered to stand part of the Bill.

Clause 61

ALLOWANCE OF CERTAIN DRILLING EXPENDITURE ETC. IN DETERMINING CHARGEABLE GAINS

Mr. Lilley: I beg to move amendment No. 148, in page 59, leave out lines 3 and 4.

The Chairman: With this we may take Government amendment No. 149.

Mr. Lilley: These are technical amendments, which also arise from detailed discussions with the industry

[Mr. Lilley.]

and we hope that they meet the industry's arguments. The industry argued, and the Government agreed, that on disposal of a licence interest clause 61 should not deny a company a capital gains deduction for drilling costs relating to an undeveloped part of the licensed area simply because when the expenditure was incurred another part of the area was covered by a development consent.

The purpose of the clause is to give a capital gains deduction for certain pre-development costs of drilling. The deduction will be given only if the expenditure is on scientific research and it is available only to the extent that any scientific research alllowance given is clawed back on disposal of the licence interest. The expenditure in question qualifies as scientific research only if it is incurred before a decision is made to develop the field for commercial production. Thus the objective of the clause is met without the need for the condition that the amendment will remove—that when the expenditure was incurred the licence should relate to an area no part of which had received development consent.

In this context, drilling for oil counts as scientific research.

Amendment agreed to.

Question put and agreed to.

Clause 61, as amended, ordered to stand part of the Bill.

Clause 62

INTERPRETATION OF SECTIONS 60 AND 61

Amendment made: No. 149, in page 60, line 4, leave out "sections 60 and 61" and insert "section 60".—[*Mr. Lilley.*]

Clause 62, as amended, ordered to stand part of the Bill.

Clause 129

REDUCED OIL ALLOWANCE FOR CERTAIN SOUTHERN BASIN AND ONSHORE FIELDS

Mr. Lilley: I beg to move amendment No. 266, in page 100, line 30, leave out "100,000" and insert "125,000".

The Chairman: With this we may take the following: amendment No. 268, in page 100, line 30, leave out "100,000" and insert "150,000".

Government amendment No. 267.

Amendment No. 269, in page 100, line 32, leave out "2 million" and insert "3 million".

Mr. Lilley: My right honourable Friend the Chancellor said in his Budget speech that he would restructure the regime for Southern Basin and onshore fields developed after 1982. Our aim was to make that regime more sensitive to profitability, thus encouraging the development of marginal fields. We had accepted the argument put by the oil industry in its pre-Budget submission that royalty is a non-profit-related tax which could potentially render unprofitable marginal fields which might otherwise go ahead.

To achieve an improvement in the profit-relatedness of the south North sea oil regime, we had to abolish royalty entirely. That has to be paid for and we decided to do so by reducing the allowance against petroleum revenue tax available on each field. The effect of changing the regime in that way was to make it more likely that marginal fields would be brought forward for development and the cost of reducing the royalty generally was met by increasing the burden of tax on more profitable fields. It was no part of our objective to increase the aggregate amount of tax paid by base fields, taken as a whole. Instead, we wanted to set the petroleum revenue tax oil allowance at a level that would leave the overall tax take unchanged over the life of the fields affected by the restructuring.

On the information that was available to us before the Budget, it appeared that a petroleum revenue tax oil allowance of 100,000 tonnes was the right level to achieve revenue neutrality. The oil industry did not agree with that assessment and judged that with an oil allowance set that low overall tax paid by the Southern Basin fields would rise substantially. That was not our objective, so during the past few weeks we have consulted the industry to try to establish why it reached such a different view. Part of the difference seems to be that the industry is slightly more optimistic than the Government about future oil prices. Obviously, that will increase the prospective profitability of Southern Basin fields, so they are seen as potentially paying more petroleum revenue tax and losing more from the reduction in petroleum revenue tax oil allowance. The rest of the difference relates to technical factors such as the size of reserves for Southern Basin fields, how those reserves will be developed and the costs that will be involved. That is a difficult matter and we have held urgent and detailed discussions to analyse the industry's proposals case by case.

Those discussions have enabled us to update the information on which the original decision was based. The industry has succeeded in reducing its development costs by more than we previously allowed, so we took that into account with all the other information and the detailed figures for individual fields when we agreed that the industry's figures were better than ours. It appears that broad revenue neutrality will occur with a petroleum revenue tax oil allowance not of 100,000 tonnes—but of 125,000 tonnes. We introduced the amendment to increase the allowance to 125,000 tonnes, which will correspondingly increase the cumulative total over the lifetime of the fields to $2\frac{1}{2}$ million tonnes.

I know that the industry sought a bigger increase in the level of oil allowances proposed for Southern Basin fields, possibly to as much as 160,000 tonnes. We do not believe that that is justified on the figures that we have reached following our discussions. We carefully considered the detailed information that the industry gave and made certain revisions. Even with those

revisions. however, 125,000 tonnes seems to be the best estimate of the oil allowance necessary to achieve revenue neutrality. To go beyond that would mean reducing the total tax paid by post-1982 Southern Basin fields and I do not believe that that could be justified.

The changes that we proposed even before the amendment mean that oil companies will see an increase in their cash flow during the first years of the new regime, the gain in their cash flow being recouped out of higher petroleum revenue tax payments later in the life of the fields. That effect will be increased further by the amendment. In effect, we are benefiting their cash flow during the difficult early period while oil prices are low.

In a written answer today, my right honourable Friend the Minister of State, Department of Energy, said that he would seek to wind up the Oil and Pipelines Agency, which accepts royalty oil in kind from the oil industry on behalf of the Government. In future, we shall not receive it not in kind but in cash, and we shall receive the money four months' later. That, too, is of benefit to the cash flow of oil companies in the short term although, of course, it is no way matched field by field with the effects of this change as here we are dealing with the abolition of royalty. It will be of general benefit to the oil industry and I hope that it will improve the climate within which it operates and make it aware that we have every desire to encourage its activities in the North sea.

6.30 pm

Mr. Chris Smith: We believe that the Government are right in principle to remove the penalty of royalties and, at the same time, to provide a compensating reduction in the oil allowance which, effectively, is the threshold at which petroleum revenue tax starts to bite. The crucial question in relation to this group of amendments is whether the Government have got the figure right. After hearing the explanation given by the Economic Secretary I remain unconvinced that they have it right. The industry argued for 160,000 tonnes and it will be noted from amendments Nos. 268 and 269 that the Opposition argued for 150,000 tonnes. We accepted most although not all of the industry's case and the Government have come half way to meet us with a figure of 125,000 tonnes. I shall explain why I hope that the Government will want to reconsider their position.

There has always been an assumption that there should be a lower oil allowance for the gas fields of the Southern Basin. The reasons for that are fairly obvious; gas is cheaper to develop, generally the fields are in shallower water, platforms are lighter, cheaper to construct, generally closer to the shore and they have cheaper transport costs.

I believe that, in making their calculation for the abolition of royalties, the Government have ignored a number of crucial factors. First, there is the impact of the status of British Gas as the monopoly buyer of the product of the fields. British Gas buys strictly on a rate of return basis and, to put it bluntly, it gets gas as cheaply as possible from the producers and sells it to consumers at as expensive a figure as it can get away with. The company makes assumptions about the cost of production of the oil companies, adds on a return and that is the price at which gas has to be sold to it.

If the rate of return formula employed by British Gas for the purchase of gas continues to be used and if, and we suspect, it becomes more expensive to produce gas from most of the southern Basin fields, one of the run-on impacts of the Government's changes will be that gas supplied to the ordinary consumer is more expensive. I am sure that the Government would wish to avoid that run-on impact and I hope that they will want to consider their position.

However, there are other problems because British Gas tends to be more interested in security of supply than in the strategic, sensible development of North sea reserves. Therefore, it organises its purchases so that the break-even point for the southern Basin fields is around 400 billion cubic feet, which is a large size of field as the break-even point for potential development. That figure is crucially affected by the tax regime which the Government place upon the southern Basin. Our worry is that far from moving from that figure of viability to one below 400 billion cubic feet. That is the direction in which we hope that it will move, but we suspect that the Government's proposed change will move it to a figure which will mean that fewer reserves are exploited and developed. At present, because of that 400 billion cut-off point, any smaller potential field is not worth developing. There are many small pockets of gas in the southern field—many companies come across them in the course of larger-scale work. With a sensible planned strategy for the development of gas reserves from the southern basin, those smaller fields could be developed. But that will not happen unless the Government and British Gas between them change their minds about the pricing regime for the development companies.

The Government seem to be in two minds. On the one hand they forced British Gas to cancel the Norwegian Sleipner contract—it was right for them to do so; yet, through their tax regime and the changes which it introduces, they make it less advantageous for British companies to develop small fields.

The calculation of balance between the abolition of royalties and the level at which PRT begins to bite is difficult to make. The balance of advantage and disadvantage is bound to vary from field to field. That is where the Government's problem comes in to its fullest extent.

The one example which I have been able to discover of the Government's change being marginally beneficial is the North Ravensburn field. The operator of that field said that the new formula in the Bill—clearly it will be better with the 125,000 figure which the Government hope to introduce—triggered BGC acceptability for the field, with a 3 per cent improvement in the rate of return. However, North Ravensburn is totally unrepresentative of the southern Basin fields. Its geology is such that it is dissimilar to the majority of the other fields which are available for exploitation.

Those operators in the rest of the industry who realise that the gas reserves are there to be developed and might want to develop other fields in the southern basin feel that the Government have got the figure wrong,

[Mr. Chris Smith.]

even with the Government's welcome movement from 100,000 to 125,000. We agree. In making that balance, in assessing it field by field, we think that on the whole the industry has made a fairer assessment than the Government. We believe that the change will probably discourage rather than encourage development. This is a difficult and technical matter. It is important to get right the assessment of balance of advantage to the Exchequer and to the future development of fields, I hope—I say this in a non-partisan spirit—that the Government will think again, even given that they are making some welcome progress in the right direction.

Miss Ann Widdecombe (Maidstone): I, too, am somewhat worried by the figures which the Government eventually produced. Equally, I am concerned by the amendment tabled by the hon. Member for Islington, South and Finsbury (Mr. Smith). First, it appears to accept the oil companies' case as right. By accepting the figure of 150,000 the hon. Gentleman accepts the figure produced by the oil companies.

There is room for further exploration by the oil companies and the Government, and I hope that the Minister will assure us that the Government will reconsider various aspects of it.

Another important option to simply going up to 160,000 tonnes which has not been discussed today is the possibility of exempting already-committed fields. That was the oil companies' original position and the Government, after considering it, rejected it. I am grateful for the rise in the figures from 100,000 to 125,000 but if a difficulty arose between those figures which could not be resolved easily, perhaps the Government could reconsider the possibility of exempting committed fields. After all, companies make huge investments in those fields and work from a different set of assumptions from those which are proposed under the change.

Like the hon. Member for Islington, South and Finsbury and my hon. Friends, I accept that it makes sense to change from a non-profit sensitive tax to a profit-sensitive tax. We accept that the royalty had to go. I regret that that change was not used as an opportunity for fiscal incentives, because when the royalty was removed from the northern sector, no attempt was made to claw back and achieve fiscal neutrality. That resulted in a huge expansion in developments. The decision not to claw back was an act of faith that was extremely well repaid in terms of investment and development following that tax change.

If the oil companies are right in their estimate of 150,000 for fiscal neutrality, it follows that what the Government are now doing is producing a positive fiscal disincentive to development. The difference in calculation is crucial. My hon. Friend the Minister explained that there are differences among himself, his right honourable Friends and the companies on future price assumptions. But in that case, at least the bases on which the calculations are being made are known and can be disputed. I am sure that members of the Committee have received representations from the oil companies to the effect that they are not terribly happy with the Government's information about the assumptions on future fields and the costs and revenues appertaining to them. They feel that they would be better able to work out why the difference in arithmetic has arisen if they were given fuller information on those assumptions. I do not know whether that position is accurate. I should welcome my hon Friend the Minister's comments because that argument forms a strong part of the representations of affected companies.

If the oil companies are right and the Government have not calculated the figure accurately, there will be a fiscal disincentive. Therefore, there will be a positive disincentive to invest in the future, not least because there will be a lack of confidence in the fiscal regime. I understand that never before has there been an increase in the tax burden—which would be the result if fiscal neutrality were at 150,000 tonnes—at the same time as falling prices. If the companies cannot rely on the Government—they have always had good reason to do so in the past—to ensure that they are not fiscally disadvantaged when prices are weak, decisions will be affected, especially as several other Governments have liberalised their tax regimes on oil and gas in the past two years.

In developing future fields, companies start off with the proper information. So it is important to consider the committed fields to which I have referred. Companies invested huge sums of money in them and did so on a completely different set of assumptions. The Government should consider two matters. First, whether the oil companies have been properly informed about the field assumptions made by the Government and, secondly, whether they will re-examine the possibility of exempting committed fields.

There are disadvantages with a two-tier system. If future fields and committed fields receive different treatment, the system may seem rather untidy. But it is already a two-tier system because pre-1982 fields will have a different level of tonnage—the northern sector has 500,000 tonnes—so perhaps my hon. Friend should consider the matter.

Having said that, I shall support the amendment because it represents a considerable improvement on the 100,000 tonnes that the Government originally proposed. I do not like the idea of leaping to 150,000 tonnes without further exploration, but nor do I like the idea of writing off further exploration and saying that this is the final picture.

6.45 pm

Mr. Andrew Mitchell (Gedling): I shall speak to amendment No. 266 briefly. The hon. Member for Islington, South and Finsbury (Mr. Smith) and my hon. Friend the Member for Maidstone (Miss Widdecombe) were perhaps a little hard on my hon. Friend the Minister. After all, he has made two specific concessions. The oil industry should dub him "the listening Minister". First, he made the concession on the pressure to abolish the royalty, which could render marginally profitable fields unprofitable. Secondly, he listened carefully and, to all accounts, permitted his officials to go into considerable depth with oil companies the analysis of the way in which the figure

of 125,000 has been arrived at. Furthermore, he has stated that he wishes the measure to be fiscally neutral.

In all these circumstances we should support the amendment as evidence that the Government have taken careful note of what the industry has had to say, have listened, and have tabled an amendment which, by my calculations, means a difference of about £80 million—a substantial sum. My hon. Friend has honoured his commitment in the spirit of the Budget by bringing forward the amendment this afternoon.

Mr. Andrew Hunter (Basingstoke): I wish to put on record that I believe that the Government were correct in their original assessment of the need to advance along the lines of abolishing royalties, adjusting the allowance level and seeking to achieve neutrality in taxation. The initial proposals may have been slightly off target, but the industry should now accept the amendment. It restores that neutrality and will maintain a financial climate that will encourage further development.

Even during this year, nine new projects, valued at £1.3 billion, have been started and there is every reason to believe that the fiscal climate of the 125,000 tonnes allowance and the 2.5 million tonnes will encourage further development. With that in mind, I welcome the Government amendment.

Mr. Lilley: I am pleased that the Committee as a whole accept the broad principle of what has been done—an attempt to make the south North sea fiscal regime more profit-related and thereby encourage the development of more marginal fields.

We are now arguing only about the figures. I am impressed that members of the Committee can dispute the figures down to such a small margin of error. It took me a great deal of study to understand the enormous number of figures relating to an enormous number of fields. Inevitably, there is still uncertainty about them, but we are convinced that the figure of 125,000 tonnes will bring fiscal neutrality.

The hon. Member for Islington, South and Finsbury (Mr. Smith) argued that because, in his view, British Gas has a monopoly, or monopsony, power which it uses to ensure that oil and gas companies in the south North sea get only a fixed margin above their costs, we should be more generous. The logic of the hon. Gentleman's argument is that nothing that we do to alter the oil allowance will make the slightest difference to the incentives available to oil companies. They will be left with the same profit margin by British Gas after any changes that the Government make. If we were to reduce the tax burden, all the benefit would go to British Gas and not to the oil and gas companies.

However, the hon. Gentleman's basic presumption that British Gas has total monopsony power is incorrect. It is a powerful bargainer and uses that power in the interests of its shareholders. But that is within a regime where there is competition and alternative sources of gas and customers. The alternative sources of gas, in the long run, are from outside the North sea—so it argues against the marginal price for supplies from abroad—and within the North sea as a result of the Oil and Gas (Enterprise) Act 1982 which was introduced by my right honourable Friend the Chancellor, in his previous incarnation as the Secretary of State for Energy. That Act provides theoretical options and such options can be used in bargaining with oil and gas companies to sell their gas direct to customers on shore and use British Gas's network of pipelines to do so.

I invoke as evidence against the thesis of the hon. Member for Islington, South and Finsbury the fact that the arguments for this concession have come from the oil companies which believe that they will gain. They have not come from British Gas, as one would expect if British Gas were likely to gain from this change.

The hon. Gentleman also asserted that British Gas imposes a cut-off point of about 400 billion cu ft. I am not sure that that is correct, but if it is, the Budget proposals should reduce and not increase the damage. The proposals will give most help to smaller, less profitable fields which might be the victims of this alleged policy.

Mr. Morgan: Does the Minister accept that the first major user of the British Gas pipeline system, but selling to a market on a massive scale, will be the proposed new 1,000 MW gas power station on the lower Thames? It will have a major impact on the total market for hydrocarbon fuels subsequent to privatisation of the electricity industry, should that pass through Parliament in the next two years. If it is eventually built—planning permission has been requested from the London Docklands Development Corporation—it will impose a completely new pattern on the gas industry. The gas supplies from the southern North sea will be used for that power station, involving the pipeline system from East Anglia to London. Will that cause a new pattern of gas use and, therefore, the need for a fresh look, perhaps next year, at gas taxation and its bearing on the price of oil, gas and other sources of hydrocarbon fuels for power station use?

Mr. Lilley: I cannot give the hon. Gentleman a detailed breakdown of future supply of and demand for North sea gas. I would be ruled out of order if I were to endeavour to do so. But as the clause is designed to increase the profitability of marginal fields in the North sea—the amendment re-emphasises that intention—the potential supply of gas from the North sea will be increased and it will be easier for British Gas and the British gas industry to meet demands such as that which the hon. Gentleman mentioned may come on stream in addition to existing demand. So it is designed to push in that direction and I hope that it will do so.

The hon. Member for Islington, South and Finsbury said that Ravenspurn North is not a typical field. He is correct, but none the less management have said clearly that as a result of this package of measures in the Budget it was able to bring forward for development that quite large, though marginal, gas field in the south North sea. Most committed fields, especially committed gas fields in the south North sea, are significantly more profitable. Some of them are extremely profitable and we welcome that. This measure is particularly aimed at marginal fields which, by definition, will not be typical of all fields developed in the south North sea.

[Mr. Lilley.]

My hon. Friend the Member for Maidstone (Miss Widdecombe) suggested that we could meet the remaining concerns of oil companies by exempting committed fields from this tax. If we were to do that, we could not make the measure revenue neutral. Indeed, any attempt to do so would mean reducing the oil allowance probably to a negative level—I have not done the sums. However, it would mean foregoing any attempt to be revenue neutral if we did that.

My hon. Friend also expressed concern about the figures given to the oil industry and whether it had received sufficient information to help to achieve agreement. There has been an unprecedented degree of consultation between our officials, the officials of the United Kingdom Offshore Operators Association, and employers of the companies concerned. I am extremely grateful and pay tribute to my officials, the Inland Revenue, the Department of Energy and people in the oil industry who were involved.

We have endeavoured to make available to all companies which have asked for them, details of the assumptions on which our figures are based. By and large we received equally open access to information in return, although some companies were unable to give us all of the detailed assumptions on which their figures were calculated.

My hon. Friend said that she thought that there was a danger that we had created a disincentive in an attempt to create an incentive in the south North sea. I shall argue that, since the oil industry has argued strongly that we should do more in this respect and not suggest that any field should not go ahead as a result of this, there is no evidence of a disincentive at the level of specific fields, and potential fields. Indeed, we know one field that has gone ahead as a result of this measure.

The industry goes on to say that, nonetheless, the measure will alter the climate—its degree of happiness and security in the sense that the regime within which it will operate will be stable and desirable. I believe that once the momentum, which the lobbying effort has built up, has subsided, and the industry looks at this measure more objectively and becomes used to it, it will realise that mainfestly this Government are determined to have a regime in the North sea, north and south, which is to the mutual benefit of the oil industry and to the country.

The particular measure that I mentioned en passant in my introductory remarks will be to the benefit of the oil industry in so far as not taking royalty oil in kind any more is a small indicator of that. We are giving something for nothing. We are always happy to do so, although we rarely get so much attention when we try to make measures revenue neutral.

I am grateful to my hon. Friends the Members for Gedling (Mr. Mitchell) and for Basingstoke (Mr. Hunter) for their support for the measure and the amendment. They are right to suggest that overall the package will benefit the oil industry and the country and that it will be revenue neutral. I therefore commend the amendment to the Committee.

Mr. Chris Smith: The Minister clearly feels that the concession that he has made to the industry in the movement from 100,000 to 125,000 tonnes is sufficient to meet the industry's concerns. I fear that [redacted] remain sceptical. I know that we have to treat with caution demands from an industry which is directly affected by a fiscal regime, and the argument that immediately comes to mind when special pleading comes from the oil industry is, "They would say that, wouldn't they". Nonetheless, it is important to look at the arguments put forward by the industry. For example, when Conoco say in its letter

> "The Government's proposed amendment leaves the overall impact on industry strongly negative."

there seems to be a substantial gap between the view of the Economic Secretary and of the industry.

7 pm

The Economic Secretary was somewhat unfair to my argument in claiming that the logic of my comment about the British Gas negotiating position was that nothing that the Treasury might do would alter the viability to the producer of the southern basin field. That is not true. The problem is that the producers from the field have two dominant factors operating upon them—the policies, attitudes and negotiating stance of British Gas and the tax regime that they operate against. Their problem at present is that the 400 billion cu. ft. figure is necessitated by that joint operation of factors upon them. As we are looking to the future, to the strategic development of smaller pockets of gas within the southern basin, we have to consider ways of reducing that viability figure. I am sure that the change is welcome, although the abolition of royalty is welcome in that respect. I am not sure that the Government's proposed changes will achieve that.

The Economic Secretary has said that he believes that fiscal neutrality has been achieved by the figure that the Government are proposing. The industry clearly disagrees. I suspect that the Economic Secretary is immoveable on this issue at present, from what he said. I hope that that is not so, and that if further clear representations on a field-by-field basis are made to the Government, they will be prepared to think again. I hope in particular that if the operation of the new threshold figure—if it emerges from the Bill—turns out to have been adverse in the way in which the industry said that it is likely to be, the Government will bring forward further proposals to fine-tune the system to the benefit of further development.

Mr. Morgan: Does my hon. Friend agree that the Minister did not fully understand my earlier point? I suspect that he did not, though I say that in the nicest way possible in the new spirit of cooperation between Government and Opposition that was achieved last night in the Chamber. Now that gas as a fuel will be sold right across the board, including into the power station market, not only must the treatment of the gas industry in exploration terms be fiscally neutral, it must be gigajoules neutral as between oil and gas. Does he agree that the Government must pay more attention to the fact that gas in now becoming a normal fuel, sold

right across the board and not retained for premium purposes?

Mr. [redacted] Smith: My hon. Friend is absolutely right. That will determine how the Government, in terms of their fiscal and energy policies, look at the spread of energy production. It will also make British Gas more determined to ensure security of supply as its primary dominating motive in how it operates its purchasing procedures.

I suspect that the Government will not change on this issue immediately. I hope that they will consider carefully the impact of the proposed changes. I suspect that if they do not move we shall be here arguing about the right figure again next year. I fear that the Government's plans will, on the whole, discourage rather than encourage new development.

Amendment agreed to.

Amendment made: No. 267, in page 100, line 32, leave out "2" and insert "2.5".—[*Mr. Lilley.*]

Clause 129, as amended, ordered to stand part of the Bill.

Clause 130 ordered to stand part of the Bill.

Further consideration adjourned.—[*Mr. Lennox-Boyd.*]

Adjourned accordingly at five minutes past Seven o'clock till Tuesday 21 June at half-past Four o'clock.

THE FOLLOWING MEMBERS ATTENDED THE COMMITTEE:

Hunt, Mr. John *(Chairman)*
Arbuthnot, Mr.
Armstrong, Ms
Battle, Mr.
Boswell, Mr.
Bright, Mr.
Brooke, Mr.
Brown, Mr. Gordon
Brown, Mr. Nicholas
Butterfill, Mr.
Campbell-Savours, Mr.
Carrington, Mr.
Coombs, Mr. Anthony
Darling, Mr.
Davies, Mr. Quentin
Favell, Mr.
Forman, Mr.
Henderson, Mr.
Howarth, Mr. Gerald
Hunter, Mr.
Ingram, Mr.
Jack, Mr.
Lamont, Mr. Norman
Lennox-Boyd, Mr.
Lilley, Mr.
Major, Mr.
Maples, Mr.
Marek, Dr.
Mitchell, Mr. Andrew
Morgan, Mr.
Nicholson, Mr. David
Quin, Ms
Ross, Mr. William
Shaw, Mr. David
Smith, Mr. Andrew
Smith, Mr. Chris
Stern, Mr.
Taylor, Mr. Ian
Wallace, Mr.
Wardle, Mr. Charles
Watts, Mr.
Widdecombe, Miss

Inland Revenue

Policy Division
Somerset House

FROM : A C GRAY
16 June 1988

Financial Secretary

JOHN BUTTERFILL'S NEW CLAUSES : QUESTIONS FOR COMING MEETING

As requested at the meeting on 9 June we attach a list of questions to put to Mr Butterfill at your meeting with him next Monday.

A C GRAY

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cc. PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Culpin
Miss Peirson
Mr McIntyre
Miss C Evans
Mr Cropper
Mr Tyrie
Mr Call
Miss M Hay
Mr Painter
Mr Johns
Mr O'Connor
Mr J F Hall
Mr Davenport
Mr Yard
Mr Martin
Mr I Stewart
Mr Gray
PS/IR

NEW CLAUSE 10

A. What is the purpose behind New Clause 10?

Comment

Its effect would be to give annuitants year by year relief for interest paid by means of a further loan taken out for that purpose with the same lender. It is a new proposal; it did not figure in Mr Butterfill's earlier representations and his explanatory letter of 28 April, introducing his new clauses, is silent on this.

B. Is New Clause 10 aimed at borrowing by the annuitant or the personal representatives? If the latter, why is there any case for tax relief when the whole idea is that the rolled-up interest is paid out of the sale proceeds of the house?

C. If the former, how does New Clause 10 tie up with the whole expressed thrust of Mr Butterfill's proposals, which is to allow relief after the annuitant's death for interest rolled-up and paid at that stage?

D. [Assuming that Mr Butterfill confirms that the object is to allow annuitants year by year relief where a further loan is taken out to meet the interest]. Given the difficulty in tax principle of giving relief where the interest is not really paid off - which effectively achieves the same result as giving relief for interest on interest - would Mr Butterfill still wish to press his proposals in New Clauses 9 and 11, ie. dropping New Clause 10 completely?

OTHER MATTERS

E. Why is it considered that tax relief is crucial to the development of rolled-up interest schemes?

Comment

Mr Butterfill has alleged that, without tax relief, lenders would only lend 20 per cent of the value of the house, compared with 30 per cent with tax relief. But our figures, at current interest rates etc., indicate that a loan with a life expectancy of 10 years need only be reduced from 30 per cent to 27 per cent of the value of the house without tax relief to give the same final rolled-up debt as a loan of 30 per cent with tax relief. Thus with a £100,000 house the net annuity income is nearly doubled, from about £1,900 under existing annuity relief schemes, to about £3,750 under a rolled-up scheme without tax relief - only £400 less than the income (£4,150) under a rolled-up scheme with tax relief.

F. Does he have any hard evidence to support his contention that these proposals will help significant numbers of elderly people on low incomes?

Comment

His letter of 28 April said that he will be trying to assemble some statistics on elderly people with expensive houses but low incomes. We have been able to trace very little information on the subject; such as it is indicates that elderly people are likely to have slightly below average value houses (current average value about £45,000).

G. We accept that the cost of his proposals (without New Clause 10) will be negligible or even a small yield in discounted terms. But what precisely are the public expenditure savings which he hopes will be made?

Comment

Our analysis indicates that there will be very little public expenditure savings in terms of income related social security benefits, and that public expenditure will in fact be increased by his proposals. Many people on income support could lose out if encouraged to take up annuity schemes (see extract from Age Concern booklet attached). In addition there will be extra public expenditure as relief given to non-taxpayers like personal representatives is public expenditure not tax relief.

H. Why does he think it is justifiable to give further tax relief to Allied Dunbar-type home loan annuity schemes, compared with other schemes on the market, notably home reversion schemes?

Comment

There are advantages and disadvantages in reversionary schemes compared with annuity schemes, but no obvious reasons of policy to favour one rather than the other.

EXTRACT FROM AGE CONCERN BOOKLET

cases. For example, if Mrs Smith (see page 9) takes £2400 of her £30,000 loan as cash, this cuts her income by £40 a month.

Because of Inland Revenue regulations you can take only up to 10 per cent of the loan as a cash sum, and most companies restrict you to 7 or 8 per cent.

Your need for cash may be pressing enough to outweigh the disadvantages of a lump sum scheme – for instance, you might need to carry out urgent repairs to the house. But if you only need cash to cover these costs and don't want a regular income, there may be other ways of getting financial assistance, as outlined in Age Concern England's fact sheet No 13 **Repairing and Improving Your Home**, free on receipt of a large SAE from the Information and Policy Department.

You may also need a lump sum to repay an existing loan or mortgage. In this case the reduced income from the annuity will be compensated for, in part, by no longer having to pay interest on that loan. Alternatively, you may simply like the idea of having cash in hand, which could be an advantage if your property is worth at least £35,000 and you are a single man aged 72 or more, a single woman over 76 or a couple in their 80s.

Opting for an initial cash sum could be a disadvantage if you are claiming supplementary pension and the extra cash brings your capital to £3,000 or more and so disqualifies you from benefit. After April 1988 there will be a sliding scale of benefit for someone with capital of between £3,000 to £6,000, and these figures will also apply to people receiving housing benefit.

How are State benefits affected?

If you are receiving any welfare benefits, you must think carefully before arranging an HIP. If you receive supplementary pension, income from an HIP could mean you would lose all your benefit, which would also mean having to pay for dental treatment and glasses, and losing the right to claim lump sum payments for single items. You might also

have to pay for a home help if you have one. Likewise, you could lose any housing benefit (ie rates rebate) which you currently receive. In other words, would the income from an HIP be enough to compensate for the loss of State benefits and provide a real increase in your standard of living?

The following two examples show how a home income plan can affect supplementary pension and how carefully you must check out the position as it relates to your circumstances. It is dangerous to lay down general rules because people's situations vary so much; but an HIP is likely to be worthwhile only if it gives you extra income of at least £16 to £20 a week, and you will probably want this extra income to be at least 3 or 4 times as much as the State benefits you may lose.

People who claim housing benefit to help with the cost of their rates will be assessed only on the income received from an annuity *after* the interest has been deducted. On this basis, for every extra £1 of income, you are likely to lose 13p of housing benefit.

- *Mrs Jackson* is an 80-year-old widow, with a State pension of £39.75. She also has a supplementary pension of £4.75 a week, so that her total weekly income is £44.50. On top of this, her rates of £5.10 a week are paid by State benefit.

  Mrs Jackson's house is worth £40,000. If she took out an HIP with a loan of £30,000, her income from the scheme would be £45.50 a week. However, she would lose entitlement to supplementary pension and housing benefit. Nevertheless, with an HIP her income would be increased by £35.65 a week, and so an HIP is probably suitable for her circumstances.

- *Mrs Braddock* is only 70 years old, and lives in a house worth £30,000. Her supplementary pension is £5 a week, and her rates of £6.15 are covered by State benefit. With an HIP, she could have a loan of £22,500, which would give her a weekly income of £20.50. She would no longer be eligible for supplementary pension, and would probably have to pay about £4 a week for rates. By opting for an HIP, she would only be about £11 a week better off; bearing in mind the loan which will have to be repaid on her death, it would not be in her interests to take out an HIP.

53/2/LPD/3751/039

FROM: G R WESTHEAD
DATE: 16 June 1988

MR TREVETT - C&E

cc PS/Chancellor
PS/Chief Secretary
Mr Culpin
Mr Gilhooly
Mr Michie
PS/IR

Mr Fryett - C&E
Mr Wilmott - C&E
Mr Holloway - C&E
Mr Orr - C&E

CLAUSE 16 FINANCE (NO 2) BILL : SERIOUS MISDECLARATION PENALTY

The Economic Secretary has seen and was grateful for your minute of 9 June. As you know, he has now sent the letters to Mr Hardy, President of the Institute of Taxation and to Sir Peregrine Rhodes about the serious misdeclaration penalty. As I confirmed, by telephone, the Economic Secretary would like there to be a written arranged PQ on the day of Report Stage of the Finance Bill giving assurances about the limited application of this penalty. However, he did not wish to include any - even oblique - reference to this in his letter to Mr Hardy as he thought it not appropriate (quite rightly, on reflection!) for him to notify Mr Hardy in advance of notifying Parliament.

Guy Westhead

GUY WESTHEAD
Assistant Private Secretary

Council for the Protection of Rural England

4 Hobart Place, London SW1W 0HY
tel: 01-235 9481

17 JUN 1988

Patron: Her Majesty the Queen *President:* David Puttnam CBE
Chairman: David W Astor *Director:* Andrew Purkis

CAMPAIGN FOR THE COUNTRYSIDE
CPRE

AP/cm

16 June 1988

Rt Hon Norman Lamont MP
Financial Secretary to the Treasury
Treasury Chambers
Parliament Street
London
SW1P 3AG

FINANCIAL SECRETARY
REC. 17 JUN 1988
ACTION Mr. Elliott - IR
COPIES TO PPS; CST
Mr. Monck
Mr. Burgner
Mr. Bonney
Mr. Corlett
PS/IR

Dear Mr Lamont,

Finance Bill - Forestry

I am writing to you about an amendment to the Finance Bill on forestry management laid by Tim Boswell MP. CPRE does not support this amendment because we do not consider it can achieve what is claimed of it by its promoters.

As you will know from my letter of 18 March to the Chancellor, CPRE is very keen to see the introduction of support for environmentally sensitive woodland management. However it is CPRE's view that grants will be more effective in encouraging the sensitive management of Britain's broadleaf and ancient woodlands, than a system of tax concessions.

There are two reasons for this. Firstly, in CPRE's opinion environmental conditions are much more easily attached to direct payments than to tax concessions.

Secondly, tax concessions frequently do not reach those individuals who need help most, including the many economically-struggling farmers, whose land contains woodland. The old regime of tax concessions did little for the proper management of such woodlands, in CPRE's view.

For example, the 1983 Countryside/Dartington Institute Report ('Small Woods on Farms') which concludes:

> ' ... the small woods of England and Wales found mainly on farmland are a considerable (and to an extent) quantifiable asset which is badly used and whose value is diminishing as a result.'

In other words, because the measure proposed by the amendment would not, in CPRE's view, achieve the sensitive management of traditional woodlands, CPRE does not support it.

My office have canvassed some of the other major conservation bodies involved in the forestry debate. It appears that the CPRE attitude I have just described, is shared by the two statutory agencies, the Countryside Commission and Nature Conservancy Council, and the Royal Society for the Protection of Birds.

Hence, we have great sympathy with the aim of the amendment, but our preferred solution is annual management grants for existing traditional woodlands. We strongly urge the Government to develop that option.

Yours sincerely,

Andrew Purkis

Andrew Purkis
Director

cc PS/Chancellor
PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Sir Peter Middleton
Mr Scholar
Mr Culpin
Mr Gilhooly
Mr Michie
Mr Riley

Mr Evans
Mr Cropper
Mr Tyrie
Parliamentary Counsel
PS/Inland Revenue
Mr Houghton - IR
Mrs Smyth - IR
Mr Fawcett - IR

Treasury Chambers, Parliament Street, SW1P 3AG

G D Swaine Esq
Chairman
Taxation Committee
Confederation of British Industry
Centre Point
103 New Oxford Street
LONDON WC1A 1DU

16 June 1988

Dear Mr Swaine

Thank you for your letter of 1 June about Clause 64 of the Finance Bill (company residence). You had a meeting with the Inland Revenue before you wrote to me and I understand from the Inland Revenue that you have had a further meeting with them to discuss both the points you raised in your letter and the new clause (New Clause 31) which the Government has subsequently tabled.

2. In your letter you draw particular attention to three concerns - the lack of consultation on the clause; the impact of the clause on existing companies incorporated but not resident in the UK; and whether there is any override of the UK's double taxation agreements in the Government's proposals.

3. First, **consultation.** I would like to assure you that the Government do attach considerable importance to consultation, particularly on proposals they contemplate for the Finance Bill. Indeed we have consulted industry frequently on such proposals, in the international field most recently in relation to dual resident companies and controlled foreign companies. There was detailed consultation on company residence in the early 1980s, and the Inland Revenue Press Release of January 1981 referred specifically to the possibility of an incorporation test for company residence in the UK. The substantial points made then have been taken into account in framing the legislation, for example in rejecting an "effective management" test and in introducing a five year transitional period before companies incorporated in the UK, but not resident here under the existing rules on Budget Day, become resident under the proposed rules. The Government took the view that in the particular circumstances of these proposals it had consulted appropriately.

4. Second, **existing incorporated but non-resident companies.** You see no justification for bringing these companies into UK residence for tax purposes after the five year period provided for in the clause. The purpose of the five year period was to give time for companies to reorganise, but you say that that period would be of very limited help because of the tax and reorganisation costs and other business risks to which reorganisation might give rise in the overseas country of operation. I understand that you have discussed this matter in some detail with the Inland Revenue, who have given me a full report of your discussions. I am currently looking at this matter further, in the light of that report, and hope to say something about it in Committee - which will of course be very shortly.

5. Third, **treaty override.** You thought that there was some doubt about the proper interpretation of the clause, in the context of treaty override. I would like to take the opportunity to clarify this matter and allay that doubt.

6. Clause 64(1) sets out a rule for determining the residence of a company for the purposes of the Tax Acts. The rider that, where a different place of residence is given by any rule of law, that place is no longer to be taken into account is similarly limited. While double taxation agreements have effect in UK law by virtue of Section 788 Taxes Act 1988, those agreements are not themselves part of the Tax Acts (see the definition in Schedule 1 of the Interpretation Act 1978 as substituted by Schedule 15, paragraph 12, Finance Act 1987). While, therefore, a place of residence given by a double taxation agreement is given by "any rule of law" within the meaning of Clause 64, it is not given for the purposes of the Tax Acts.

7. The correctness of this proposition can perhaps be tested by considering the position at the present time. If a company is centrally managed and controlled in the UK, it is resident in the UK for the purposes of the Tax Acts. If at the same time it is shown to be effectively managed in another territory, and accordingly is regarded as resident in that territory for the purposes of the double taxation agreement with that territory, it does not cease to be resident in the UK for the purposes of the Tax Acts. The operation of provisions of the Tax Acts may be affected in relation to that company because of its residence for the purposes of the agreement; but it does not cease to be resident in the UK for the purposes of applying those provisions which are not so affected.

8. More generally, I think that the Government's intentions in this matter are clear, if you look at the New Clause 31 which has been tabled since your letter. This clause supplements the provisions of Clauses 99 and 100 concerning company migration: it closes a possible loophole by providing that where a company, while remaining resident in the UK under domestic law, becomes resident in another country for the purposes of a double taxation treaty on or after Budget Day, it is deemed for capital gains tax purposes to have disposed of certain of its assets immediately

before it became a resident of the other country. I think that the premise in subsection (1) of the new clause makes it clear that Clause 64(1) could not have the effect of overriding double taxation agreements.

9. I would finally like to make quite clear that the new clause itself is not intended to, and in the Government's view does not, override the provisions of our double taxation agreements either. All it seeks to do is to allow the UK to tax any unrealised gains up to the date when the company comes within the scope of the treaty "tie-breaker" provison, and becomes resident only in the other country for the purposes of the double taxation agreement. The charge to tax only applies to growth in value before the treaty comes into play; it has no effect after the treaty has come into play and cannot therefore be said to override the treaty in any way.

10. I have written at some length and in some detail about treaty override. But this is an important matter and I hope that the full explanation I have given will allay your concern in this matter.

Yours sincerely

P.P. Brooke

pp **PETER BROOKE**

(Approved by the Paymaster General and signed on his behalf in his absence from London)

Inland Revenue

Policy Division
Somerset House

FROM : A C GRAY
16 June 1988

Chief Secretary

FINANCE BILL : CLAUSE 40 : REPLY TO MR CAMPBELL-SAVOURS MP ON MORTGAGE INTEREST RELIEF ABUSE

During the debate on Clause 40 in Finance Bill Committee Mr Campbell-Savours raised a question about possible abuse of MIRAS tax relief by people buying second homes in Lake District etc. areas. You said you would ascertain what checks we carry out on relief claims and write to him. (Standing Committee A Report, 9 June, cols 347-356, attached, Chief Secretary's copy only.)

A suggested reply is attached.

A C GRAY

---

cc. PS/Chancellor
PS/Financial Secretary
Mr Culpin
Miss Hay
Mr Painter
Mr Johns
Mr O'Connor
Mr Davenport
Mr M Smith FD(W)
Mr MacDonald (T1/14)
Mr Gray
PS/IR

CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

June 1988

Dale Campbell-Savours Esq MP
House of Commons
London SW1A OAA

During the Standing Committee debate on Clause 40 of the Finance Bill on 9 June I said I would write to you about Inland Revenue checks on claims to mortgage interest relief, particularly as regards loans to buy second homes, on which you expressed concern in that debate.

Mortgage interest relief is available, up to the £30,000 limit, on loans used to buy the borrower's main residence. Relief is not available here for a second residence, regardless of whether the mortgage on the main home has already been paid off. So, as I assured you in debate, any such claims would be fraudulent.

Relief for home loans is, as you know, now overwhelmingly given under the MIRAS net payments scheme, which building societies, banks and other lenders are involved in operating. Every borrower claiming MIRAS relief has to complete a form declaring that the loan will be used to buy his main home. (For loans taken out before 6 April the relief is also available for home improvements. But, again, the improvements have to be to the main residence and not to a second home.)

The notes attached to the form give a summary of the relief rules and make it clear that it is a criminal offence to make a false declaration. Lenders too are under an obligation to report to the Revenue any instance where they have reason to believe that relief is being wrongly claimed. Extensive guidance has been and continues to be provided to lenders about MIRAS eligibility. There should then be no grounds at all for misapprehension among either borrowers or lenders about, for example, the fact that relief on a further advance - whether to buy another property or for any other purpose - is not available where the borrower has already bought his home with an earlier loan. (The Revenue will also be supplying further detailed guidance in due course to lenders about the implementation of the change to the residence basis of mortgage relief.)

To back up these instructions the Revenue undertake compliance checks on both borrowers and lenders. Borrowers' claim forms are mainly sent to a Central MIRAS Unit where samples of the various types of loans are selected for specific checks. This involves taking the matter up with the borrower direct and seeking evidence from him in support of his claim as necessary.

In addition to this, the Revenue audit officers carry out separate verification of lenders, including on the spot inspection of their systems and records, to ensure that their MIRAS relief repayment claims are correct. This involves, notably, seeing that claims for properties other than the borrower's main residence are kept out of the system.

Some fraudulent claims do occur here as no doubt in other areas of the tax system. Indeed there was quite a serious problem on home improvement loans, and Revenue checks indicate that some of these false claims, albeit a very small proportion, involved the purchase of second homes. But this year's Budget changes, by abolishing relief for new improvement loans, will remove that problem and so limit the scope for abuse in future. The Revenue remain very much alive to the possibility of abuse and keep their compliance procedures under regular review. They will of course be glad to receive any hard evidence about abuse in specific areas that can be provided.

JOHN MAJOR

Inland Revenue

Policy Division
Somerset House

FROM A C GRAY
DATE 17 JUNE 1988

FINANCIAL SECRETARY

MEETING WITH MR JOHN BUTTERFILL

You asked for a summary of the present case on Mr Butterfill's proposals. Our overall judgement is that, even without the adding complication of New Clause 10 (dealt with in points A. to D. of my note of 16 June on the questions for the coming meeting) Mr Butterfill has failed to make out his case for further special tax relief to apply to rolled-up interest home annuity loan schemes. The following summarises his arguments and our responses:

General

1. The whole justification for his proposals is that they would benefit reasonable numbers of elderly home owners with low incomes, including social security beneficiaries.

Response:

i. Because a deferred annuity scheme involves a smaller initial loan than can be offered under the existing annuity relief, existing schemes in fact provide more benefit for elderly home owners with houses up to about the national average value (£45,000). In the Budget debate he instanced a widow of 75 with a £100,000 house as the sort of person who would benefit.

cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Culpin
Miss Peirson
Mr McIntyre
Miss C Evans
Mr Tyrie
Mr Call
Miss M Hay
Mr Painter
Mr Johns
Mr O'Connor
Mr J F Hall
Mr Davenport
Mr Yard
Mr Martin
Mr I Stewart
Mr Gray
PS/IR

ii. We have no hard evidence that elderly home owners have higher than average value properties; in fact what evidence we have gathered indicates that elderly people tend to have properties of marginally less than average value.

iii. Elderly people receiving income related social security benefits will find their benefits reduced to the extent that they receive further annuity income. They are therefore unlikely to have any great incentive to take up deferred schemes.

2. Mr Butterfill indicates that tax relief on rolled-up interest paid after the annuitant's death is crucial to the development of deferred interest schemes.

Response:

Our figures indicate that to the elderly people with above average homes to whom a deferred interest scheme might be worthwhile, the addition of tax relief on simple interest payable by the annuitants does not add a great deal to the benefit which a deferred scheme, even without the tax relief, could confer.

3. Mr Butterfill says his proposals would not cost the Government anything and indeed save public expenditure.

Response:

We accept that overall there is unlikely to be any overall cost to the Government. But his proposals will involve an increase in public expenditure (tax relief given to personal representatives with little/no tax liability).

Other points

4. New Clause 10 This would appear to give annuitants year by year relief for interest paid via a further loan taken out with the same lender. Effectively the interest is not really

paid off and this achieves the same result as giving relief for interest on interest, which he has accepted would not be justifiable.

5. The current Budget has abolished relief for improvement loans and brought in other restrictions on mortgage interest relief. Against this background it is not clear that extending relief in this particular area, unconnected with house purchase, would be justifiable. Broad concern about "level playing fields" also points to caution in providing a further tax subsidy for this as against any other type of scheme to enable elderly people to release their housing equity. Ministers have had representations to this effect from providers of reversionary schemes.

A C GRAY

FP7K

FROM: D I SPARKES
DATE: 17 JUNE 1988

PS/CHIEF SECRETARY

cc Principal Private Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir Peter Middleton
Mr Scholar
Mr Culpin
Mr Odling-Smee
Mr R I G Allen
Mr Pickford
Mr Gilhooly
Mr Riley
Miss Evans
Mr Dyer
Mr Michie
Miss Hay
Mrs Burnhams
Mr Towers
Mr R Evans
Mr Cropper
Mr Tyrie
Mr Call

PS/IR
Mr Denton - IR
PS/C&E
Ms French - C&E

FINANCE BILL

... I attach details of next week's business on the Finance Bill.

D I SPARKES

FINANCE (No 2) BILL BRIEFING
STANDING COMMITTEE (10th DAY): TUESDAY 21 JUNE
STANDING COMMITTEE (11th DAY): THURSDAY 23 JUNE

The following clauses are due to be taken:

Clause 63 and Schedule 6: Forestry
(Financial Secretary)

This clause and schedule reform the tax treatment of commercial woodlands and thus end a widely-criticised tax shelter. Occupiers of commercial woodlands could get tax relief for planting and other expenses but were effectively exempt on sale proceeds. In future, commercial woodlands will be removed from the scope of income and corporation tax altogether. There are transitional provisions extending for five years for existing occupiers of woodlands. In addition, the overall level of Exchequer support for forestry will be maintained by means of higher planting grants. This shift in emphasis from support using grants rather than tax reliefs will enable environmental objectives to be realised more effectively.

Clause 64: Test of company residence
(Paymaster General)

This clause introduces a new test of company residence for tax purposes; a company incorporated in the UK will be regarded as resident here. This is a straightforward and objective test which brings UK practice into line with most international practice. There are transitional provisions to avoid overnight changes in residence status that might otherwise take place. Companies not incorporated in the UK will continue to be regarded as resident here if their central management and control is situated in the UK.

Clause 99: Company migration
(Paymaster General)

This clause provides that if a company migrates (ie becomes non-resident) it will normally have to pay tax on any unrealised

capital gains on those assets which do not remain within the UK tax net. If companies were able to migrate at will and realise capital gains after doing so, such gains would not in many cases be taxed at all, either in the UK or elsewhere. This reform allows the repeal of the present requirement that a company obtain the Treasury's consent before migrating.

Clause 100: Deferral of tax on migration
(Paymaster General)

This clause provides that when a subsidiary of a resident company migrates it may in certain circumstances defer the tax charge to the extent that it relates to foreign assets of a foreign trade. Special treatment is appropriate for assets associated with an overseas trade.

Clause 122: Arrangements prior to migration
(Paymaster General)

This clause sets out the conditions that must be satisfied by a company wishing to migrate. It must notify the Inland Revenue of its intentions and make suitable arrangements to ensure payment of UK tax up to the time of migration.

Clause 123: Penalties for failure to comply
(Paymaster General)

This clause provides for penalties for failure to comply with clause 122. In some cases, persons other than the migrating company may be liable for the penalties.

Clause 124: Tax unpaid by a migrating company
(Paymaster General)

This clause permits the Inland Revenue recourse to various other parties where a company which has migrated fails to pay the tax it owes.

Clause 65: Employees' priority share applications
(Financial Secretary)

This clause ensures that the benefit derived from entitlement to a priority share application by virtue of one's employment will not in general be treated as a taxable benefit-in-kind. The Inland Revenue have not in the past regarded such a benefit as taxable; this clause clarifies the position.

Clause 66: Loans to take up share options
(Financial Secretary)

This clause allows holders of share options under approved schemes to borrow to exercise those options without losing tax relief. The clause removes an unintended effect of existing legislation.

Clause 67: Payroll giving scheme
(Paymaster General)

This clause doubles the limit on tax-relieved contributions under the payroll giving scheme to £240 a year. This meets representations for a higher limit made by some charities.

Clause 68: Entertaining overseas customers
(Financial Secretary)

This clause disallows as a business expense for tax purposes the cost of entertaining overseas customers. This brings the treatment of such expenditure into line with that of entertainment expenditure generally. Special reliefs of this sort are no longer justified now that rates of income and corporation tax have been reduced to sensible levels.

Clause 69: Exemption and top-slicing for redundancy payments
(Financial Secretary)

This clause increases the tax-free limit for redundancy and certain other lump-sum payments from £25,000 to £30,000 and abolishes top-slicing relief for lump sums which exceed this limit. The reform

is a simplification and removes a relief that is unnecessary now that tax rates have been reduced to sensible levels.

Clause 70: Top-slicing for lease premiums
(Financial Secretary)

This clause withdraws the complex top-slicing arrangements for tax charged on premiums for leases and certain other payments. The relief was designed to mitigate the effect of penal marginal income tax rates and is no longer necessary.

Clause 71: Definition of a recognised clearing system
(Financial Secretary)

This clause amends for tax deduction purposes the definition of a recognised clearing system to include those systems handling only foreign securities. It brings into line the tax treatment of overseas securities held in overseas and UK recognised systems and affects only the mechanism and timing of the existing liability to UK tax. It should enable a clearing system handling international transactions in securities to be set up in this country.

Clauses 72 to 84: Unapproved employee share schemes
(Financial Secretary)

These clauses introduce major changes to the present wide-ranging anti-avoidance provisions for employee shares acquired outside an approved scheme. These provisions are aimed at preventing employees avoiding income tax by receiving remuneration in the form of artifically-engineered capital gains on shares. In most cases the present charge to income tax on the capital appreciation of such shares will be replaced by a more narrowly targetted charge that will arise only if manipulation of share values actually occurs. The changes, which apply from 26 October 1987, when draft clauses for consultation were published, should help in particular those companies that cannot or do not choose to provide shares to employees under one of the approved share schemes.

Clause 85: Industrial buildings allowance
(Chief Secretary)

This clause corrects a defect in the rules for calculating industrial buildings allowance which could result in excessive relief being allowed when a person acquires a building for industrial use from someone outside the UK tax net.

Clause 86: Elections under capital allowance provisions
(Chief Secretary)

This clause introduces a two-year time limit (the usual standard) for making an election under the capital allowance rules which relate to sales of assets between persons who are connected for tax purposes.

Clause 87: Capital allowance succession provisions
(Chief Secretary)

This clause corrects defects in the special rules for calculating capital allowances when a person succeeds to a trade previously carried on by a person with whom he is connected for tax purposes. It also introduces a two-year time limit for making an election under these rules.

Clause 88: Capital allowances for safety at sports grounds
(Financial Secretary)

This clause amends the capital allowance provisions for safety expenditure at sports grounds to reflect recent changes to the safety legislation. The clause allows the existing capital allowances to continue in force and to apply rather more widely than before.

Clause 89: Capital allowances for quarantine premises
(Financial Secretary)

This clause withdraws the special capital allowance for expenditure at pre-1972 quarantine premises which was introduced specifically to assist people running such premises to comply with new Government standards. The abolition of this allowance places all quarantine

premises on the same footing for tax purposes and aligns their tax treatment with that of commercial buildings generally.

Clause 90: Capital allowances for assured tenancies
(Financial Secretary)

This clause provides transitional arrangements to deal with the potential consequences of the Housing Bill for the existing system of capital allowances for property let on assured tenancy terms. These allowances are to be replaced by a BES-style relief, which the Government believes will be a more effective means of increasing the supply of rented accommodation. This clause ensures that capital allowances for existing assured tenancies continue and that allowances for construction expenditure on land already acquired for these purposes remain available until 1992.

Clause 92: Alignment of capital gains and income tax rates
(Chief Secretary)

This clause provides for the capital gains of individuals to be charged at the rates that would apply if they were the top slice of taxable income, and for those of most trusts to be taxed at the basic rate. This important reform, which has been facilitated by the reductions in the basic and higher rates of income tax, will substantially reduce the distortions and tax planning that result from taxing income and capital gains at different rates.

Clause 93: Capital gains of married couples
(Financial Secretary)

This clause adapts the rules for computing the gains of married couples to take account of the new CGT rates. A couple's aggregate gains will be taxed at the rates that would apply if they were the marginal slice of the husband's income, with a single annual exemption between them. The clause applies only for 1988-89 and 1989-90; from the introduction of independent taxation in April 1990, married couples will be taxed separately on their gains under the provisions of clause 98.

Clause 94: Capital gains of accumulation and discretionary trusts
(Financial Secretary)

This clause charges the gains of accumulation and discretionary settlements at a rate equivalent to the sum of the basic and additional rates of income tax (ie 25 per cent plus 10 per cent in 1988-89), the same combined rate as applies to their income. This is consequential upon clause 92, which aligns the tax rates on the gains of individuals and trusts (other than those covered by this clause) with those on their income.

Clause 95: Capital gains of Lloyd's underwriters
(Financial Secretary)

This clause adapts the capital gains provisions for Lloyd's underwriters to take account of the new CGT rates.

Clause 96: Capital gains in special cases
(Financial Secretary)

This clause contains detailed rules for determining the CGT rate in certain special circumstances. It preserves the benefit of top-slicing relief for certain life policies so as not to prejudice the outcome of the current review of life assurance taxation.

Clause 97: Start-date for capital gains aggregation
(Financial Secretary)

This clause provides that clauses 92 to 96, which in general mean that capital gains will in future be taxed as the top slice of income, take effect for disposals on or after 6 April 1988.

Clause 101: Capital gains annual exempt amount
(Financial Secretary)

This clause sets the CGT annual exempt amount for 1988-89 at £5,000 for individuals (compared to £6,600 in 1987-88). Normally, the exempt amount is revalorised annually but this year it is being reduced in recognition of the fact that gains have been rebased to

1982, thereby taking all purely "inflationary" gains out of tax. Moreover, with capital gains now being taxed at the same rates as income, it is logical to reduce CGT exempt amount somewhat, though a separate exempt amount is still required for administrative reasons. Under existing law the exempt amount for most trusts is automatically half that for individuals, and will therefore be £2,500 in 1988-89.

Clause 102: Capital gains retirement relief
(Financial Secretary)

This clause extends capital gains retirement relief, which applies to the disposal on retirement of a business owned for at least ten years. At present the first £125,000 of any gain is tax free; this clause exempts in addition half any gain between £125,000 and £500,000. It is a further indication of the Government's desire to foster small businesses.

Clause 103: Capital gains on homes of dependent relatives
(Financial Secretary)

This clause abolishes the CGT exemption for a home provided rent-free for a dependent relative, except for existing cases. It ties in with the abolition of the dependent relative allowance and of mortgage interest relief on properties provided for dependent relatives. The provisions are anachronistic, dating back to days when social circumstances and welfare provision were very different.

Clause 104: Capital gains rollover relief
(Financial Secretary)

This clause extends rollover relief to milk and potato quotas, and to satellites and spacecraft. Rollover relief, which is already available for a wide class of business assets, enables the tax charge on a capital gain to be deferred where the proceeds from the sale of an asset are simply reinvested in the purchase of a replacement. It is important that tax law keeps pace with technological and other changes.

Clause 105: Capital gains indexation allowance and building society shares
(Economic Secretary)

This clause ensures that when money is withdrawn from a building society share account (which is technically an asset chargeable to CGT), no CGT indexation allowance shall be given. Otherwise a loss could be created for tax purposes, which would be anomalous.

Clause 106 and Schedule 8: Capital gains indexation allowance and intra-group lending
(Financial Secretary)

This clause and schedule counter exploitation of the capital gains indexation allowance to create large artifical losses by arranging intra-group lending in particular legal forms.

Clause 107: Capital gains on intra-group share exchanges
(Financial Secretary)

This clause reverses a recent Court decision to ensure that reorganisations involving share exchanges between companies in the same group do not result in capital gains being charged, or capital losses being allowed, more than once.

Clause 108: Losses on personal equity plans
(Financial Secretary)

This clause enables the Treasury to make regulations to ensure that, as always intended, a disposal of an investment in a personal equity plan should not create an allowable loss for capital gains tax purposes. The intention in general is that PEPs should be right outside the usual rules for capital gains and losses. This clause simply clarifies that position. The change is being effected by the issue of regulations rather than by primary legislation because the original PEPs legislation is contained in regulations.

Clause 109: Definition of investment trust
(Financial Secretary)

This clause simply restores a part of the definition of an investment trust that was inadvertently repealed by the Finance (No 2) Act 1987.

Clause 110: Capital gains indexation provisions
(Financial Secretary)

This clause makes certain technical amendments to the capital gains indexation provisions which are necessary as a consequence of rebasing gains to 1982.

Clause 111: Schedule D in-year assessments
(Financial Secretary)

This clause ensures that the Inland Revenue has statutory authority for its longstanding practice of making in-year estimated income tax assessments for certain types of income. Doubt had been cast on the strict legality of this practice which ensures timely payment of tax.

Clauses 112 to 114: Notifying liability to tax
(Economic Secretary)

These clauses clarify the taxpayer's obligation to notify the Revenue of chargeability to tax and update the penalties for failure to do so. They implement, in modified form, recommendations of the Keith Committee. Clause 112 relates to income tax, clause 113 to corporation tax and clause 114 to capital gains tax.

Clause 115: Time limit for information sought
(Economic Secretary)

This clause prevents the Inland Revenue going back more than three years when they seek information from a third party about certain types of income received by a client (eg in obtaining returns of interest payments from a bank). It implements a recommendation of the Keith Committee.

Clauses 116 and 117: Powers to call for information
(Economic Secretary)

These clauses affect the Inland Revenue's powers to call for certain specified types of information from third parties. Clause 116 extends the list of persons to include Government departments and other public bodies; clause 117 extends the types of information to include grants and subsidies paid from public funds. The clauses implement, in a modified form, recommendations of the Keith Committee and help ensure that taxpayers pay the correct amounts of tax.

Clause 118: Information about unnamed taxpayers
(Economic Secretary)

This clause extends the Inland Revenue's powers to require a third party to provide access to documents relating to a person's tax affairs. It allows, subject to certain safeguards, the powers to be used where the true identity of taxpayer(s) under enquiry is not known and it will thus assist the detection and deterrence of tax evasion. In particular, it will enable the Revenue to discover the identity of taxpayers using a tax avoidance scheme which has been shown to be legally ineffective. The clause also brings the Department of National Savings within the scope of the Revenue's information powers, thus putting it on the same footing as the high street banks. These extensions to the Revenue's powers were recommended by the Keith Committee.

Clause 119: Information held on computer
(Economic Secretary)

This clause extends the Inland Revenue's information powers to allow it the same access to records held on computers as it is allowed to records held on paper. It implements a recommendation of the Keith Committee.

Clause 120: Interest on delayed PAYE payments
(Economic Secretary)

This clause paves the way for regulations allowing an employer to be charged interest on overdue PAYE and for interest to be paid by the Inland Revenue on overpaid PAYE repaid late to employers. These provisions, which implement a recommendation of the Keith Committee, will not come into force before 1992.

Clause 121: Limit on penalties for tax offences
(Economic Secretary)

This clause limits the total penalties that can be charged where two or more tax-geared penalties are due in respect of the same tax. It provides that the total penalty cannot exceed the largest of the penalties due. The clause simply clarifies existing practice.

Clause 125: Appeals procedure in Northern Ireland
(Paymaster General)

This clause extends to Northern Ireland the system by which General Commissioners of Income Tax (lay tribunals) hear appeals on tax matters. For historical reasons there are at present no General Commissioners in Northern Ireland and appeals are heard by the Special Commissioners, the full time tax specialists, instead. This reform, which will be brought into operation at a date to be fixed by the Lord Chancellor, will provide taxpayers with quicker access to an independent tribunal.

Clause 126: Time limit for cases stated in Northern Ireland
(Paymaster General)

This clause removes the current restrictive time limit for Commissioners in Northern Ireland to provide a stated case (ie a reasoned judgement) for the opinion of the Court of Appeal and instead provides that cases should be stated as soon as reasonably possible. It thus allows the parties involved more time to prepare a stated case and brings practice in Northern Ireland into line with practice in Great Britain.

FORTHCOMING BUSINESS

Standing Committee (12th day) Tuesday 28 June
Standing Committee (13th day) Wednesday 29 June
Standing Committee (14th day) Thursday 30 June

Clauses will continue to be taken in broadly numerical order, new clauses being taken on the last two days. Report stage will probably commence on Wednesday 13 July and continue the following day.

FP Division
17 June 1988

CONFIDENTIAL

FROM: T U BURGNER
DATE: 17 JUNE 1988

FINANCIAL SECRETARY

cc PPS
Mr Monck
Mr Scholar
Mr Bonney
Mr Donovan
Mr Cropper
Mr Elliott IR

FORESTRY: FINANCE BILL - BRIEFING

As requested at your meeting this morning, I attach:

(i) Briefing notes, prepared by Mr Donovan, dealing with the criticisms by the Labour Party of the Budget forestry package;

(ii) A speaking note to put the criticism about maintenance in the context of the package as a whole, and to suggest that if adjustment is needed in the future this is best done by the grants rather than the tax route. (The note is cleared with the Forestry Commission).

You also asked for a note setting out the figures of the grant regime and the Farm Woodlands Scheme. This was handed over by the Inland Revenue at the end of your meeting but I attach a further copy for convenience.

Mr Donovan will be one of the team in the officials box on Tuesday to deal with non-tax points on forestry.

TB

T U BURGNER

1. **Woodland Grant Scheme too generous for conifers**

Increases in percentage rates of grants for conifers were higher than for broadleaves. But what matters in assessing the effects of the new grants is not the percentage change but the total support before and after the tax and grant changes for different sorts of planting and for people in different tax positions.

Grants will now be worth the same for everyone, regardless of their tax position. In general the old top rate taxpayer will get rather less than before; people who paid no tax or tax at low rates will get more than before.

The lowest grant, now £615 a hectare, is for large scale conifer plantations; the highest grant, now £1575 a hectare, is for a small scale plantation of pure broadleaves. The grants for pure broadleaves under the previous scheme were already raising the share of broadleaved trees in total planting. But nearly half of broadleaved trees are planted in mixed woodland, for good silvicultural reasons. In future broadleaves in mixed plantations will receive grants at the rate previously available only for a pure broadleaf plantation; as a result this category will receive the largest increase, equivalent to between £505 and £685 a hectare.

In addition the incentive to plant on better quality land (defined as arable or improved grassland) is being increased by a new supplement of £200 a hectare on top of the other grants.

The changes in Government support for forestry when taken together amount to a real shift in emphasis which we believe will help ensure that the right trees are planted in the right places.

2. **Transitional relief could cost Exchequer £28 million a year for next five years**

Not clear how estimate arrived at but appears to be based on estimated cost of tax relief, before Budget, applied to planting on 235,000 hectares. Too high since area of planting which could benefit under transitional arrangements substantially below 235,000 hectares and tax rates reduced in Budget.

cannot estimate precisely the effects of changes on tax revenue or public expenditure since landowners will need to reassess their position before deciding whether to continue under previous arrangements during transitional period or switch to new Woodland Grant Scheme. But estimates of increase in expenditure of £4 million in 1988-89 rising to £8 million in 1991-92, offset by increases in tax revenue, published in FSBR took account of all relevant factors, including area for which clearance for planting had already been given.

3. **Planting will take place on 235,000 hectares cleared for planting before the Budget**

Estimate of 235,000 hectares cleared for planting before Budget incorrect (although understandable). Relates to gross area of land where approval given: this includes existing woodlands to be felled and restocked, areas of unplantable land (mountain tops and lakes) and areas which cannot be planted for environmental or landscape reasons (stream borders, wildlife habitats). Total also includes areas where, due to change of ownership, more than one application for grant aid has been made.

Area available for new afforestration where clearance was given before the Budget is approximately 100,000 hectares. Approval for grant aid is valid for five years and, typically, planting is spread over that period. So if owners do plant, this will contribute to achieving Government's stated aim of 33,000 hectares of planting a year.

4. **Government support for forestry will lead to permanent damage to the Flow Country.**

The Secretary of State for Scotland is responsible for policy on land use in the Flow Country. He announced on 26 January (OR Vol 126 cols 71-73) that the Government accepts that much of the Flow Country is of national and international importance for conservation. In the Government's view the only satisfactory approach to protecting this area is by notification of Sites of Special Scientific Interest and the Nature Conservancy Council has

been invited to consider what further areas should be designated. In addition the Highland Regional Council is preparing a land use strategy for the area.

There is therefore no question of forest planting in the Flow Country being approved without full regard to the conservation case.

5. **Transitional period too long**

Approvals for grant aid given by the Forestry Commission are valid for five years. This was adopted because experience showed that woodland owners needed this period if work was to be planned and managed properly. Planting after approval is, typically spread over this period. A transitional period of less than five years would therefore have left the Government open to charges of breach of faith.

CONFIDENTIAL

FINANCE BILL - FORESTRY
MAINTENANCE COSTS - SPEAKING NOTE

A number of hon. Friends have argued strongly in support of amendments to set off maintenance costs against other agriculture income. I hope I have said enough to show that perpetuating tax reliefs in this way would quite undermine the balanced nature of the Government's proposals for forestry. The package as a whole is generous and the new higher rate of grants reflect maintenance costs in the early years. The Budget through the reduction in tax rates has left woodland owners considerably better off and it is not unreasonable to expect them to employ part of this to maintain and enhance woodlands in their ownership. It is very much in their own interests to do so.

The change to the arrangements for forestry support is a major step to remove an anomalous tax shelter which was widely criticised and to replace it with a grant system which can be better targeted to meet the Government's objectives for forestry and the environment, including a better balance between broadleaves and conifers. We now need to see how those already in the industry and new investors respond to the grant package. The scale of the changes together with the transitional arrangements means that it will inevitably be sometime before those effects are apparent. But I can assure you that my rt. hon Friends will be watching the position closely and will no doubt want to review the grant structure in due course. Any effects on the maintenance of mature woodlands can be taken into account at that time.

MAIN FEATURES OF THE FORESTRY AND WOODLAND GRANT SCHEMES

1. Ministers may like to be aware of some background figures on the different grant schemes. Detailed comment on the grant system and forestry is the responsibility of the Minister of Agriculture Fisheries and Food. The rates for Northern Ireland vary slightly.

OLD SYSTEM

2. The pre-Budget Day grant system under the Forestry Grant Scheme allows for payments of:

Area of Wood (hectares)	Conifers (per hectare)	Broadleaves (per hectare)
0.25 to 0.9	£630	£890
1.0 to 2.9	£505	£735
3.0 to 9.9	£420	£630
10 and over	£240	£470

NEW GRANTS

3. The post-Budget Day revised planting grants under the Woodland Grant Scheme are:

Area approved for planting or regeneration (hectares)	Rates of grant	
	Conifers £ per hectare	Broadleaves £ per hectare
Area band 0.25-0.9	1,005	1,575
1.0-2.9	880	1,375
3.0-9.9	795	1,175
10 and over	615	975

These rates of grant are generally £375 per hectare higher than under the previous forestry grant and broadleaved woodland grant schemes, but the increase for broadleaved trees planted or regenerated in mixed woodlands will be substantially larger.

For new planting on existing arable or improved grassland of less than 10 years of age which is undertaken outside the farm woodland scheme, there will be a supplement of £200 per hectare.

Both old and new style grants for new planting are paid in three instalments, 70 per cent on completion of planting and further instalments of 20 per cent and 10 per cent at five yearly intervals thereafter, subject to satisfactory establishment and maintenance. The rules for regeneration are more complicated with instalments of 50 per cemt, 30 per cent and 20 per cent but no fixed time limits.

FARM WOODLAND SCHEME

4. Planting grants under the farm woodland scheme are a combination of old system grants for conifers and the new rates for broadleaves, they are:

(a) Hectares	Conifers £ per hectare	Broadleaves and mixed £ per hectare
Area band 0.25-0.9	630	1,575
1.0-2.9	505	1,375
3.0-9.9	420	1,175
10-40	240	975

In addition farmers are paid an annual payment in lieu of farming income foregone which is taxable as farming income in the same way as the income it replaces. The rates vary according to the land categories planted:

Severely disadvantaged areas (also known as less favoured areas)	£100 per hectare
Disadvantaged areas	£150 per hectare
Elsewhere (mainly lowlands)	£190 per hectare
Unimproved grasslands (severely disadvantaged and disadvantaged)	£30 per hectare

(b) These payments are made annually for differing periods as follows:

40 years for pure oak and beech

30 years for other broadleaves and mixed woodlands of which more than half is broadleaved

20 years for mixed woodland with a lower proportion of broadleaves.

10 years for coppice.

I attach as an alternative summary a photocopy of an article from Big Farm Weekly.

Storm Damage Supplementary Grants

It was announced on 7 June 1988 that a supplement to normal planting grants was to be made in respect of restocking of woodlands damaged by the storm in October 1987.

The supplement will be £150 per hectare for conifers and £400 per hectare for broadleaves.

It is available in addition to old or new style grants and for planting already made.

Finding out the facts on forestry

THE new grant schemes available to farmers who plant trees have proved complicated to say the least. *BFW*, MAFF and the NFU have put their heads together to explain the system.

FARM WOODLANDS SCHEME

- Provices, for the first time, an annual income while woods are growing.
- Three year scheme with planting target of 36,000 hectares and annual target of 12,000ha.
- Eligible land is arable and improved pasture (ploughed and reseeded within the last 10 years).
- 3,000ha of the 36,000ha target reserved for planting unimproved pasture is in the Less Favoured Areas.
- Minimum area to be planted per holding is 3ha; maximum limit 40ha per holding. Each wood must extend to at least 1ha.
- Applications are likely to be made jointly to the Forestry Commission for approval of planting grant and agriculture departments for approval of annual payments
- Annual payments commence one year after first instalment of planting grants. They will be taxed as farm income.
- Payments will be made at the rates shown in Table A.
- Annual payments will be made for 10 years for coppice, 20 years for pure conifers; 20 years for mixed woods with more than 50 per cent conifers; 30 years for pure broadleaves (except oak and beech); 30 years for mixed woods with more than 50 per cent broadleaves; 40 years for pure oak and beech.
- The FWS is available to owner-occupiers, tenants (with landowner's consent), farming companies and partnerships where farming is the main occupat on.
- The scheme should be operational from October 1 this year. For precise eligibility, check with MAFF divisional offices.

Table A

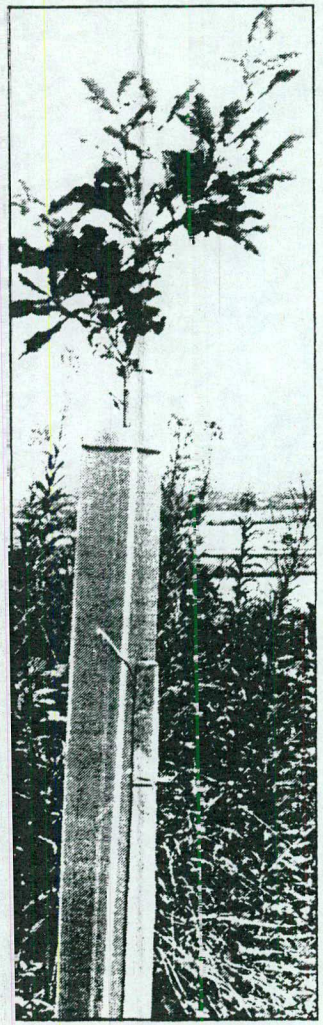
Arable and improved grasslands	Severely Disadvantaged Areas	– £100/ha
	Disadvantaged Areas	– £150/ha
	Other	– £190/ha
Unimproved grasslands	Severely Disadvantaged Areas and Disadvantaged Areas	– £30/ha

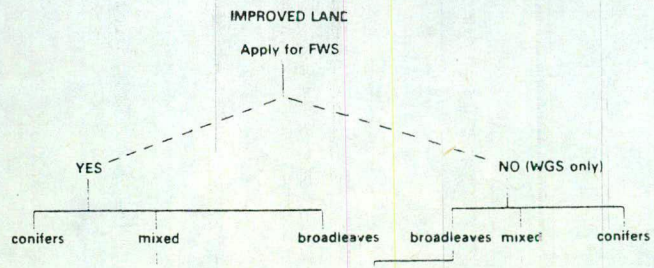
Table B

Area approved for planting	Conifers (FWS rate) £ per ha	Conifers (Non-FWS) £ per ha	Broadleaves £ per ha
0.25 – 0.90	630	1,005	1,575
1.00 – 2.90	505	880	1,375
3.00 – 9.90	420	795	1,175
10 and over	240	615	975

WOODLAND GRANT SCHEME

- Replaces previous Broadleaved Woodland Grant Scheme and Forestry Grant Scheme following removal of commercial forestry from income tax provisions. Although grants will not be taxed, no facility for offsetting costs against other taxable income exists.
- Planting grants for conifers where the applicant enters the Farm Woodland Scheme are those previously paid under the Forestry Grant Scheme (see rate in Table B).
- These rates apply for woodlands planted with mixtures of conifers *and* broadleaves as well as for woodlands planted with conifers *or* broadleaves.
- In addition to the above grants, anyone planting arable or improved grassland who does *not* enter the FWS will receive a supplement of £200 per hectare planted.
- Planting grants will be paid in 3 instalments: 70 per cent on completion of planting; 20 per cent and 10 per cent at five yearly intervals thereafter.





There's nothing weedy about Gramonol Five.

21 JUN 1988

FRESHFIELDS

H S K Peppiatt
P C Peddie
D O Bates
D A Redfern
G A Whalley
J K Grieves
J M H Hunter
R J C Shuttleworth
J K McCall
R W Harris
W N Parker
P M Leonard
J C Nowell-Smith
J C T Foster
N D Tarling
M L H Clode
M M MacCabe
P W Goodwin

R M Nelson
J P L Davis
I L Hewitt
T A Ling
P R Macklin
Penelope Freer
G B Nicholson
F G Sandison
G L B Darlington
A M V Salz
I M Fisher
Josanne Rickard
R A Chamberlin
D C ap Simon
T W R Head
W N Richards
I Taylor
P J R Bloxham

R M Ballard
J L McKeand
D N Spearing
J N Byrne
M Thompson
A S McWhirter
S A D Hall
G W Morton
B J O'Brien
V R Clempson
E T H Evans
G N Prentice
I K Terry
K N Dierden
J E Francis
P Bowden
L G D Marr
A P Richards

B W Staveley
A Littlejohns
C W Rough
G Le Pard
S M Revell
T A Moore
Rachel Brandenburger
J A H Lawden
S L Hoyle
J P A Goddard
Ailsa Urwin
J G Davies
Vanessa Knapp
C L A July

Resident in New York
J Part
P J Jeffcote
D C Bonsall

Resident in Paris
A C L Smith
R S McCormick
S J McGairl

Resident in Singapore
K J Julian

Resident in Hong Kong
M A Freeman
H W J Stubbs
Ruth Markland

Walden House,
17-24 Cathedral Place
London EC4M 7JA
Telephone 01-606 6677
Telex 263396
Fax 01-329 6022 LDE/CDE No.23

Our reference PWG/LT02

Your reference 42/2.BTW.4375/02

20th June, 1988.

Dear Norman,

Finance Bill - Clause 94

Many thanks for your letter of 13th June and for your comments. It is naturally disappointing that the issue is unlikely to be sorted out this year but I do accept that it is certainly a complex area.

Yours ever,

P V t W

Peter Goodwin

FINANCIAL SECRETARY	
REC.	21 JUN 1988
ACTION	Mr. Cayley IR
COPIES TO	PPS, CST
	Mrs. Lomax
	Mr. Culpin
	Mr. Cropper

PS: I was sorry to read your note that your mother had been in hospital; I do hope she is making a good recovery. Mr. Tyrie PS/IR

Rt. Hon. Norman Lamont, Esq., P.C., M.P.,
Treasury Chambers,
Parliament Street,
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THE INSTITUTE OF TAXATION

12 UPPER BELGRAVE STREET LONDON SW1X 8BB 01-235 9381

Secretary Ronald J Ison LLB FTII Solicitor

PMP

Please reply to: 19 Cobham Road,
Leatherhead,
Surrey.
KT22 9AU

20 June 1988

FOR QUICK ADVICE PLEASE

ECONOMIC SECRETARY 21/6
REC'D 21 JUN 1988
ACTION MR TREVETT
COPIES TO PS/CHX PS/CST
MR CULPIN
MR BOLTON MR MCMICHAEL
B/R PS/IR
MR JEFFERSON-SMITH

Peter Lilley Esq. M.P.,
Economic Secretary to the Treasury,
Treasury Chambers,
Parliament Street,
London SW1P 3AG.

Dear Mr. Lilley,

Finance (No. 2) Bill 1988

Thank you for your letter of 14 June which is some comfort to us and we express our appreciation of the assurance in the last paragraph of your letter.

In view of the importance to our members of this matter would you have any objection if I published my letter to you of 2 June and your reply of 14 June. My intention would be that it would appear in "Taxation Practitioner" our Institute monthly magazine but of course it would then be available for copying.

Yours sincerely,

(J.W. Hardy)
President

42/2/4366/006/MDG

FROM: MISS S J FEEST
DATE: 20 June 1988

MR H B THOMPSON - IR

cc: PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Mr Scholar
Mr Culpin
Miss Sinclair
Mr Cropper
Mr Jenkins (Parliamentary Counsel)
Mr P J Davies(Parliamentary Counsel

FINANCE (NO 2) BILL - SCHEDULE 8 INDEXATION AND GROUPS

The Financial Secretary was grateful for your submissions of 6 June 1988 and 15 June 1988.

2. He is content to table both these amendments for Report Stage.

Susan Feest

SUSAN FEEST

42/2/4375/086/MDG

FROM: MISS S J FEEST
DATE: 20 June 1988

MR MICHAEL - IR

cc: PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Culpin
Miss Sinclair
Mr Cropper
Mr Jenkins - (OPC)

FINANCE BILL: CGT REBASING

The Financial Secretary was grateful for your minute of 14 June 1988 and approves the suggested amendments.

2. He would be grateful for a draft letter to send to Gordon Brown advising him of the amendments and the reasons for making them.

Susan Feest

SUSAN FEEST

53/2/LPD/3754/003

ECONOMIC SECRETARY
DATE: 20 June 1988

CHIEF SECRETARY

cc Chancellor
Financial Secretary
Paymaster General
Mr Michie
Mr Tyrie

Mr Brown - C&E
PS/C&E

SEARCH OF PERSON : FINANCE BILL CLAUSE 10

We have spoken about a possible "mini-concession" for Report stage. We were a little concerned by suggestions in the Committee debate that many passengers were unaware of their appeal rights, particularly those whose command of English was poor.

2. I have discussed with Customs officials the possibility of providing some form of notice of appeal rights, whether in English or in foreign languages. I am satisfied that it would be both inconvenient and unnecessary to require Customs to provide each suspect with a multi-language written notice of appeal rights. Nor would it even be desirable to show such a written notice to all suspects since this bureaucratic process can chill the atmosphere.

3. Customs intend to have a poster-notice pinned up in search rooms detailing (in English) the appeal rights that will already have been orally advised to the passenger. This will act as a visual reminder of their rights to suspects before and during search.

4. In cases where passengers do not speak English, Customs either speak in the passenger's own language (they have special language allowances in payment at many ports and airports designed to reward staff with linguistic aptitude), or find an interpreter. It would be quite rare for a passenger to get through the initial questioning and examination of baggage without having understood what was going on.

5. However, I think there is a case for having the appeal rights available in a variety of languages, to show to those who do not appear to have a clear grasp of the situation, so that they can read their rights in their own language. To this end, I have agreed with Customs that they will have the appeal rights translated into 17 commonly-encountered languages and distributed to points of entry. This can be done at very modest cost and no inconvenience, (unlike the alternative proposal of providing all passengers with a written notification of appeal rights). This will be an administrative procedure and will not require amendment to the Finance Bill.

6. I hope you will agree that this is a satisfactory compromise and that if we come under pressure again at Report stage it will be useful to show that we have taken the Opposition's comments seriously.

7. I think that a concession along these lines will demonstrate our willingness to respond to the points made in Committee. I hope you agree.

PETER LILLEY

4366/11

MR FRASER - IR

FROM: MISS S J FEEST
DATE: 20 June 1988

cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Mr Scholar
Mrs Case
Mr Revolta
Ms Sinclair
Mr A R Williams
Mr Cropper
Mr Tyrie
Mr Call
PS/IR

NEW CLAUSE: SEFARERS' TAXATION

The Financial Secretary was grateful for your minute of 17 June 1988 and approves the brief provided.

Susan Feest

SUSAN FEEST
Assistant Private Secretary

MORTGAGE ACTION LTD

1/3 THE DRIVE HOVE EAST SUSSEX BN3 3JE

Telephone (0273) 820030 Fax (0273) 23293

Our Ref: IME/AL

Your Ref:

Norman Lamont
Financial Secretary to the Treasury
HOUSE OF COMMONS
LONDON
SW1A 0AA

29 JUN 1988

FINANCIAL SECRETARY
29 JUN 1988
ACTION Mr. B. O'Connor IR
COPIES TO PPS, PMG
Miss Peirson Mr Culpin,
MB Lomax Mr Cropper,
Mr Tyrie, Mr Call,
Mr Johns IR, PS/IR

20 June 1988

Dear Sir

Finance Bill - Tax Relief on Home Annuity Schemes

We write to place on record our support for the proposals which would extend Tax Relief to those Home Annuity Schemes which provide for rolled-up interest.

This is clearly going to help a lot of elderly people with their savings or capital locked up in their home.

We have recently been advised by the Inland Revenue that a Scheme which we have been working on for Crusader Insurance PLC does not qualify for Tax Relief for the elderly. The proposed amendments from Mr John Butterfill MP, will give considerable help to elderly people looking for assistance in this way and we urge you to support the proposed amendments.

Yours faithfully

I M Ellis
Director

ACTION
BUTTERFILL LIST

002/3291

FROM: JILL RUTTER
DATE: 21 June 1988

PS/FINANCIAL SECRETARY

cc:
Principal Private Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Mr Culpin
Mr Gilhooly
Ms Evans
Mr Denton - IR
Ms French - C & E

Mr Jenkins - OPS
Mr Lennox-Boyd MP

NEW CLAUSES

I attach a tenative division of new clauses. We will not obviously know the selection of non-government new clauses until next week.

I would be grateful for any comments you or other Ministers may have on this allocation which is still provisional.

JILL RUTTER
Private Secretary

NEW GOVERNMENT CLAUSES

Already Tabled

NC 29 **VAT on Spectacles etc** [EST]

The new clause gives effect to a ruling of the ECJ that goods supplied by medical and allied professions may be exempted from VAT only if they are minor and indissociable from the services of medical ease. Its main effect will be to apply VAT at the standard rate to spectacles, contact lenses and hearing aids.

NC 31 Deemed disposal of assets on company ceasing to be liable to UK tax [PMG]

The new clause is a necessary complement to Clause 99. It imposes a similar charge on unrealised gains when a company takes its assets out of the scope of the UK tax system, not by migration but by becoming resident in anothers country for double taxation treaty purposes.

NC 32 **Consideration for certain restrictive undertakings** [FST]

The new clause removes the present favourable tax treatment of payments to employees under restrictive covenants entered into with their employers. In future, such payments will be treated as if they form part of ordinary pay and payments will be deductable in the calculation of the employer's taxable profits. It will apply to covenants entered into on or after 9 June.

NC 33 **Post Consolidation Amendments** [FST]

The new clause corrects errors in the Income and Corporation Taxes Act 1988. Some of the errors derive from pre-consolidation amendments made by the Finance Act 1987. There will also be a new schedule of amendments.

34 **Jurisdiction of General Commissioners** [PMG]

The new clause allows taxpayers to agree with their tax offices that appeals and other proceedings will be brought before General Commissioners other than those indicated by the Taxes Management Act. Follows consultation procedures.

NC 36 **Gains arising from certain settled property** [FST]

To prevent avoidance of higher rate CGT by non-discretionary Trusts through the use of settlements in which the settlor or his spouse has an interest.

Non-Government New clauses already tabled

1 * *	Profit-related pay	Beith/Wallace	PMG
NC 2 * *	Mortgage interest relief	Beith/Wallace	CST
NC 3	Independent taxation of pensions	Beith/Wallace	FST
NC 4	Definition of a covenanted payment to charity	Beith/Wallace	FST
NC 5	Bad debt relief	Sir W Clark	EST
NC 6	Relief for expenditure on eligible securities	Beith/Wallace/Kennedy	FST
NC 7	Accession Tax	Beith/Wallace/Kennedy	FST
NC 8	Small scale Bingo	Watts and 13 others	EST
NC 9	Relief for interest paid by personal reps	Butterfill and 8 others	FST
NC 10	Additional loans to pay loan interest	Butterfill and 8 others	"
NC 11	MIRAS on 9 and 10 above	Butterfill and 8 others	"
NC 12	VAT gaming machines	Watts and 12 others	EST
NC 13	Benefits in Kind threshold 1988/89	Sir W Clark/Sir M Fox	PMG
NC 14	Amendment of Sch 23 ICTA 1988	Sir W Clark/Sir M Fox	FST
NC 15	Amendment of S 393 ICTA 1988	Butterfill/Riddick	FST
NC 16	First year allowances for ships	Sir W Clark	FST
NC 17	Replacement of a ship (roll over relief)	Sir W Clark	FST
[NC 18	Earnings from work done abroad	Sir W Clark	FST]
NC 19	Relief for technical education and development	Sir W Clark/Beaumont Dark	FST
NC 20 * *	VAT zero rating	J Smith and 5 others	EST
NC 21	Corporation tax deductions	J Smith and 5 others	CST
NC 22 * *	Anti avoidance	J Smith and 5 others	FST
NC 23 * ^	Total reliefs (No 1) [£10,000]	J Smith and 5 others	CST
NC 24 * *	Total reliefs (No 2) [£20,000]	J Smith and 5 others	"
NC 25 * *	Total reliefs (No 3) [£30,000]	J Smith and 5 others	"
NC 26 * *	Restriction on reliefs [basic rate]	J Smith and 5 others	"
NC 27 * *	NHS lottery	Barnes	FST
NC 28	Removal of obstacles to employee ownership	I Taylor and 5 others	FST
NC 30	Tax relief on company cars *	Shersby	PMG
NC 35	Woodlands (amendments to Inheritance Act 1984)	Arbuthnot/Boswell/Hurst	FST
NC 37	Share options	Sir W Clark	FST

replaced by Govt. new clause

* considered in SC 9 June

** Mr Jenkins told me there would probably be out of order

PS/Chancellor

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Standing Committee A

FINANCE (NO. 2) BILL

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

Tenth Sitting
Tuesday 21 June 1988
[*Part I*]

CONTENTS

CLAUSE 63 agreed to.
SCHEDULE 6, as amended, under consideration.

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Standing Committee A

Tuesday 21 June 1988

[*Part I*]

[MR. JOHN HUNT *in the Chair.*]

Finance (No. 2) Bill

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

Clause 63

COMMERCIAL WOODLANDS

4.30 pm

The Chairman: Hon. Members will see that in my provisional selection of amendments under clause 64, amendment No. 319 is in square brackets because at the time of selection there was some doubt about it. I have decided to select it.

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

Mr. Chris Smith (Islington, South and Finsbury): Perhaps, Mr. Hunt, I can crave your indulgence before discussing clause stand part to inform the Committee that my hon. Friend the Member for Edinburgh, Central (Mr. Darling) is unable, sadly, to be with us today, but for a happy reason: he has just become a father.

[*Hon. Members: "Hear, hear."*]

My hon. Friends are arranging to send a telegram of congratulations, at least from Opposition Members. Clause 63 implements schedule 6 of the Bill. We greatly welcome the Chancellor's step in the Budget to remove the tax relief advantages from forestry. The planting of forestry and the claiming of tax relief for it, and in many cases the use of schedule D in the early stages of the life of a plantation, and switching later to schedule B and the passing on of ownership of woodland, was plainly a tax abuse, and many of us have argued for some years that it should be abolished. It had adverse environmental consequences and we felt that it ought to be scrapped. We are delighted that the Chancellor has done that.

On schedule 6, we shall voice our deep concern about the transitional arrangements that the Bill will set in place. We do not think that the Chancellor has gone anything like far enough in the schedule. The principle of the abolition of tax relief is warmly welcomed and we are happy for clause 63 to stand part of the Bill.

Mr. Tim Boswell (Daventry): It might help if I commented on clause stand part and confined other remarks to the amendments as they arise. It is appropriate now to raise general issues.

I agree with the hon. Member for Islington, South and Finsbury (Mr. Smith) in his general approach to the philosophy of the Government's changes. I have no wish, nor have my hon. Friends, to restore the old tax regime by a back door through later amendments to the schedule. I detect relatively little enthusiasm for that reversion among landowners and responsible land-owning bodies.

Before drafting the amendments we consulted a dozen such bodies. They are broadly in line in their approach to these issues and we tried to confine them to the limited number of matters that we regard as salient and critical.

Perhaps I should comment in passing, as on other issues that of course the Government's sweeping, radical and desirable reductions in the top tax rate have by themselves reduced the tax shelter. One could say that the Government have once again comprehensively shot, if not a dead at least a moribund fox, by proceeding against forestry. The case for their changes stands alone and needs to be established separately.

I have always felt that schedule B, a clear, special schedule for trees, is a flimsy base for a flourishing forestry industry. I want to widen that base, and not just to those who hit the headlines such as pop stars who buy ready-made or to-be-planted forests. Many landowners—often without making much money out of it, as I shall mention later—have quietly carried out traditional forestry on their estates. But forestry should now be brought further down the hill—perhaps even further out of Scotland and more into England and Wales—and the base of the forestry industry should be broadened. It is no longer an activity, if I may so put it, for consenting adults in private.

There is also a national interest in ensuring that the planting effort is maintained. It would be inapposite for this Committee to have a primarily agricultural/silvicultural discussion, but the Government have set ambitious—perhaps over-ambitious—planting targets of 33,000 hectares per year. It is relevant that those targets have recently been increased because of the circumstances created by the reduction in pressure for agricultural production as a result of food surpluses in Europe and world wide. Nevertheless, the target exists and it is important to approximate some way towards it.

It would not be helpful for this Committee to debate at length the balance between conifers and broad-leaves or other detailed and distinctly forestry issues, but it would be unfair to the Committee if I did not put on record the advice given to me that there has been no record of land being bought by forestry management companies since my right honourable Friend the Chancellor of the Exchequer announced his Budget. Evidence suggests that 26,000 hectares were planted in 1987, which is three-quarters of the target, but it seems that only about 4,000 or 5,000 hectares may be planted this year. I freely accept that that is an adjustment factor which, for the reasons that I mentioned earlier, may later redress itself. Nevertheless, it is a matter for concern and one that Ministers may wish to monitor carefully.

As for the general points appropriate to the clause stand part debate, I draw the Committee's attention,

[Mr. Boswell.]

first, to the long growing cycle for trees. The hon. Member for Edinburgh, Central (Mr. Darling) cannot be here today, but let us suppose that he plants a tree for his son or daughter. I did not hear which it was, but I congratulate the hon. Gentleman on doing better than me—I have only daughters—

[*Interruption.*]

I did not intend to inflame the Committee—I am very fond of my daughters, but I do not have a mixed brood. Let us suppose that the hon. Gentleman plants a tree for his son or daughter today—that would be an interesting thing to do in the middle of May—and continues to water it. There would be no possibility of his offspring, of whatever sex, living to benefit from the produce of that tree unless it were culled for thinning. A broad-leaved tree would not come to maturity for 120 years and arguably a coniferous tree might take 45 or 50 years even in a favourable location. At present, forestry and trees cannot be treated as short-rotation crop. Even in New Zealand, which I recently visited, the very best Radiata pine takes 28 years to turn around.

These issues are relevant to new clause 35—if you see fit to call it later, Mr. Hunt—which relates to inheritance tax, so I shall not dwell on them today, but it is important to remember that forestry cannot be an in-and-out exercise. Merely removing the income tax regime does not, ipso facto, remove all taxation. It is difficult to avoid inheritance tax considerations in forestry matters.

Secondly, forests are often—though not always—occupied together with other types of land. It is interesting that the main thrust of the European Community's forestry action programme for the 1990s, which is to operate from January next year, is geared towards an integration of forestry with farming—a fruitful practice often seen in Scandinavian and central European countries. It applies to two particular areas. The first is farm forestry and the second is estate forestry of the more traditional kind. There are both administrative and practical problems in separating them, as well as issues of policy as to whether we want to draw a firm distinction or set up a Chinese wall between them.

My third point is directly relevant to the clause rather than to the schedule. In a sense, much forestry is uneconomic and we need to probe the Government as to what a "commercial woodland" is. The burden of argument in the past has been that the only reason why people planted trees was the favourable tax regime if they were high taxpayers. If that was really so, we may find that there are very few commercial woodlands available. We shall then have to consider whether it is a matter of public policy to have no trees planted at all.

To classify some woodlands, or the target woodlands, as economic or commercial, as the clause does for the first time, is to point up an issue that has long lain decently dormant. If trees were occupied together with other land enterprises, in the past their produce could be taxed as income on receipt of the produce of those trees however long it took for them to be felled and fall into profits. Estate owners who have long had trees may suddenly find themselves faced with the kind of blinding revelation that Committee Members will remember in Le Bourgeois Gentilhomme, when Monsieur Jourdain discovered in mid-life—possibly as a mid-life crisis—that he had been speaking prose all his life. These chaps must decide whether they have been growing commercial trees or non-commercial trees all their lives. That may well be a difficult decision for them and for the Revenue in assessing them.

What on earth will happen if someone suddenly discovers, after a lifetime in forestry, that all of his enterprise is non-commercial? Much flows from that, but this is the most immediate part of what I wanted to raise. If one has a non-commercial woodland, in principle no maintenance or continuing expenditure of any kind on that woodland will be allowed, not just from the end of the transitional period but from Budget day. More to the point, no interest will be allowable on any loans that have been taken out in consideration of that woodland, or partially so.

There is also a question mark over capital allowances in relation to previous capital expenditure, which may or may not be split between various enterprises. The landowner will have to decide what to do about that, how to present his accounts and what he can make plausible or acceptable to the Revenue. Looking ahead to inheritance tax problems, he will have to decide—notwithstanding the fact that the clause sweeps away the separate assessment of forestry income for income tax—whether he has to keep a separate shadow set of accounts so that in due course he can define a business asset and a separate business enterprise so as to claim business asset relief on a transfer.

Those are significant issues. In summarising them, my general approach to the clause and to the schedule is that, unlike the Opposition, I accept that a five-year transitional period is broadly right. I do not seek in any sense to extend that period or to shorten it. I believe that it will be essential to tune up the new system, the philosophy of which is established, and to get the details right. That will require a good deal of further thought by my right honourable Friend the Minister and his colleagues and a degree of further consultation not only with landowners but with conservation interests and others who rightfully wish to join in these arguments to achieve the right solution, particularly in relation to sensitive aspects such as broad-leaved trees. I hope that we shall have an opportunity to discuss those further.

4.45 pm

Sitting suspended for a Division in the House.

5 pm

On resuming—

Mr. Boswell: I was about to draw my remarks to a close, but the enforced interruption gave me an opportunity to reflect on what I had said earlier. I will share with the Committee the fact that I insisted that each of my daughters had a tree planted for her more or less on her birthday, which happened to come at

convenient times of year. If any of them wants to be a professional forester in due course, I shall be more than pleased, although I should not expect her to be particularly well remunerated.

Ms Joyce Quin (Gateshead, East): Would the hon. Gentleman like to inform the Committee whether the tree planted was a conifer or a broadleaf?

Mr. Boswell: That is an interesting question. The answer is a lilac. It probably had something to do with the need to make a demonstration of the matter. It was purely an amenity point. That was a most helpful intervention, if I may say so.

To summarise the first point that I made, we are anxious that the five-year period should be used constructively to tune up the new system and to consult and refine it, so that we get the results that we all want—a flourishing forestry industry much less monolithic than it was, with a better balance between conifers and broadleaves and between uplands and lowlands, and a wider spread of ownership and involvement. Those are positive factors on which I hope that my right honourable Friend will build.

The second matter on which I ask my right honourable Friend the Minister to comment is the difficult question of whether woodlands are commercial. I am still worried about what is to be classified as a commercial woodland and, conversely, what is a non-commercial woodland. If it is within the power of the landowner to designate woodlands as commercial, the problem is largely met, but it would have to be understood that not all woodlands, especially the traditional ones, would yield a positive cash return, because they were there for other purposes.

The basis of "no costs in, no tax out" is acceptable, but I am worried about what may happen where money has been borrowed under the previous regime and in years to come a zealous inspector says, "Of course, this was never a commercial enterprise, so we have decided to strike out that proportion of your costs or your loans which have been attributed to it and you will have tax to pay". There could be some nasty shocks in the future. The Revenue cannot simply turn a Nelson's eye to the problem and hope that it does not arise.

Ms Quin: I should like to make a few general remarks, although I realise that the more detailed arguments will come up in the debate on the amendments.

I was pleased that the Chancellor of the Exchequer introduced the clause into the Bill. I should like to think that the weight of the arguments advanced in my early-day motion caused him to introduce the measure, but it would be presumptuous of me to do so. I am glad that more than 100 of my hon. Friend's supported that motion and I congratulate those of my hon. Friends who in the weeks before the Budget drew attention to the misuse of the tax concessions. I also congratulate all the organisations, especially the wildlife organisations, the Royal Society for the Protection of Birds and the Countryside Commission, which produced many articles and documents showing the damage being done by the use of those tax concessions, which had existed for a considerable time and were being used on a wide scale. Even small-scale investors were being urged by many journals to plant a forest with the taxman's help, and there were many startling examples of whole tracts of countryside, especially in northern Scotland but also elsewhere throughout the United Kingdom, being exploited as a result of those fiscal privileges. Outside investors ruined whole areas of countryside which they had possibly never even visited and to which they owed no particular loyalty. The damage done to those areas was considerable, as was the unfavourable reaction of local residents.

The hon. Member for Daventry (Mr. Boswell) said that this Committee was not the place for a general forestry-agricultural debate, and I share that view, although I feel that the hon. Gentleman is perhaps keener than I am on the encouragement of forestry, especially the coniferous variety. My favourite walking territory—the Northumberland moorlands—has been disfigured by ugly, geometrical slabs of monochrome conifers, which have had the highly undesirable effect of acidifying the soil, destroying wildlife habitats and driving away tourists. Countryside which depends on distant, open moorland views is certainly not enhanced by irregular or regular slabs of conifers planted at intervals.

I am pleased that this measure was introduced in the Budget, but there are still some matters for concern, especially in view of the contradictory statements made by other Departments since the Budget measures were announced. It seems as though there will be an end to large-scale coniferous plantations in the English uplands, but the same cannot be said for Scotland and Wales. I live quite close to the Cheviot hills, and I wonder whether one side of those hills will be free of conifers while the other side will be one unvarying plantation. The statements of the Minister of Agriculture, Fisheries and Food and the Secretary of State for Scotland need to be reconciled. I hope that that will be done in favour of environmental and other interests, not purely on a timber-growing basis. For many reasons which we do not have time to go into today, such an approach is rather one-sided and unhelpful for our countryside.

I know that many specific matters will come up when we debate the relevant amendments, but I felt that I would like to make a few general comments at this stage.

The Financial Secretary to the Treasury (Mr. Norman Lamont): Perhaps I may reply very briefly as we shall be debating the key issues when we come to the specific amendments.

I am grateful to the hon. Members for Islington, South and Finsbury (Mr. Smith) and for Gateshead, East (Ms Quin) for making it clear that they welcome the broad thrust of what has been proposed, even if they have reservations about the transitional period, which we shall be debating shortly. I agree with the hon. Member for Gateshead, East about environmental effects. I was in Sutherland two weeks ago. It is one of the most beautiful parts of the country but, alas, some of it has been severely damaged by pyjama-top forestry on the hills.

Mr. Andrew Hunter (Basingstoke): I wish to make a

[Mr. Hunter.]

small point on the environmental front. One environmentally positive factor is that the conifer is deterring the grey squirrel and allowing the red squirrel to reappear in many parts of the country where it had been absent for some years.

Mr. Lamont: That may be so, and any reappearance of the red squirrel is to be welcomed, but if I outlined to my hon. Friend the effect of tall conifers on the approach flight-line of the black-throated diver into the lochs of Sutherland, he would realise that conifers can have an adverse effect on other important and rare parts of our wildlife. We certainly do not want the nesting sites of divers—there are few enough of them—to be destroyed.

Mr. Tony Worthington (Clydebank and Milngavie): Does the Minister agree that the effect of conifers is to darken everything so much that it does not matter whether there are grey squirrels or red squirrels because it is impossible to see either?

Mr. Lamont: I am not sure that that is entirely true. I can disclose that on my way to Sutherland I visited the admittedly very ancient coniferous forests around Aviemore and the Spey where it was reported to me that red squirrels were to be seen, so visibility must have been reasonably good despite the conifers.

Mr. Chris Smith *rose—*

Mr. Lamont: I hope that members of the Committee will allow me to get on, as progress would be a good thing.

My hon. Friend the Member for Daventry (Mr. Boswell) made other points about the importance of forestry as an industry. We recognise its importance to the paper and board industry, and we have planting targets which have not yet been achieved. It remains the Government's intention that the industry should flourish. By taking forestry out of the tax system and making grants the method of support in future, the amount of support from the Government is broadly the same but the position may be different for each individual forester. There will be winners and losers under the proposal, but people's motives for planting trees will not just be tax driven. Furthermore, the grant system will give more control to the Forestry Commission and it will be possible to give greater consideration to environmental matters. My hon. Friend was concerned that there might already be evidence of a fall-off in planting since the Budget. I accept that woodland owners will need time to reassess the position after the Budget change, but large areas of land exist where approval for grant was given before the Budget and owners would have been aiming to plant there later this year, so it is too early to reach any firm conclusions in that respect.

My hon. Friend also made some remarks about the distinction between commercial and amenity woodlands. I should like to reflect on what he said, but I am not sure that there is a great problem. Non-commercial woodlands—amenity woodlands—have been out of the tax system for the last 25 years. At least, that is the theory—and that is how it should have operated in practice. If it has not operated that way in practice, that may be another matter into which I should not enquire too closely. From now on, there should be a closer alignment between amenity and commercial forestry in respect of tax. It is up to the individual to apply for the grant that is available for forestry purposes. Whether he is in it professionally or is not seeking to make a profit is a matter of fact. I shall consider what my hon. Friend has said, but I assure him that although we wish to correct the environmental abuses and to end the tax-driven system, we recognise the importance of the industry.

Question put and agreed to.

Clause 63 ordered to stand part of the Bill.

Schedule 6

COMMERCIAL WOODLANDS

Mr. James Arbuthnot (Wanstead and Woodford): I beg to move amendment No. 248, in page 132, line 28, leave out "of a trade".

The Chairman: With this we may take amendment No. 249, in page 132, line 29, after "under" insert—"Schedule A or".

5.15 pm

Mr. Arbuthnot: In his Budget speech, my right honourable Friend the Chancellor of the Exchequer said that receipts from the sale of trees or felled timber would not longer be liable to tax. A press release issued on Budget day stated:

"Commercial woodlands will be wholly removed from the scope of income tax and corporation tax."

Commercial lands were taxed under schedule B, a charge that the Bill abolishes. This means that, because of the abolition, in theory a charge could arise instead under schedule D, case 1, as

"profits or gains or losses of a trade".

Previously, this was prevented by the very existence of schedule B because the schedules are exclusive of each other. Paragraph 3(2) of schedule 6 therefore states that

"profits or gains or losses . . . from commercial woodlands shall not be regarded for any purposes as profits or gains or losses of a trade chargeable under Schedule D".

My concern is that the abolition of that possible charge—of a trade under schedule D, case 1—might mean that a charge could then arise under schedule D, case 6, which is a case which charges any annual profits or gains not falling under any other case of schedule D or under schedules A, B, C or E. Schedule D, case 6 is rather tough because it allows no relief for losses, for example, and I do not think that that was intended. Amendment No. 248 seeks to correct that.

Amendment No. 249 covers the same sort of problem but relates to schedule A. Section 6 of the Income and Corporation Taxes Act 1970 charges to tax various items including

"receipts arising to a person from, or by virtue of, his ownership of an estate or interest in or right over such"

land. That could include commercial woodlands, which clearly my right honourable Friend did not intend.

Mr. Lamont: As my hon. Friend the Member for Wanstead and Woodford (Mr. Arbuthnot) said, the purpose of amendment No. 248 is to put in belt and braces to ensure that there is no possibility of tax being charged on commercial woodlands after the proposals in schedule 6 have taken effect under case 6 of schedule D. Such a charge was never intended as we propose to remove woodlands from tax altogether. I agree that it is right to make that point clear beyond doubt, and I am happy to accept my hon. Friend's amendment.

Amendment No. 249 covers the same sort of point but relates to schedule A. I assure him that there will be no question of the Inland Revenue seeking to charge tax under schedule A in respect of a person's occupation of commercial woodlands. There are no grounds for that fear, but I will consider the matter and if I think that it is necessary to amend the provision I will come back to it on Report.

Mr. Arbuthnot: On the basis of that assurance, which I accept fully, I shall not press amendment No. 249.

Amendment agreed to.

Mr. Lamont: I beg to move amendment No. 298, in Schedule 6, page 133, line 30, leave out

"Subject to sub-paragraph (4) below".

The Chairman: With this it will be convenient to take Government amendments Nos. 299 to 317.

Mr. Lamont: The amendments have two functions. They ensure that the transitional rules for tax relief for the next five years will apply in Northern Ireland as they do in the rest of the United Kingdom. They also clarify the way in which the transitional arrangements will work when a woodland occupier who has elected to continue to be assessed under schedule D, and thus to receive tax relief during the transitional period, receives a grant under the woodlands grant scheme in respect of all or part of his woodlands.

The woodlands grant scheme grants, which will be the only form of Government support for forestry after the transitional period, have been set at a level which takes into account the removal of relief, so it would be nonsense for anyone to receive both tax relief and woodlands grant scheme grants during the transitional period. The potential overlap between tax relief and grants is not adequately catered for in the Bill. The amendments import more precise rules which provide that tax relief will cease for the first full chargeable period for which a grant is made, and that in the chargeable period in which the grant is made—that is, where it is made for part and not the whole period—only those expenses not covered by the grant will qualify for tax relief. So an occupier whose woodland has suffered storm damage will be able to clear the damage with the benefit of tax relief and then replant with the help of the woodland grant scheme.

The amendments cater for another aspect which may interest the Committee—the possibility, particularly when there is storm damage, that an occupier may wish to clear and replant his woodland in sections, instead of doing all the clearing first and then all the replanting. It will now be possible for him to elect to treat a section which has already been replanted as a separate estate, so he will lose tax relief only in relation to that section and will continue to receive relief for any clearance that he carries out on the rest of the estate. It will thus be possible for people clearing up after a storm to obtain tax relief on a part of the estate. That possibility was recommended to us after the storms that swept the south of England, and I am sure that the Committee will agree that it is a good idea.

Mr. D. N. Campbell-Savours (Workington): Is that all that people in Kent will get, bearing in mind all the representations that they made following the substantial storm damage that they suffered on 16 October? Will there be no more than this minor tax concession? What about all their other requests for help?

Mr. Lamont: Here we are dealing with a specific point. Supplements to the grants for storm damage have already been announced. People can receive tax relief, or grants at the pre-Budget level, or the new grants plus no tax relief. Whether they choose the old grants or the new grants, they will receive supplements to them for storm damage, but that is not what we are dealing with here.

Mr. Chris Smith: As the Minister pointed out, this large group of amendments seems to carry out two basic objections. The first is to extend the provisions to Northern Ireland, which is logical and we would not oppose it. The second, however, is of greater detail and effect. The amendments clarify the procedures whereby a woodland owner can opt to remain under the present tax relief system for the first period of the transitional arrangements and then move to the new woodland grant scheme at some stage during the transitional period. The amendments seek to tidy up and lay down the procedures to be followed.

As I shall make clear when we debate amendment No. 272, we have strenuous objections to the existence of the transitional arrangements, but as the Government seem intent on having a transitional period it seems logical to specify clearly how qualification for tax relief and woodland grant scheme support are to be kept distinct, and also to ensure that there can be no double claiming of both relief and new grant. It seems sensible to write that into the transitional period given that the period exists, so we shall not oppose the Government on the amendments.

I suspect that my hon. Friend the Member for Workington (Mr. Campbell-Savours) may wish to pursue the issue of those in areas such as Kent which suffered considerably from storm damage last October,

[Mr. Chris Smith.]

because the Government are not giving them enough assistance. However, that is a tangential point, and we do not oppose the amendment.

Mr. Campbell-Savours: I am a bit surprised because I thought that something more substantial, such as a statement, would be forthcoming from the Minister today about the storm damage that occurred in Kent on 16 October. Several documents have been drawn to my attention about representations that were made by many organisations to Ministers. Hon. Members representing Kent may wish to intervene to correct me. The hon. Member for Maidstone (Miss Widdecombe) may be able to inform the Committee about the activities of the Forest Windblow Action Group which was set up immediately after the storm. It comprised the Forestry Commission, the Timber Growers UK, the British Timber Merchants Association and the UK Word Processors Association. The action group made representations to the Government about harvesting, marketing, restoration work and the likely financial implications of the storm damage. I was led to believe, perhaps mistakenly that a major statement would be made in Committee today which would outline the Government's proposals to resolve the difficulties that have arisen in that part of the world.

The thanks of many timber growers in Kent will go to Timber Growers UK and all its regional secretaries who also made representations to the Government. Prior to Christmas the Forest Windblow Action Group and its various associated advisory groups prepared a detailed assessment of damage to woodlands in the south-east of England and identified market opportunities. Those details were reported to the Government through the Forestry Commission and the group now advises woodland owners. That was stimulated by seminars held in the affected areas at the end of January.

Perhaps the hon. Member for Maidstone can update my information, because there may have been developments since it was drawn to my attention. If she cannot, I presume that the information is precisely the same today as it was then.

The Chairman: Perhaps the Chair can intervene; I am waiting for the hon. Member to relate his remarks to the amendment before the Committee.

5.30 pm

Mr. Campbell-Savours: I was led to believe that tax relief would alleviate the problems confronted by many timber growers in that part of the country. In the south of England 4 million cubic metres of timber was blown down—about 15 million trees. That is a lot of wood! With the exception of one or two constituencies the south of England is represented by Tory Members of Parliament, so one would have thought that with that much timber lost, they would want to make representations on the problems confronted by timber growers in the south of England and, in particular, in Kent.

Several towns have been indentified in correspondence to me. They string along the south coast and all are in Conservative constituen[redacted]. That has been the subject of much comment in the p[redacted]ss and on television in the south, and public meetings have been convened. Yet there is silence in today's proceedings, which should provide an opportunity for discussion.

Limited time is available to harvest certain species of timber before they begin to degrade. I am not a specialist on wood, but I am told that degrading means that the wood becomes stained. As such, it is no longer fit for the markets for which it would normally be destined.

The Chairman: Order. The debate is on tax relief. We cannot have a general debate on the problems caused to forestry by the hurricane.

Mr. Campbell-Savours: I understand that, but the relevance of stained wood is that any loss must be taken into account. The wood may have fetched a higher price, had it not been stained. Such matters are not as simple in tax terms as they might appear.

I am told that there is a shortage of harvesting resources in the south, and that there are inherent additional difficulties associated with harvesting fallen trees. The storage of timber for gradual introduction to the market is costly, risky and requires extensive facilities. Additional substantial costs are involved in restoring damaged woodlands, which must be extensively cleared before replanting can commence.

Perhaps the Minister's reply covered that expenditure. Low quality or damaged fallen timber may be unmarketable, or its market value may be substantially less than the cost of clearing the damage. The net income of woodland owners in those areas, which have lost 15 million trees, will be greatly reduced. I should like to think that I have some support for advancing the argument on behalf of woodland owners in the south. Ministers should take their problems into account when the Bill is considered in the Department and debated on the Floor of the House.

I shall not read what the National Trust says, as you, Mr. Hunt, will surely intervene on my contribution, modest as it is, to bring me to order. But the National Trust is particularly concerned about the substantial expenditure into which it has been drawn as a result of the devastation in the south of England. The south suffered in a way that no other part of the country suffered during that difficult time. Surely the amendment gives Tory Back Benchers the chance to speak on behalf of the people of the southern counties, particularly Kent. My correspondence in recent months shows that they are increasingly worried about the absence of representation in the House of Commons.

Miss Ann Widdecombe (Maidstone): I fully understand the Opposition's desperation. They have to go all the way to Cumbria to find a spokesman for Kent, because they have no representatives of their own there. If the speech by the hon. Member for Workington (Mr. Campbell-Savours) is a measure of the representation that they might have expected, had there

been a Labour constituency in Kent, they are wise to choose not to have one.

Furthermore, I hardly recognise the picture of total gloom that the hon. Gentleman paints. If he lived in and represented Kent, and spent several days a week talking to local interests, which he now sets himself up as representing, he would know that there is considerable gratitude for many of the recent measures.

I do not have the hon. Member's skill in trying the patience of the Chair by going down roads which I should not go down, but what the Minister has said today is merely an added source of comfort to my constituents who are already grateful for the replanting grants because the largest devastation in Kent was in the orchards. People are grateful for the money made available and the help given to local councils on clearance, and though many areas still require further representation, which they are getting from the Kent hon. Members, people are grateful for what has been done so far and will welcome the further measures proposed today.

Mr. Lamont: May I say a sentence in reply to the hon. Member for Workington (Mr. Campbell-Savours)? The schedule deals with the withdrawal of tax relief from forestry. It has nothing directly to do with storm damage.

Mr. Campbell-Savours: It should have.

Mr. Lamont: We are withdrawing tax relief from forestry and that has been wholly welcomed by Opposition Members. I do not see how we could be more ingenious in our use of tax relief for storm damage. People with existing woodlands will be able to use tax relief for clearance purposes. As a result of the amendments, the law will be interpreted in such a way as to help them clear the damage step by step.

The answers to the hon. Gentleman's questions were set out in the statement on 7 June by my right honourable Friend the Minister of Agriculture, Fisheries and Food. I suggest that he looks at that.

Amendment agreed to.

Mr. Chris Smith: I beg to move amendment No. 272, in page 133, leave out lines 32 to 37 and insert—

"(a) he was occupying commercial woodlands on that date; or

(b) there had been work undertaken for the establishment of commercial woodlands before that date; and

(c) he had received approval for forestry grant under section 1 of the Forestry Act 1979 with respect to the use and management to the land for forestry purposes."

The Chairman: With this it will be convenient to take the following amendments: No. 270, in page 133, line 35, leave out from "date" to end of line 37.

No. 271, in page 133, line 37, at end insert—

"and

(d) the requirements of sub-paragraph (3) below are satisfied with respect to the land which comprises them;".

No. 273, in page 133, line 38, leave out from "below" to end of line 39 and insert—

" 'work undertaken' does not include work undertaken which is not evidenced by a".

No. 274, in page 133, leave out lines 41 to 50.

No. 350, in page 133, line 45, leave out "or" and insert "and".

No. 351, in page 133, line 46, leave out "made an application" and insert

"received approval from the Forestry Commissioners".

No. 352, in page 133, leave out lines 49 and 50.

Mr. Smith: This group of amendments relates to the transitional period in paragraph 4 of schedule 6. We welcome the general thrust of the Government's removal of tax relief from forestry, but we have severe reservations about the impact of the transitional period. The Government propose that if a landowner has made application to the Forestry Commission under the old grant system—I shall come back to that because the making of the application is important and is dealt with by one of the other amendments—but has not yet begun planting work on the land, he will still be able to claim tax relief and grant under the old system for any planting in the five-year period from now until the 1993 deadline.

Such a transitional arrangement might be sensible if we were talking only about a small area of land. But we are not. My hon. Friend the Member for Caerphilly (Mr. Davies) managed to flush from the Government in a series of parliamentary questions and answers the staggering and alarming fact that Forestry Commission approval has been given for 235,000 hectares but planting has not yet started. The figure would be even higher if all applications were included. That is approximately the size of Cheshire. It divides into an area of about 75,000 hectares in England, as revealed in a parliamentary question on 3 May 1988, and an area of about 8,800 hectares in Wales, as revealed in an answer on 22 April. By far the largest area is in Scotland, where there are nearly 150,000 hectares of as yet unplanted land. That was revealed in an answer on 24 April this year.

Our amendments seek to establish a different principle. Even if planting has not yet started, the Government say that for that five-year period the old tax relief system should remain for those 250,000 hectares of land. We say that it should not. If planting had not started by Budget day, the landowner should apply under the new woodland grant scheme, rather than qualify for tax relief under the old system. Amendments No. 272, 273 and 274 enshrine that basic principle. Planting should have started for the landowner to qualify for tax relief.

Amendments Nos. 270 and 271 are probing amendments to flush out more information on the same issue. Nos. 350, 351 and 352, tabled by the hon. Member for Basingstoke (Mr. Hunter), are grouped with our amendments. Amendment No. 351 seeks to tackle the provision in paragraph (4) of the schedule, which states

[Mr. Smith.]

that a landowner would qualify for tax relief if he had merely applied before 15 March for Forestry Commission approval, even if that approval had not yet been given. Indeed, even if Forestry Commission approval was refused under the old system—and it rarely happened—the tax relief would still apply if the Government's provision were introduced. Only the application is important in the current wording of paragraph (4).

The hon. Member for Basingstoke will no doubt wish to speak to his amendments, but on a first reading, we find them worthy of support and I hope that the Government will consider them carefully.

I referred to the substantial area of land—235,000 hectares—that is affected by the transitional provisions. When the Government introduced the change to the tax regime on forestry, they said that they were removing forestry from tax. In the long term that is what they are doing. But the transitional arrangements open an enormous loophole for many landowners to proceed in the old way under the old tax relief system and plant what is in many cases environmentally damaging woodland.

5.45 pm

Let me give two examples. The *Cambrian News* of 5 June 1987 revealed that the Forestry Commission had considered approving 450 acres of conifer plantation in protected areas of the Cambrian mountains. These are areas which the Government themselves have designated as environmentally sensitive. Yet grant approval was given by the Forestry Commission for new conifer plantations in Bara Ceirch, Llanddewi Brewi, Bwlch y Garreg and Talybont where not only the Nature Conservancy Council but Dyfed and Ceredigion councils and the Welsh Water Authority were concerned about the prospect of planting. Because application had been made to the Forestry Commission the owners of those areas of private forestry can still, under the transitional protection offered by paragraph 4, go ahead and engage in their environmentally damaging planting work.

Mr. Campbell-Savours: I cannot find the figures and perhaps my hon. Friend has them. Is it true that if all that land were to be sown over the next five years it would lead to a substantial increase on a year-on-year basis in the levels of afforestation? Perhaps the devious intent behind the whole affair is to increase afforestation because the Government believe that the scheme is not working satisfactorily.

Mr. Smith: I am grateful to my hon. Friend for that intervention. It anticipates a point that I shall come to in a few minutes.

My second example, to which the Minister has already referred, is that of the Flow country in Caithness and Sutherland in the far north of Scotland which is wonderfully beautiful and extremely remote. It is a land of wide skies and distant mountains which is regarded by many international bodies as being of supreme environmental and ecological significance. During the past few years however, much of that value has been destroyed by the indiscriminate planting on a massive scale of large conifer forests purely for tax reasons. Some areas within the Flow country would fall within the transitional provisions of paragraph 4.

Only in January of this year the Secretary of State for Scotland made a statement saying that he had approved four private forestry grant applications in the Flow country involving about 2,300 hectares. That area of land and other areas in the Flow country will certainly be included within the transitional protection offered by the Government. Our charge to the Government is that many environmentally important sites are likely to be damaged precisely because the Government are allowing the taxation relief system to continue for five years for that large area of land.

It is of great sadness to the Opposition that Forestry Commission approval mechanisms are conducted in secret, with little public involvement, and that the Forestry Commission is reluctant to inform the public of its decisions. That was true under the old grant system as many environmental organisations pointed out. In its most recent newsletter to members, the Ramblers' Association included an article by the national park officer of the Lake District national park which highlighted that difficulty. I hope that the processes enshrined in the Government's new woodland grant scheme will be more open and democratic.

I shall now take up a point raised by my hon. Friend the Member for Workington (Mr. Campbell-Savours). We are talking about 235,000 hectares of land and the Government are enshrining in the schedule a five-year transitional period. If everyone who owned parts of that 235,000 hectares of land availed themselves of the opportunities of the old tax relief system, which is in the schedule, we should have a greater rate of planting than 33,000 hectares, a figure that the Government seemed to pluck out of the air as the aim for forestry policy. They are building into the Bill a mechanism that will be an incentive to the owners of those areas of land to avail themselves of the tax relief and proceed with rapid planting.

Mr. Campbell-Savours: Knowing how capitalism and the free market operate, it is clear that those who own the land will be under pressure to sell it to organisations which are willing to invest on the basis of a tax relief that will end in five years. It is almost inevitable that there will be the substantial increase in planting to which my hon. Friend alludes.

Mr. Smith: My hon. Friend is slightly, and unusually, missing a crucial point. A provision of the transitional arrangements is that the person doing the planting must have owned the land at the start of the transitional period. But my hon. Friend is right to suggest that professional forestry bodies and organisations will be brought in, not on an ownership basis, but on a contract basis to afforest the land in as rapid and blanketing a manner as possible.

Mr. Campbell-Savours: I am glad that my hon. Friend clarified that. If the same persons or organisations must own the land we must question the intentions of those investing in existing companies. Will they check on the

shareholders of particular companies to ensure that there is no abuse, or am I misunderstanding again?

Mr. Smith: My hon. Friend touches on an interesting point, but it will not lead to particular problems under the schedule. Difficulties will lie elsewhere. Owners of land stand to gain directly as continuing owners of the land when they begin planting in the following five years.

I referred to the figure of 33,000 hectares that the Government have apparently established for the aim of forestry policy. The Opposition are confused about how the Government arrived at that figure. I studied with great care the debate in the House of Lords on 13 April on forestry policy. The Government spokesman, Lord Sanderson of Bowden specifically failed to answer the question put to him time and again from the Opposition Benches about how the figure of 33,000 hectares was reached. As yet, the Government have offered no convincing explanation. If the five-year period operates in the way that we think that it will, it is likely that considerably more than 33,000 hectares a year will be established during that time.

The cost to the Exchequer will be considerable. When the Government introduced this change in the Budget, they estimated in the Red Book that it would lead to a saving for the Exchequer of some £10 million a year. If the transitional arrangements go ahead unchanged—leaving aside any operation of the new grant system for other land—in the course of five years, the tax relief on that 235,000 hectares of land even at the lower rate of 40 per cent rather than 60 per cent, will cost the Exchequer a total of £82 million. The old grant system will cost the Exchequer £56 million. By our calculations, that will be a considerable increase in the cost to the Exchequer, rather than the saving that the Government said that they expected in their Budget estimate.

If our arguments on environmental grounds do not move the Government's heart—and I hope that they will—I sincerely hope that our financial arguments will. No one knew about the figure of 235,000 hectares at the time of the Budget, except, perhaps, the Forestry Commission, which let the Treasury know about it. We anticipate that that figure will mean increased, not decreased, Exchequer expenditure.

We also have considerable reservations about the operation of the new grants system. Indeed, those reservations are echoed by the Nature Conservancy Council, which says in its comments on the new system:

> "The extent to which environmental factors will lead to a refusal of grant needs to be clarified".

Indeed, the extent to which the new grant system will take account of environmental issues must be rapidly clarified.

As my hon. Friend the Member for Gateshead, East (Ms Quin) said earlier, we have had conflicting statements from different Ministers. The Secretary of State for the Environment, in a welcome statement said that approval for new large-scale planting in the uplands of England should not normally be given. We also welcomed the announcement from the Secretary of State for Scotland that forestry would take more account of environmental needs in future. Both statements were extremely welcome.

However, when we study the new grant system, we find that the grant for broadleaf planting has gone up by 60 per cent, and by 150 per cent for large-scale conifer planting. The difference between the grant available for broadleaved planting on a small scale, which is the sort of forestry development that both sides of the Committee would welcome, and the grant mechanism for large-scale conifer afforestation, which the very development that has caused to much environmental damage throughout the country has been narrowed substantially by the new arrangements.

6 pm

In a letter to my hon. Friend the Member for Caerphilly (Mr. Davies) the Oxford Forestry Institute said clearly that

> "For new conifer plantations larger than 10 hectares the new grant is £615, against average aggregate costs (without overheads) of £524 in Scotland in 1986."

The letter continues:

> "The new policy thus amounts virtually to saying 'you provide the land and we'll give you the trees'."

The prospect worries us severely and we hope that under the new grant system environmental considerations will play a far greater part than they have under the old grant system. However, our principle objection remains clearly and strongly the massive loophole that is being brought in for the five-year transitional period.

A large amount of land and many environmentally sensitive and important areas are involved. We hope that the Government will accept that there is a major problem and that they are allowing the old tax relief system, which caused such problems in the past, to continue for those areas. The system should be abandoned now for those areas as well as for the future in the manner in which the Government say that they wish to remove to.

I strongly commend amendment No. 272, which seeks to put an end to the major loophole that the schedule will create.

Mr. Hunter: As the hon. Member for Islington, South and Finsbury (Mr. Smith) has rightly said, the last three of the eight amendments in this group are tabled in my name. I am bound to say that I agree with the greater part of the hon. Gentleman's remarks. This is not an issue on which there are grounds for party political or philosophic divide. It is clear that more evidence has come to light since the pronouncements of March, and the kernel of the question is in the future of some 235,000 hectares during the next five years.

I can speak briefly because the hon. Member for Islington, South and Finsbury has expressed the essential arguments. The question is whether the rate of plantation will accelerate as a result of paragraph 4 of schedule 6. If so, it will result in loss of revenue to the Treasury and will be disadvantageous for conservation and the environment.

[Mr. Hunter.]

I need not speak further in support of my amendments, other than to say that I regard them as probing amendments and that I look forward to hearing my right honourable Friend's response.

Mr. Nigel Griffiths (Edinburgh, South): We are discussing one of the saddest and sorriest examples of the private sector taking over from the Government. It is a major ecological disaster and the result of rampant greed in the private sector, which the Government have sadly encouraged as they have in many other matters.

Unfortunately, the scheme is a result of the Budget, and there will be further devastation if the amendment is not accepted. A number of rich and famous people stand to gain even more from forestry than previously as a result of these changes. Under the old system there was a grant of £240 per hectare and on top one could expect 40 per cent tax relief of somewhere in the order of £344, giving a total of £584. Now that arrangement is to be replaced by grants of £615 per hectare, which is £31 more. The grants will be more directional, but those of us who have no faith in the Forestry Commission's ability to plan for our ecology and environment realise that the direction into which the money will be channelled—combined with the differential in grant between conifers and broadleaved plants—will lead to a further green scumming of many of the most beautiful parts of the country.

There is no doubt that after the Budget the corks popped, certainly in the Forestry Commission headquarters in Edinburgh, when the grants were announced and it knew that it could give grants to continue much of the work that it has undertaken in the past. My hon. Friend the Member for Gateshead, East (Ms Quin) mentioned the Borders and the grants available. It is worthwhile going north to examine who gained what under the Conservative Government's previous financial grants and what those people might expect to gain if they plant similar acreages now.

The Thompson twins planted nearly 890 acres at Conhess Farm in the Borders and—on the 40 per cent tax relief and on the grants prior to the Budget—made at least £209,000, according to my estimate. If they re-planted today, and were so permitted, they would stand to gain £221,000. In other words, they would gain £11,000 more from the Exchequer.

In the Borders, Baron Rockley planted 505 acres at Eskdalemuir. Under the old system, he could have expected to gain a minimum of £119,000; under the new system, that would be £125,000. Another example, I am sad to say, is Jean Balfour who chaired the Scottish Countryside Commission for 10 years. She has a holding at Corlae Wood of 1,321 acres. Her pre-Budget gains might reasonably be estimated at £311,000; her likely gains under the new system could be as much as £328,000. James Gulliver has a holding of 683 acres in central Scotland. In pre-Budget gains, he could have expected to make £150,000 from the taxpayer; now he will gain £158,000 if he invests a similar amount. Shirley Porter, we are told, has great concern for public money. We know that she is an expert on reclaiming land, and indeed, knows the dead weight value of certain properties in London. But did the Minister know when he visited the Flow country that he was probably gazing on the very trees which she had planted and which have now fallen over? Does he know that his Government helped the Conservative leader of the City of Westminster council to more than £415,000 of public money? That lady is concerned about public money—well, she has had plenty of it. Does the Minister know that under his new system, if the Forestry Commission approved the grants, she would make more than £438,000—a gain, after the Budget, of an additional £23,000 from the Government?

Mr. Campbell-Savours: Lady Porter invested that £438,000 of taxpayers' money and it might be interesting to note what she got for it—a forest of dying trees. Perhaps her judgment on the use of taxpayers' money is not too good.

Mr. Griffiths: That is true. The scheme is geared to her own personal gain—something which the amendments would eliminate. We are trying, for example, to eliminate Hurricane Higgins' windfall gains of £220,000 or more from his 933 acres in Scotland. If he had applied for grant, he would have gained not £220,000 but £232,000 or more. The ubiquitous Terry Wogan, again up in the Flow country in which the Minister has such a keen interest, stood to gain 40 per cent—I am sure he got more in tax relief—on £148,000 and now stands to gain £156,000, again on the premise of investing in a similar acreage with the Forestry Commission's permission.

This measure is a disaster and I predict that with the 235,000 acres in which the Government are now encouraging forestry speculators to invest, within the next five years past development will be nothing compared with the pace of development over the next few years as more parts of the Flow country, and other ecologically valuable sites, are further devastated.

Unless the Minister failed in his foray up there a fortnight ago, to see the devastation, let us hear what the Royal Society for the Protection of Birds had to say in its excellent document on the Flow country, which, I understand, was sent to every Member of Parliament. It called on the Secretary of State to halt further planting until a full study had been made of the effects of such forestry on birds and areas in general. Sadly, the Secretary of State did not do that when he was asked two years ago. Much further planting has occurred, according to the RSPB, causing more damage to wild life.

Before forestry began to expand so fast in the 1980s, that far north eastern corner of Scotland was the most outstanding area for nesting moorland birds in the United Kingdom. It ranked as one of the world's outstanding ecosystems. My hon. Friend the Member for Workington (Mr. Campbell-Savours) has graphically shown the pictures of what has since happened to that country. Dead and dying trees were planted with no thought for the public weal, the public good, or whether the wood was needed for our country and its economy. The sole concern of Lady Porter and others was to make a great deal of money.

Ms Quin: Would my hon. Friend consider the possibility that Lady Porter might now wish to sell her dying forests for 5p?

Mr. Griffiths: That is a point well made. But I have no doubt that Lady Porter would expect someone to pay more like £50 million for her investment. The need is not for Lady Porter to sell because we have such firms as Fountain Forestry, Tillhill Forestry and The Economic Forestry Group which are to the environment what Rachman was to housing. Planting in the Flow country has had a devastating effect and we want to convert the Government further into channelling any investment in forestry into more broadleaved plants and evergreen conifers and to ensuring that ecology is taken into account. Sadly, the Conservatives have become the radical and rapacious developers—or at least the champions of them—while the Labour party is now the new conservative protectors of the environment. That is what we intend in moving this and other amendments. We hope that the Government will see sense before the 235,000 hectares are further damaged beyond repair.

Mr. Boswell: One of the few pleasures left to a Government Backbencher is to take alternate swipes at his Front Bench and at the Opposition. On this occasion I shall be inviting the Committee firmly to resist the amendment as I hope the Financial Secretary will.

There are three basic areas in which the Opposition have not given us a realistic picture. The first is their web of costs and figures. It seems unlikely that my right honourable Friend failed to take these possible, or hypothetical, considerations into account in framing his Budget.

In particular, I was interested in the figure of 235,000 hectares of land that might still be planted under the transitional arrangements. As the annual rate of planting has not exceeded 26,000 hectares—

Mr. Campbell-Savours: Yet.

Mr. Boswell: —it is mathematically obvious that only half that area could be planted, even if nothing else were planted, or that the rate of planting should double. I fail to see why that should happen when only 26,000 hectares were planted on the assumption of a forward flow of tax relief indefinitely. If planters knew that their tax relief was to terminate after five years, I do not see why they should double their planting rate.

6.15 pm

The second point is that the amendment bears ill on the long-term nature of forestry, about which we spoke earlier. The five-year period would be about 10 per cent of the economic life of a coniferous tree and about 5 per cent of the life of a broadleaf tree. It would be merely a blink of time. I appreciate that Opposition Members may be having difficulty, because their idea of a consistent and firm policy on defence, for example, is to change their mind at least twice a week, but that is not so in forestry. We need a reasonable long-term regime. We cannot keep pulling it up. The transitional period is entirely reasonable.

Even if the amendment prevailed, it would fail to hit the target that Opposition Members want. The people about whom they are so worried could withdraw their proposals and bring them back under the grant regime, if they could obtain grants. The people who would be seriously hit by the arrangements are owners of traditional woodlands that are already fully established and halfway—but with a long way to go—to maturity. Those people would suddenly find that their tax relief was withheld and they would be extremely hard pressed. For those reasons I invite my right honourable Friend the Minister to resist the amendment.

Mr. Worthington: Opposition Members were glad that the Chancellor seemed to accept the offensiveness of the present system, but we seek explanations about what we anticipate will be the continuation of a forestry system that is geared not to the needs of this country but to the needs of those in private forestry companies. We recognise the importance of planting trees in Britain. It is interesting that the strategic importance of forestry is accepted but that of other industries is not.

[*Interruption.*]

I have limited skill in lipreading—my hon. Friend the Member for Gateshead, East (Ms Quin) refers to shipbuilding. The level of support that has been given to forestry far exceeds that given to many other industries.

We are uneasy about the transitional period. The hon. Member for Daventry (Mr. Boswell) seemed to disbelieve our proposition that there would be an acceleration in the rate of planting over the next five years. We shall come back next year and in the following years and show that we were right. It is clear that as the tax system has been so generous to those who have no stake in the communities whose acreage they are using, they will seek to make maximum use of it during the next few years.

I agree with what has been said about the role of the Forestry Commission. The Opposition have had considerable difficulty in obtaining information. A few knuckles should be rapped. The House has the right to know how publicly funded bodies such as the Forestry Commission are using their resources and there should be no further difficulty in obtaining the sort of information that we have sought.

Suspicions arise. Surely it would be clear to any investor and perhaps to the Forestry Commission that this sort of gravy train could not persist and that even under this Government there was an offensiveness about the system. I suspect that people have been buying up acres and that the Forestry Commission has been approving plans rather more rapidly than might have happened in other circumstances.

I have doubts about the transitional period. If an industry has been treated simply as a subject for speculative capitalism, why on earth should it not follow the rules of the market? Why must it be featherbedded for another five years? If there is a black Monday on the stock exchange, some people may suddenly lose massive amounts of money because the market has turned. Why should not the same conditions

[Mr. Worthington.]

apply to the vagaries of the Government's taxation policy? The Government have treated the forestry industry not in a strategic way that is bound into environmental considerations but simply as a tax break for the wealthy, so why should there continue to be a generous transitional arrangement?

"Transitional arrangement" brings to mind other references to those words in recent months.

[*Interruption.*]

Housing benefit is exactly such an example. There was no talk about transitional arrangements to cushion some of the most disadvantaged people against the withdrawal of large sums of income, which were removed overnight by the Government, until pressure caused the Government to change. I have little sympathy for the transitional arrangements. Similarly, in urban planning there is a great deal of speculative investment in land on the assumption that its designation will at some future stage be fortuitous and that an investor will be able to make a lot of profit on it.

I see no reason why the forestry industry should not take the rough with the smooth. The private forestry companies have been doing well out of the system and if there is to be a tax change, I do not understand why there should be such a generous transitional period.

Mr. John Butterfill (Bournemouth, West): Would the hon. Gentleman take the same strong view if the tax concessions related to, say, shipbuilding investment?

Mr. Worthington: I thought that I had dealt with that matter earlier. I thought that there had been double standards and that the conditions applied to the forestry industry were different from those applied to other industries where we could argue that they also needed support to strengthen them on a transitional basis.

Mr. Chris Smith: Does my hon. Friend agree that if such relief were available for an industry such as shipbuilding, it would create many more jobs at a much cheaper cost per job than does forestry, which is extremely expensive on a cost-per-job basis?

Mr. Worthington: I agree with my hon. Friend's point, which I intended to come to later.

Ms Quin: Does my hon. Friend further agree that shipbuilding subsidies would have less detrimental effects on the environment than the subsidies given to forestry over the years?

Mr. Worthington: The case gets stronger and stronger.

I represent a Scottish constituency; we have heard many references to the impact of forestry there. There has been considerable revulsion in Scotland to the development of the forestry industry, which has had no sympathy with the needs and aspirations of the local community. There is something offensive about the land that I represent being used for tax breaks for people who have never been there. The Opposition are offended that that old cemetery seller, Lady Porter, should be able to invest money in a part of Scotland that is unknown to her and derive considerable financial benefit in a manner that damages the local environment. The Government would run a mile from investing similar sums in projects that would be of direct value to the local people.

Other hon. Members have spoken of their sense of shock at seeing the impact of conifer afforestation in certain areas. The Minister also spoke about it. When he was in Sutherland I was walking in the Border area.

6.26 pm

Sitting suspended for a Division in the House.

6.40 pm

On resuming—

Mr. Worthington: I had reached the Borders and was pointing out that it was another part of the world that seemed have been spoilt by the tax incentives for the planting of conifers. I can do no better than quote the Public Accounts Committee which stated that forestry support

"should not be left to the fortuitous consequences of the exploitation of a tax loophole which depends more on the personal circumstances of the taxpayers concerned than on forestry merits".

That seems sensible.

I also support the conclusions of the Royal Society for the Protection of Birds. It stated that it could find

"no convincing economic or strategic reason for the public to support further conifer planting".

It is ironic that the Government's stated policy is to transfer most of the country's afforestation to private hands although the majority support comes from the public.

The amendment's scope is limited. We should be given an assurance by the Government that cross-departmental mechanism works. We should look at the importance of one of the country's major industries—forestry—in a way that is geared to integrating the industry to the needs of the local community and to considering its environmental impact.

Ms Quin: I support my hon. Friend the Member for Islington, South and Finsbury (Mr. Smith). Although we were pleased with the Chancellor of the Exchequer's Budget decision, we are worried that these transitional measures may go a long way towards counteracting the beneficial effects of ending tax concessions to private investors in forestry. My hon. Friends' comments about the transitional period has made me fearful of the consequences, especially the figure of 235,000 hectares, the area for which I understand applications have been approved. I have been told that, at normal rates, this represents nine years' planting which means that the Treasury is giving five years' transitional grant for nine years of planting.

Did the Treasury realise that that would be the effect when the Chancellor of the Exchequer decided to discontinue the tax concession? Surely not. Surely the Treasury hoped for a speedy end to the kind of planting which we all deplore although it has taken place on such a large scale in the past few years, as my hon. Friends said.

The statement by the Secretary of State for the Environment was mentioned. In it he said that there would be no further large-scale conifer plantations in England. I understand that this decision does not take account of the 80,000 or so hectares for which permission has already been granted. Where are these hectares? Are they in the uplands, and, if so, how many are there? Are they in environmentally sensitive areas or areas of outstanding natural beauty? We should like answers.

It is likely that many of the people to whom planting approval has been given and who will be subject to the transitional arrangements have benefited considerably from the reduction in the top rate of taxes. They are making a killing from the Budget anyway, and on top of that, they are being helped by the transitional arrangements. The money spent on having a transitional period could be better spent on countering the environmental devastation caused by the hurricane in south-east England, which was described by my hon. Friend the Member for Workington (Mr. Campbell-Savours). It would be better to spend the money on that, instead of wasting it on this transitional period. I hope that I am wrong and that the Government will accept our amendment, but so far, that does not appear likely.

6.45 pm

I agree with the reservations that my hon. Friends have expressed about the new planting grants and the role of the Forestry Commission. It is true that the Forestry Commission makes many of its decisions in secret and is judge and jury in cases that raise environmental doubts about whether planting permission should be given. I take the view that an independent organisation should be responsible for granting that permission, because for more than 50 years the remit of the Forestry Commission has been to increase timber production and nothing else.

I hope that the Government will accept our amendment, because it is quite unjustified to have a transitional period, particularly when we are talking about grant approvals. We are not talking only about applications on which work has already begun. How many of the 235,000 hectares of which we have heard relate to applications on which work has already begun in planting trees, and how many relate simply to approval of applications or applications that have merely been lodged? We need to know more of the details, because we suspect that the problem is much greater than we have been told.

Mr. Campbell-Savours: I intervene briefly to dissent, if only marginally, from the view that has been expressed by some of my hon. Friends about conifer afforestation. I live in Keswick, in perhaps one of the most beautiful parts of the United Kingdom. I look out over the fells and vast areas of land that are the subject of conifer afforestation, and I may say that it is a most beautiful sight. Perhaps I am a little Philistine in the matter, but I have never been able to understand the criticism that is levelled against the Forestry Commission for the good work that it does in my constituency, not only in providing jobs but in the important contribution that it makes to the environment.

Mr. Griffiths: Perhaps my hon. Friend is too young and does not appreciate the view of someone as eminent as Wainwright—

Mr. Campbell-Savours: Yes, he is a very good man.

Mr. Griffiths: —who in his books describes the great beauty that has now disappeared for ever.

Mr. Campbell-Savours: Beauty is in the eye of the beholder, and what Mr. Wainwright may find ugly today—that is not necessarily true—I may find attractive. We should be a little more objective about what constitutes beauty.

Ms Quin: I know that certain aspects of conifer plantations in the Lake District are attractive in certain areas, but is my hon. Friend aware of the studies that show how the large-scale planting of conifers can acidify the soil and increase the problem of acid rain?

Mr. Campbell-Savours: That is so, but most of the incidence of acid rain in the Lake District is in the tarn areas, which are invariably higher than the highest level of afforestation. It may be that that problem does not affect my constituency as it affects many in Scotland.

I am indebted to my hon. Friend the Member for Dunfermline, East (Mr. Brown) for advising me about the validity of a point that I made in an intervention. I do not fully understand. I listened carefully but, having consulted my colleagues, I am still at a loss. If it is true that approximately 25,000 hectares are planted annually under present arrangements, that 235,000 hectares will be available for afforestation over the next five years and that the tax regime will end after that time, it is likely that the people who hold that land will, by one means or another, find a way to utilise the tax arrangement before it expires. I was wrong in presuming that people could divest themselves of their interests and that the people who acquired them would be able to take advantage of the tax relief. However, it seems that those who have those interests will benefit from the tax relief.

My hon. Friend the Member for Edinburgh, South (Mr. Griffiths) drew to my attention four main forestry companies—the Economic Forestry Group, Fountain Forestry, Tillhill Forestry and the Scottish Woodland Owners (Commercial) Ltd. I am told that they own a large proportion of the forestry in both Scotland and Cornwall. I am also told that searches by the Royal Society for the Protection of Birds reveal that by December 1986 Fountain Forestry had bought more than 92,000 acres of the main Flow country at an average of about £80 an acre. It had sold about one

[Mr. Campbell-Savours.]

third at four times the price to 76 investors, 72 of whom had English addresses.

From that morsel of information, we can establish the flow of transactions. Large companies acquire land and then sell off small packages of it to individuals for forestry. The 76 investors are not identified, but they exist. I presume that the 235,000 hectares to which my hon. Friend referred me has been through that cycle and has now fallen into the hands of individuals downstream, who will be able to claim tax relief. To judge from the lack of noise from Conservative Members, I assume that I am correct. If I am, those people will have a clear interest in securing the afforestation of their holdings. Whether we produced 10,000, 20,000 or 50,000 acres of afforested land last year is of no consequence. Those people now have a target date. They have to complete the process by the last day of the fifth year and I believe that they are likely to do so.

I want to ask the Minister a simple question. Am I right or wrong? What are his projections for the level of afforestation over the next five years, which will take advantage of the transitional tax arrangements? If he can assure me that it will not be more than the current level of afforestation—we hope that it will be less—it might mitigate our argument. If it exceeds the current level, the scheme is, as I said, a devious attempt to increase afforestation, as the Government obviously believe that the policy has not been as successful as it should have been.

Mr. James Wallace (Orkney and Shetland): I wish to ask the Minister a few questions. Much has been said, not least by the hon. Member for Islington, South and Finsbury (Mr. Smith), about the Flow country. There has been widespread anxiety about what has been going on there, although I believe that only between 10 and 15 per cent of plantable land is under discussion. The matter has made national headlines and generated widespread concern because of the well-known names that are sometimes associated with it.

In the Highlands of Scotland there are working farmers who own very small amounts of land. How does the Minister perceive the arrangements affecting them? In particular, concern has been expressed that the planting grants that have been introduced to counterbalance the withdrawal of relief seem designed to encourage the planting of trees in areas where, for agricultural reasons, the case for diversification has been much greater. I am thinking of places such as East Anglia and even some parts of east Scotland. There is an imbalance that will take away advantages from the small-scale farmers in upland areas.

I am sure that the Minister is aware of the concern of the crofting communities that permission for planting trees must be sought not only from public bodies but from the landlord. I understand that the Government have been reviewing the matter, and should be interested in the Minister's comments. Have the transitional implications for crofters, who are tenants of the land, been considered? What are the implications for the small-scale farmer who wishes to continue to plant forestry in his smallholding in a very modest way for good livestock or land husbandry reasons?

Mr. Lamont: The hon. Member for Workington (Mr. Campbell-Savours) expressed a minority view on conifers. My views are more like those of the hon. Member for Islington, South and Finsbury (Mr. Smith). However, it is not a matter of personal aesthetics. The arguments are about the effect on the environment and the wildlife. There are objections to closely planted conifer forests not just because of what they look like, but because of their effect on plants, bird life and animal life. Moreover, some of those trees replace other landscapes such as moorland, the Flow country and heathland, which are ecologically important and interesting. So it is not a matter of artistic or aesthetic judgment.

Much of the debate has concentrated on whether there should be a transitional period. The amendments deal with where precisely we should draw the line and I shall be discussing them later. When the hon. Member for Workington spoke about the effect and the incentive for people to go in for vast amounts of afforestation, I am sure that he was aware that we are drawing the line only where commitments have been entered into. Transitional relief is available only if people were occupying woodlands—that is, if they had planted commercial woodlands—on Budget day, or if they were committed to acquiring woodlands by contractual or other arrangements or if, although not actually occupying the woodlands on Budget day, they had before that day contracted to have trees planted on bare land or had applied for Forestry Commission planting grants.

There may be room for argument about the proper degree of commitment to allow, but the situation is not quite as unrestrained as the hon. Member for Workington implied. Rightly or wrongly, we have confined the relief to conditions that involve a degree of commitment. Nevertheless, there must be a transitional period. After all, when tax changes affect individuals or important industries it is normal to have transitional arrangements. It would be unprecedented to introduce overnight tax changes that would have a retrospective effect, with no provision for transition.

7 pm

We should bear in mind the obvious point—it has not been mentioned much in the debate—about the length of time it takes for trees to grow. As my hon. Friend the Member for Daventry (Mr. Boswell) emphasised, it takes 50 years for a conifer and 100 years for some broadleaf trees, so a transitional period of five years is not unthinkable. Tax relief for five years will be linked to commitments entered into on the basis of the previous law at Budget day, and it would be wrong to assume that planting carried out with tax relief will be uncontrolled. Let us not forget that no significant area of planting by the private sector is undertaken without the Forestry Commission's approval under its grant schemes. Approval is given only after appropriate consultation with other authorities, such as the local planning authorities. As

Opposition Members know, if unresolved objections arise from such consultation, the Forestry Commission cannot simply override them without involving the Secretary of State, so the situation is not quite so wild and uncontrolled as some Opposition speeches have implied.

Mr. Campbell-Savours: Would an oral agreement between a landowner and someone responsible for planting constitute a reason for granting tax relief under the arrangements that the Minister has set out? If the agreement is not oral, what is it?

Mr. Lamont: I shall come to that, as it is the subject of the amendments.

The hon. Member for Islington, South and Finsbury (Mr. Smith) referred to the increases that were made in the new grants after Budget day. He pointed out that the percentage increases for conifers were larger than for broadleaves, but that is not the whole story. One crucial point concerns the mix between broadleaves and conifers within a forest. Grants already exist for trees in mixed woodlands but we have altered the grant regime for "mixed forests" in a way that is helpful to broadleaves and will enable even forests with a small proportion of broadleaves to qualify for higher grants in future. The hon. Gentleman's point is therefore not quite correct. Despite the apparent paradox in the Budget, to which the hon. Member for Islington, South and Finsbury referred, the system is now heavily tilted in favour of broadleaves, although it remains to be seen whether it will be enough to provide the desired economic incentive.

The hon. Member for Workington (Mr. Campbell-Savours) said that planting is to take place on 235,000 hectares that were cleared before the Budget. I understand how the hon. Gentleman arrived at that figure, but it is incorrect. That figure relates to the gross area of land for which approval has been given and includes existing woodlands to be felled and restocked, areas of unplantable land such as mountain tops and lakes, areas that cannot be planted for environmental or landscape reasons, and areas where due to a change of ownership more than one application for grant aid has been made. The total area available for new afforestation where clearance was given before the Budget is approximately 100,000 hectares, and that will no doubt contribute to achieving the target of 33,000 hectares to which my hon. Friend the Member for Daventry (Mr. Boswell) has referred, although we have been far short of that figure even when we had large amounts of land in the pipeline in the past. I repeat and emphasise that we expect the tax measures in this Bill to cost nothing in 1988–89 and 1989–90, but to build up to a positive yield to the Exchequer to £10 million.

I congratulate the hon. Member for Islington, South and Finsbury on his Welsh accent. He referred to two cases. I do not know about the Welsh one, but by chance I know of and have enquired about the Scottish one. I, too, have read about that case, and there was a reference to the Flow country which has featured largely in this debate. My right honourable and learned Friend the Secretary of State for Scotland gave approval to over 1,000 hectares of new planting, but he refused planting on nearly 500 hectares. He also stipulated that 950 hectares with high conservation value were to remain unplanted. One of the points of moving away from a system of tax relief to one that is dependent on grants is that both the Forestry Commission and the Secretary of State have the ability to make decisions and control the development of forestry more on environmental grounds.

Ms Quin: The Minister said that 100,000 hectares was a more accurate figure for the area for which approval had been given for planting. Of that 100,000 hectares, on how many has planting work already begun, and how many are simply areas for which approval has been given? That is important for our amendment.

Mr. Lamont: I am sorry, but I do not have that figure to hand. It is not a crucial figure, as hon. Members well know.

[*Interruption.*]

I welcome the hon. Member for Edinburgh, Central (Mr. Darling) and convey to him the warm congratulations of all Members of the House.

The precise question before the Committee is how we should draw the line in relation to commitments that have been entered into. The Opposition have put forward two sets of amendments. I shall discuss in detail amendments Nos. 270 and 271 if the hon. Member for Islington, South and Finsbury wishes me to, but I assure him that they do not make much sense, as I believe that he acknowledged. He described them as probing amendments, seeking to apply restrictions to existing woodlands and to tie the transitional provisions to the application for a grant. That obviously does not make any sense for existing woodlands as occupiers of existing woodlands would not need to apply for a grant.

The more serious set of amendments, Nos. 272 to 274, seek to ensure that the only people who can continue to receive tax relief for the five-year period are those who were already occupiers of woodland or who had started work on planting their woodland by Budget day. We have enabled those who had not started planting trees before Budget day to continue to receive tax relief because we took account of the commitments that had been made. We thought that it would be unreasonable to make the change overnight. Those people would have made their applications or committed themselves in one way or another at a time when they had every good reason to suppose that tax relief would continue.

The proposals of the hon. Member for Islington, South and Finsbury would produce a curious result. An existing owner of woodlands would be denied relief under the transitional provision unless he had received approval for a forestry grant. In many circumstances, that would deny relief to people who are ineligible for a grant because their woodlands were already established and who thus had no intention of carrying out further planting. Denying the availability of the transitional relief would be unjustifiable in those circumstances. Again, under the hon. Gentleman's proposals owners of woodlands in the process of establishment would

[Mr. Lamont.]

need to produce documentary evidence of work undertaken before Budget day. Thus owners who contracted for work with a forestry mangement company would qualify for relief, while owners who did the clearance work themselves would not qualify because they would be unable to produce the documentary evidence. The hon. Gentleman's suggestions as alternative conditions to those in the Bill which I read out a few moments ago would not make any sense.

My hon. Friend the Member for Basingstoke (Mr. Hunter) has proposed different restrictions. His amendment seeks to restrict even more severely the categories of people who may continue to receive relief. As I have explained, we have provided that relief during the transitional period will be available either to people who are committed to planting trees on bare land or who have applied to the Forestry Commission for a grant. My hon. Friend proposes that it should be available only to people who have both committed themselves to planting bare land and recieved approval for planting from the Forestry Commission. I have explained why we have drawn the line where we have and why we think that where there are commitments it would be unfair to penalise people through a sudden change in the tax system. My hon. Friend's amendments would be very restrictive. An application to the Forestry Commission for a grant may be quite an expensive matter. The commission requires detailed plans on landscaping and applicants may well have to seek professional advice before submitting their applications. It may take many months to complete the process. The conditions suggested by my hon. Friend would thus be far too restrictive.

We all enjoy the speeches of the hon. Member for Edinburgh, South (Mr. Griffiths). The further out of touch they are with reality, the more we enjoy them. He made one of his best speeches tonight. I loved his description of people in forestry uncorking champagne bottles. They do not seem to be the same people who have been writing angry letters to me about the harm that the Government are doing to the forestry industry. The hon. Gentleman made a bad point when he described people as being enormous gainers under the Budget change. He was simply taking account of the new grants and taking no account, beyond the transitional period, of the loss of tax deductibility for planting, which has been the whole economic basis of forestry hitherto. When I said that the amount of support and grants that we were giving roughly compensated, in aggregate, for the tax relief taken away, that was based on an aggregate tax relief figure, taking account of higher rate taxpayers and basic rate taxpayers. Not everybody in forestry paid tax at the highest rate under the old tax rates. Some individuals will definitely lose under the new regime as compared with the old, even if the total support is, in aggregate, broadly similar.

7.15 pm

Mr. Griffiths: I wish to ask two questions. The first will give the Financial Secretary a chance to get the answer. Will he tell us the proportion of people not in the higher tax bracket who he thinks are benefiting from the scheme? I suspect that the figure is zero, but I shall stand corrected if the right hono[illegible]ble Gentleman can supply the true figures.

Does the Financial Secretary deny that by introducing aggregate figures he seeks to confuse the matter? The truth is that under the old system a grant was available at £240 per hectare or approximately £97 per acre, and the tax relief available at the time of planting was £344 per hectare or approximately £139 per acre. That gave a total of £584 per hectare, whereas now grants of £615—£31 more—are available for conifer planting.

Mr. Lamont: The hon. Gentleman misrepresents the situation. I can make the point simply. The new regime will cost the Exchequer no more money, so how can the hon. Gentleman possibly be right? We expect to gain £10 million from the tax change in the long run. That gives the hon. Gentleman his answer, and shows that what he said is utterly false. I do not have figures for higher rate taxpayers and basic rate taxpayers, but I know that they will not all pay tax at the highest rate. I do not need any figures, because I know that to be the case.

The comments of the hon. Member for Edinburgh, South contain another contradiction. He says that the new regime is terribly generous and outrageous. Yet the hon. Member for Islington, South and Finsbury constantly says that we were too generous under the old regime. That is the contradiction. The hon. Member for Edinburgh, South alleges that the new regime is too generous, while his hon. Friends complain that people will stay on under the old regime. I can only assume that the hon. Member for Edinburgh, South will vote against the amendment tabled by the hon. Member for Islington, South and Finsbury. The hon. Member for Edinburgh, South should recognise that the Government's changes have not been wildly pleasing to the forestry industry. My hon. Friends who know about the industry have confirmed that, and they have expressed fears about whether we shall attain the planting targets that we have set.

The changes that have benefited the environment have been welcomed. The hon. Member for Islington, South and Finsbury quoted the Royal Society for the Protection of Birds before the Budget but not afterwards when it welcomed the Government's changes, as should my hon. Friends.

Mr. Chris Smith: The Minister said that my hon. Friend the Member for Edinburgh, South (Mr. Griffiths) described the new grant regime as being terribly generous, as indeed it is, but the crucial point on which my hon. Friend and I agree is that, at least the new grant regime makes some attempt to take account of environmental considerations and consequences. The tax rating system that operated before was blind to environmental and ecological consequences. That is the difference between the two systems, and that is why we would rather that land that forms part of the transitional arrangements falls under the new system.

The Minister referred to the Royal Society for the Protection of Birds. The society fully supports our amendment as does the Ramblers Association. Both organisations represent tens of thousands of members up and down the country who have long campaigned for changes in the forestry tax regime.

The Minister made great play of the fact that the transitional arrangements would apply only where commitments had been made. But the only commitment necessary for the transitional protection to be invoked is for an application to have been made to the Forestry Commission under the old system before 15 March. That is the only step that a landlord need take for the tax regime to continue for the next five years.

The Minister also emphasised his estimate of 100,000 hectares rather than our estimate of 235,000 hectares. Ours is a gross figure. The Government and the Forestry Commission refuse to give any information about how they arrive at their figure—what constitutes unplantable land or land that has to be felled before replanting can take place and where changes of ownership occur. No public information is available, so we shall continue to argue about the exact extent of land involved. The area of land in question is very large and much has great environmental significance. Wildlife and bird life habitats and the landscape may be marred irrevocably by forestry planting on a large scale. The Government should not allow that to continue for a further five years. I strongly urge my hon. Friends to vote in favour of our amendment.

Mr. Hunter: In view of my right honourable Friend the Minister's powerful, persuasive and eloquent speech, I shall not press the three amendments in this group tabled in my name.

Question put, That the amendment be made:

The Committee divided: Ayes 14, Noes 20.

AYES

Armstrong, Ms Hilary	Ingram, Mr. Adam
Battle, Mr. John	Morgan, Mr. Rhodri
Brown, Mr. Nicholas	Quin, Ms Joyce
Campbell-Savours, Mr. D. N.	Smith, Mr. Andrew
Darling, Mr. Alistair	Smith, Mr. Chris
Griffiths, Mr. Nigel	Wallace, Mr. James
Henderson, Mr. Doug	Worthington, Mr. Tony

NOES

Arbuthnot, Mr. James	Hunter, Mr. Andrew
Boswell, Mr. Tim	Jack, Mr. Michael
Bright, Mr. Graham	Lamont, Mr. Norman
Brooke, Mr. Peter	Lennox-Boyd, Mr. Mark
Butterfill, Mr. John	Maples, Mr. John
Carrington, Mr. Matthew	Mitchell, Mr. Andrew
Coombs, Mr. Anthony	Shaw, Mr. David
Davies, Mr. Quentin	Stern, Mr. Michael
Favell, Mr. Tony	Wardle, Mr. Charles
Howarth, Mr. Gerald	Widdecombe, Miss Ann

Question accordingly negatived.

7.25 pm

Sitting suspended.

[Continued in col. 557]

PS/Chancellor

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Standing Committee A

FINANCE (NO. 2) BILL

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

Tenth Sitting
Tuesday 21 June 1988
[*Part II*]

CONTENTS

SCHEDULE 6, as amended, agreed to.
CLAUSE 64, as amended, agreed to.
CLAUSES 65 to 90 agreed to.
CLAUSES 99, 100 and 122 to 124, as amended, agreed to.
Adjourned till Thursday 23 June at half-past Four o'clock.

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Standing Committee A

Tuesday 21 June 1988

[*Part II*]

[MR. JOHN HUNT *in the Chair*.]

Finance (No. 2) Bill

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

[*continuation from c. 556*]

9.15 pm

On resuming

Mr. Arbuthnot: I beg to move amendment No. 250, in page 133. line 37, at end insert—

"or (d) he became entitled to occupy the commercial woodland on or after 15 March 1988 on the death of his spouse and that spouse satisfied the conditions of this sub-paragraph;".

The amendment is designed to allow the transitional relief under paragraph 4 to apply if a spouse inherits woodlands during the transitional period, which ends on 5 April 1993. The transitional relief allows a person in occupation of commercial woodlands on Budget day to be taxed under schedule D until 1993. If he sells the land, disposes of it, or gets a new grant for it, that relief is lost. In the case of death when the land is passed on to a spouse, that could be a little harsh. There are other examples of reliefs being preserved when property passes between spouses on death, such as agriculture property relief and capital gains tax retirement relief. I ask my right honourable Friend the Minister to consider whether this should not be another such case.

Mr. Lamont: My hon. Friend is suggesting that the continuation of tax relief for a transitional period for expenses incurred should be available not only to those in occupation—those who planted the trees on Budget day—but also, if they die, to their widows for the transitional period. My hon. Friend has made an important point, which had not occurred to me. We may accept the amendment, or include the proposals in another form. I am seriously interested in the issue and if my hon. Friend will seek leave to withdraw the amendment I undertake to reply on Report.

Mr. Arbuthnot: On that basis, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Amendments made: No. 299, in page 133, line 47, leave out from "1979" to end of line 48 and insert

"or section 2 (1)(e) of the Forestry Act (Northern Ireland) 1953 with respect to the land;".

No. 300, in page 133, line 50, at end insert

"or, in Northern Ireland, by the Department of Agriculture".

No. 301, in page 134, line 1, leave out sub-paragraph (4).

No. 302, in page 134, line 8, at beginning insert

"Subject to sub-paragraph (5A) below."

No. 303, in page 134, line 12, leave out "as respects" and insert "in relation to".

No. 304, in page 134, line 13, leave out "as respects" and insert "in relation to".

No. 305, in page 134, line 16, leave out

"and for the purposes of paragraph (c) above" and insert—

"(5A) An election made under sub-paragraph (1) above in respect of any commercial woodlands shall not have effect in relation to any chargeable period if before the beginning of that period a relevant grant has been made with respect to any land which comprises woodlands on the same estate.

(5B) For the purposes of sub-paragraphs (5) and (5A)".

No. 306, in page 134, line 18, leave out "ten" and insert "two".

No. 307, in page 134, line 23, at end insert—

"(6A) In this paragraph and paragraph 5 below 'relevant grant' means a grant under section 1 of the Forestry Act 1979 or section 2(1)(e) of the Forestry Act (Northern Ireland) 1953 which—

(a) is made on terms and conditions first published after 15 March 1988; and

(b) is not made by way of supplement to a grant made on terms and conditions first published before that date."

No. 308, in page 134, line 26, leave out from beginning to "in" in line 27 and insert

"For any chargeable period in relation to which an election made under paragraph 4(1) above by any person has effect."

No. 309, in page 134, line 30, leave out "that Schedule" and insert "Schedule D".

No. 310, in page 134, line 31, leave out "and" and insert—

"(aa) in computing those profits or gains or losses, no account shall be taken of any relevant grant and no deduction shall be made for any expenditure in respect of which any such grant was made; and".

No. 311, in page 134, line 47, leave out

"the year of assessment 1992–93"

and insert

"a year of assessment".

No. 312, in page 134, line 48, leave out "and" and insert—

"(aa) that year of assessment is the final year of assessment for which that sub-paragraph, as it so applies, has effect as respects that person's occupation of those woodlands; and".

[Mr. Arbuthnot.]

No. 313, in page 134, line 49, leave out

"basis period for the relevant year and 6th April 1993"

and insert

"relevant basis period and the beginning of the next following year of assessment".

No. 314, in page 135, line 4, leave out " 'year' and insert

'basis period', in relation to a year of assessment".

No. 315, in page 135, line 5, leave out "the year 1992–93" and insert "that year of assessment".

No. 316, in page 135, line 7, after "1988" insert "the basis period for".

No. 317, in page 135, line 9, leave out "year 1993–94" and insert

"basis period for the next following year of assessment".—[*Mr. Lamont.*]

Mr. Boswell: I beg to move amendment No. 251, in page 135, line 13 at beginning insert—

"5A.—(1) Where, on or after 6th April 1988, a person incurs qualifying expenditure on woodlands in the United Kingdom of which he is the occupier, he may take a claim under this paragraph.

(2) This paragraph shall not apply in any year in which paragraph 4 of the Schedule applies.

(3) If a person makes a claim under this paragraph, any qualifying expenditure incurred by that person in the year of which the claim is made may be deducted from and may accordingly reduce any agricultural income of that person of that year which would otherwise be chargeable to income tax or corporation tax:
Provided that where the qualifying expenditure exceeds the agricultural income, the excess of qualifying expenditure shall not be deducted but shall instead be carried forward and added to any qualifying expenditure incurred in the next subsequent year.

(4) A claim under this paragraph shall be by notice in writing delivered to the inspector not later than two years after the end of the year of assessment to which the claim applies.

(5) In this paragraph—

(a) 'qualifying expenditure' means the amount by which expenditure wholly and exclusively incurred in respect of planting, replanting, maintaining and managing woodlands exceeds the aggregate of—

(i) income from such woodlands, and

(ii) grants receivable in respect of such woodlands.

(b) 'agricultural income' means either—

(i) income chargeable under Schedule A in respect of land, houses or other buildings in the United Kingdom occupied wholly or mainly for the purposes of husbandry, or

(ii) income chargeable under Schedule D in respect of farming or market gardening in the United Kingdom.

(c) a person who, in connection with any trade carried on by him, has the use of any woodlands wholly or mainly for the purposes of—

(i) felling, processing or removing timber; or

(ii) clearing or otherwise preparing the lands, or any part of them, for replanting;

shall not be treated as the occupier of the woodlands for the purposes of this paragraph.".

The amendment is perhaps the most substantial of the series on forestry topics—

[*Interruption.*]

—from the Conservative Benches. As we had a full debate on the subject, I wish, if possible, to avoid going over the same ground—

[*Hon. Members: "Hear, hear."*]

I am grateful to my hon. Friends and hon. Gentlemen for their encouragement.

Perhaps I may briefly remind the Committee of the significant and substantial characteristics of woodland enterprises. The first factor is their intimate relationship with agricultural land in many instances. The second is the long duration of the production cycle. The third is that recurrent maintenance costs are incurred.

As drafted, the Bill would produce a philosophy which leads to a planting ground at the beginning, no income support through the life of the woodland project—except perhaps some income from commercial thinnings, about one third of the way along the life cycle—and a commercial return at the end. But, as that return is well into the distance, forest owners will inevitably have to find their recurrent maintenance costs out of capital. That applies especially to broadleaves—for the reasons which were explored earlier—which have a longer life cycle.

When my hon. Friends and I tabled the amendment, we had in mind several different problems on which I wish to sound out my right honourable Friend the Financial Secretary this evening and which must be put right in good time before the end of the transitional period, if not with the immediacy of the earlier debate. Clearly, the earlier we know, the better.

The first problem relates to farm forestry. I declare an interest as a farmer, with a few trees. I do not have any fancy forests which would save me a great deal of tax. I have a few trees, however, and am well aware of the thrust of Government policy—I believe that it is supported on both sides of the House—to encourage farm-forestry enterprises. I see an administrative problem in the clear distinction between taxable farm activities and out-of-tax forests, and that is how they will be kept separate, administratively speaking. I fear especially that a zealous inspector or, indeed, one zealous accountant will reprove the farm forester, who may not be very sophisticated and is reluctant to involve himself in forestry, and say to him, "We notice that you have a few trees, Mr. Boswell. We should like some time sheets. How much time did you spend in your woods? How much time did your men spend down there? What equipment was used? Have you attempted to apportion the use of your capital equipment between the two uses?" The Revenue will have to adopt Nelson's eye. If not, there could be some embarrassing and, I believe, counter-productive unstitching later. Will my right honourable Friend the Financial Secretary comment on that?

Representations about the second problem have been made by the Historic Houses Association and other representative bodies. They feel strongly about heritage

woodlands which accompany a park. Earlier, we discussed what was or was not commercial. A traditional estate would have a big house, a park, parkland, amenity woods close to home and perhaps home farms in support, as well as some let farms. Traditionally, they have been run as part of the estate enterprise. If money has come in from timber, it has been taxed, and probably under schedule D. But that has hardly been the centre part of the activity. We are anxious that legitimate and public purposes, which, in many instances, are recognised by the heritage arrangements now in place, are not frustrated by the change.

The third subset of concern is that of existing woodland owners, which will often be the same as that of the traditional estate owners already mentioned. Those with a predominantly broadleaved species wood that is now 30 or 40 years old may be 50, 60, 70 or even 100 years away from commercialisation of that property. They cannot possibly obtain planting grants on the old or the new scales because the woods already exist. They will not get a commercial return for at least two generations and they face the considerable costs of running the wood for the time being. Those costs include thinning, pruning, maintenance of fences, anti-deer precautions and precautions against grey squirrels, which are extremely important in broadleaved woods.

I emphasise again that the main thrust of our concern is towards broadleaved woods because of their long timespan and the difficulty of making anything of them at the best of times, and certainly in the short term. However, the amendment is not confined to broadleaved trees, important though they are, because there are also significant forestry interests.

Those of us who have begun to learn a little about trees in the recent past have become aware of the need for much more active silvicultural management than has traditionally been practised in this country by, for example, the Forestry Commission. It is no use just shoving the trees in and coming back 60 years later to see whether they have grown. We must be prepared to do pre-commercial thinning, early pruning and so forth, which cost money. It is not easy to carry out those activities without some acknowledgement of running costs and some cash flow.

I have adverted briefly to New Zealand and will do so just once more. New Zealanders practise very active silviculture and prune more than any other country. They produce some of the highest quality commercial softwood timber, and we could do the same if we were prepared to put the effort into management. I fear that in commercial forestry the scales will be tipped against us and that in traditional broadleaf forestry many estates will leave their woods to carry on as they are in the hope of getting a bit more out of them one day.

In introducing the amendment, I must make it clear that there is no question of grants exceeding 100 per cent of the costs of establishment, which rather gives the lie to what Opposition Members said in an earlier debate. The costs extend over perhaps a 10-year period before the weeding and brushing off are done and the trees are fairly launched on their future career. My understanding of the planting scheme is that roughly 55 to 60 per cent of establishment costs will be met by the new grants, leaving about 40 per cent in the planters' hands. That result may be right, but it means that planters will have to find subsequent expenditure on maintenance out of their capital, with a long timespan still to go.

Amendment No. 251 is rather long, but its effects would be relatively straightforward. It may be wise if I first give an estimate of cost. On the basis that the abolition of schedule B will yield £10 billion a year, or that it will build up to such a yield, we estimate that my proposals would cost about £2 million per annum, which we regard as a very limited relief. All reliefs must be carefully considered and justified, but we consider that this is a sensible way to achieve our objectives.

Paragraphs (1) and (2) of the amendment would introduce the new relief on 6 April 1988, but it could not be claimed in any year to which the proposed transitional arrangements applied. Under paragraph (3), which contains the substantive point, the excessive expenditure incurred over income and grants could be set off against any schedule A income from agricultural property or farming income. I shall return to this aspect later. The set-off could not create a loss. We are not in the business of reintroducing the old tax reliefs or tax shelters.

Paragraph (5) of the amendment would define "qualifying expenditure" and "agricultural income". The concept is established in revenue law. The proposals would mean that losses could not be set off against other forms of income such as television appearance fees or pop star appearance money. It would not be of any significant benefit to absentee owners or to commercial woodlands. On reflection, I would be prepared to consider a definition which confined it to land occupied as part of an agricultural estate, so there would be no question of buying a free-standing forest with which one had no local connection. We want to avoid that kind of weakness.

9.30pm

I hope that my right hon. Friend the Financial Secretary will consider the genuine economic problem of such a planting effort, especially for the broadleaves and the lowlands, because of the long lead times involved between planting grant and commercialisation. I hope that he will examine our proposals with an open mind and be ready to consider all representations, bearing in mind that they have the bulk of forestry opinion behind them. If possible, I hope that he will give an assurance that he will reflect carefully on this matter, tune up the new proposals and improve them in good time, well before the end of the transitional period.

Mr. Chris Smith: The amendment moved by the hon. Member for Daventry (Mr. Boswell) was proposed by the Country Landowners Association and the Historic Houses Association, among others. The Opposition have no objection to the principle of ensuring and facilitating the good and sound management of existing woodlands, which is the stated aim of the amendment, but we do not believe that introducing a further tax relief schedule is a sensible way of going about it.

[Mr. Chris Smith.]

We have two specific complaints about the amendment. One has already been touched on by the hon. Gentleman himself. As the amendment stands, a farmer farming in Gloucestershire would be able to claim relief against the establishment of woodlands in the Flow country of Caithness and Sutherland. That is not the purpose of the amendment, but it is an effect that we could not possibly support. In addition, the effect of the amendment is not tailored to maintenance operations but would include other forestry operations such as planting. That is not an effective targeting of the proposals. We should prefer a proper grant system for the good, sound maintenance of existing woodlands, especially to help farmers with small areas of woodland and the owners of properties with woodlands attached to them. The amendment is not a sensible way of going about that.

Mr. Lamont: My hon. Friend the Member for Daventry (Mr. Boswell) has identified the problem of maintenance. He is saying, in effect, "You have taken them out of tax—that system is equitable and you have given planting grants, but how is the single forester or the small person not part of the large estate to deal with the cash flow problem of maintaining the estate?" I remind my hon. Friend—not that he needs reminding—that the unsatisfactory feature of the present situation is that it allows full tax relief for expenditure while not imposing any tax charge on profits. My hon. Friend's proposal would structurally cut right across the solution that we have adopted. That is not acceptable.

I have some sympathy with the point made by the hon. Member for Islington, South and Finsbury (Mr. Smith). If there is a problem with maintenance it would probably be better tackled through the grant system. My hon. Friend the Member for Daventry (Mr. Boswell) is well aware that part of the grant provision that we have introduced is for maintenance and that some of the largest maintenance costs in the life of a tree occur in the early years. That is catered for in the existing grants.

I am not saying that the solution that we have arrived at must endure for ever, but we want to see how the changes that we have made work out. I understand that the problem of maintenance and yearly upkeep worries people, but the amendment cuts across the tax changes that we have made and there are other ways of tackling the problem. Nevertheless, we will bear it in mind and examine the effects.

Mr. Boswell: I am grateful to my right honourable Friend the Financial Secretary for his comments and in no sense am I setting myself against those of the hon. Member for Islington, South and Finsbury (Mr. Smith). The important point is that the Committee sees that there is a problem. My right honourable Friend has said that he is prepared to consider the matter, but I am still concerned about the timescale because there was some implication that this would have to wait until the new arrangements were firmly in place. That is for interpretation, however, and I hope that my right honourable Friend will be able to consider representations from all sides in the interim period before the transitional arrangement applies. Subject to that and the spirit of my right honourable Friend's comments, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Schedule 6, as amended, agreed to.

Clause 64

COMPANY RESIDENCE

The Paymaster General (Mr. Peter Brooke): I beg to move amendment No. 281, in page 61, line 6, leave out "Tax" and insert "Taxes".

The Chairman: With this it will be convenient to take Government amendments Nos. 282 and 285.

Mr. Brooke: These are minor amendments intended to put beyond doubt that the provisions of clause 64 apply for all purposes of the Taxes Acts including the Taxes Management Act 1970.

Amendment agreed to.

Mr. Gordon Brown (Dunfermline, East): I beg to move amendment No. 319, in page 61, line 8, at end insert—

"(1)(A) A company, whether or not incorporated in the United Kingdom, which is not ultimately managed and controlled in the United Kingdom shall, in respect of business activity conducted in the United Kingdom of a type specified in Regulations to be made by the Board and subject to an affirmative resolution of the House of Commons be within the charge to corporation tax on income and gains arising directly or indirectly from such activity.

(1)(B) The Regulations referred to above shall have regard to the scale of investment and related activity conducted in the United Kingdom by non resident entities and their influence on specific areas of economic activity in the United Kingdom.".

The amendment seeks to draw attention to anomalies that we believe are at the heart of the taxation system for non-resident companies. I say immediately that we accept the general point behind the Government's proposal in clause 64 that companies incorporated in the United Kingdom should, for tax purposes, be regarded as resident in the United Kingdom. We hope that the Minister will accept our amendment to advance the date on which that will happen and thus minimise the scope for tax avoidance by companies which would otherwise immediately be affected by the clause.

Amendment No. 319 seeks to draw attention to the anomalous treatment of three types of non-resident companies. First, there are non-resident companies which are commercial operations and deemed to be trading operations, where tax is paid both on income and on capital gains if trading through a branch in the United Kingdom. Secondly, there are non-resident commercial operations which are deemed to be investment operations, subject only to income tax at the basic rate and not subject to corporation tax, and which as a result have differential advantages.

Thirdly, there is the special type of operation—I hope that the Minister will use this opportunity to answer

questions about this—with sovereign immunity, which is enjoyed by non-resident commercial operations and about which there is much concern.

The distinction between trading operations and investment operations forms part of our concern in moving amendment No. 319. Although there is plenty of case law surrounding the distinction between trading and investment, the distinction becomes more blurred when we examine share operations. There is absolutely no doubt that a company which actively deals in shares may be deemed to be investing in those shares and thus escape liability for corporation tax on its capital gains. This is not purely a problem that affects non-resident companies. We believe that the time is ripe for a review to end a practice that has caused a considerable loss of revenue to the Exchequer.

Secondly, I wish briefly to express our concern about non-resident commercial operations which are covered by sovereign immunity. While a number of organisations or Governments may be covered under the term sovereign immunity, it is clear to us—and to everyone else—that the scale of operations involved in the Kuwait Investment Office is such that some action needs to be considered. The Kuwait Investment Office is said to have a £15 billion share portfolio in the United Kingdom. It has stakes in 30 or more companies amounting to 5 per cent or more of the share capital as well as stakes in a large number of other companies. It has a property arm and trades on the stock exchange, both buying and selling. In the famous Exco case £6 million was made in a period of a few days. Also, of course, there is the major investment in Britain's largest company—British Petroleum—in which the Kuwait Investment Office now has a 22 per cent stake.

It is reported that the profits of Kuwait Investment Office operations in the United Kingdom amounted to more than £1,000 million last year. It is further reported that the tax due on dividends alone should have been £250 million or more, but that no tax is paid due to sovereign immunity. It is ironic that the Government's failure to close this tax loophole in a Budget that was supposed to close tax loopholes means that the biggest beneficiaries of the Budget are not the British people, no matter how rich, or even the Kuwaiti people, but the Kuwaiti royal family who pay no tax on their dividends and no corporation tax on capital gains made by dealing on the stock exchange.

The question is whether sovereign immunity should extend to what is clearly a commercial operation. Sovereign immunity as we understand it has no basis in international law or in statute. It is a concept based on reciprocal arrangements between countries and thus on good will, but it was developed in the 19th century for circumstances entirely different from those which govern the highly commercialised, active and aggressive operations of the Kuwait Investment Office. Sovereign immunity appears to give the Kuwait Investment Office exemption from tax on dividends gained from its investments in the United Kingdom. As the tax paid is refunded, the Minister must be able to tell us the amount involved. Sovereign immunity also gives the Kuwait Investment Office exemption from corporation tax on capital gains. In other words, the Kuwait Investment Office has advantages which are available to no other non-resident commercial organisation that we can detect and which are far superior to those available to any British company or investor.

The main advantage to the Kuwait Investment Office has been in the past few months. The end result of the fiasco over the British Petroleum sale is that the Government spent £18 million on advertising and £73 million in underwriting fees, only to hand over most of the shares that were on offer to the Kuwait Investment Office. The Government then had to pay back the £30 million tax paid on the first instalment of dividends to the Kuwait Investment Office. The net result was not just the transfer of a company in public hands to private hands but from British to foreign hands. As a result, no tax will be paid on dividends and if the shares are sold no corporation tax will be paid either. That could affect not just BP but other privatisation issues. Whereas it is possible for investors in this country to buy shares offered at knock-down prices, British investors and British companies cannot buy shares at knock-down prices—for example, in the electricity industry when it is sold—and escape paying tax on the dividends and on share transactions.

9.45 pm

It is clearly in the national interest that that should not continue. The Minister must answer the following questions today. What are the criteria whereby sovereign immunity is granted? Where is the dividing line between the activities of a state and those of a highly commercialised operation which is clearly the equivalent of a multi-national holding company? Who monitors the activities carried out under sovereign immunity? We know that BP shares were bought by the Kuwait Investment Office, that the Treasury met Kuwait officials and that on 28 January the Chancellor met the Kuwait oil minister. Was sovereign immunity and its continuation any part of those discussions? Given that Kuwait bailed the Government out and saved the Chancellor's face, the Paymaster General should tell us today whether sovereign immunity was discussed, what was agreed, and what has been the result.

The benefits of sovereign immunity to a few people and organisations have been great and they seem to be given on a far more flexible basis in Britain than in other countries. We do not suggest ending a situation where there is scope for sovereign immunity and for reciprocal agreements to be made, but when clearly commercial operations are making profits out of activities in the United Kingdom we should operate the practice which appears to be current in the United States of America, where such commercial operations are deemed to be commercial and taxed appropriately.

The Paymaster General may say that because sovereign immunity has lasted 70 or 100 years or more this is not the time to do anything about it, but it is because it has lasted so long that it is no longer a suitable instrument to deal with the commercial operations of a highly aggressive multi-national holding company in the United Kingdom. He may say that no previous Government acted on this, but it is only now that the scale of the operations and the losses involved to the Exchequer have become known. For those

[Mr. Brown.]

reasons, any Government concerned about equity should act on the matter immediately.

We know that £250 million or more may have been lost this year in advanced corporation tax on dividends alone. The total may be more than £1,000 million just for the 1980s. We also know what that money could do in employing nurses, building hospitals, repairing schools, improving our welfare state and avoiding social security changes. All the cuts could have been avoided if we had received that taxation revenue this year.

Mr. Butterfill: Has the hon. Gentleman made an estimate of the benefit that may have accrued to the United Kingdom economy as a result of the billions of pounds of investment made by the Kuwait Investment Office and how many jobs may have been created by that investment?

Mr. Brown: I hope that the Minister will answer that question. If Britain's future is to be based on giving tax immunity to commercial operations in this country, the Exchequer will be extremely poor. I estimate that, for the £1,000 million that we may have lost in tax revenues during the 1980s, the Government could have created many jobs, particularly in the National Health Service and in education.

We are continuously told that the Bill seeks to simplify taxation and to stop tax loopholes. That is one tax loophole that the Government are duty-bound to examine, now that it has been mentioned. In Spain, where the activities of the Kuwait Investment Office are being monitored, action is already being taken. The Government owe the Committee an explanation of what has happened, a commitment that they will examine what has gone wrong, and an explanation of what they will do to resolve such problems in the future. I hope that the Minister will respond favourably to the points that we have raised, as the matter affects large tax revenues which should be available to the British people.

Mr. Andrew Smith (Oxford, East): In concurring with the comments of my hon. Friend the Member for Dunfermline, East (Mr. Brown) in support of the extension of tax liability to companies incorporated in this country, I shall speak principally in support of the amendment. It proposes that companies carrying out business here, but not incorporated, managed or controlled here, should be liable to corporation tax on the profits arising from their activities.

As my hon. Friend said, and as revealed in *The Sunday Times*. Insight article last Sunday, which has done us all a service, it is scandalous that organisations like the Kuwait Investment Office, which operate under liberally interpreted and out-dated sovereign immunity conventions, can rip off the British taxpayer and the public services for which he pays.

The sums involved are very large: an estimated £250 million each year in advance corporation tax is paid back to the Kuwait Investment Office, and a further £260 million worth of capital gains tax each year are not paid. As my hon. Friend the Member for Dunfermline, East said, it is a commercial organisation with a total portfolio in this country of some £[illegible] billion and annual profits estimated at between £1,000 billion and £1,500 billion.

It is equally scandalous that the amount that that is costing the country has not yet been made known. How many other overseas Governments' organisations, royal families, sheiks and assorted potentates are on to that massive rip-off? The Committee, the House and the general public have a right to know how much it is costing us. I believe that some Conservative Members will support our demand that that drain on the public purse be identified, quantified, itemised and stopped.

How much is sovereign immunity costing the country in repaid corporation tax advance payments and foregone capital gains tax? Furthermore, how is that amount broken down between what might be described as genuine governmental organisations and commercial front organisations, such as the Kuwait Investment Office?

As my hon. Friend the Member for Dunfermline, East said, this country is particularly liberal in its interpretation of the sovereign immunity convention. Bodies such as the Kuwait Investment Office are, by no stretch of the imagination, anything other than commercial organisations. As such, they should be assessed and taxed on the same basis as commercial organisations incorporated here. They should not be able to hide behind an interpretation of sovereign immunity, which would not stand up in other countries. It does not stand up in the United States, where the internal revenue service has made it clear that it distinguishes between Government organisations that are in for a profit and those that incur a profit on genuine business. There is no reason why Britain cannot do the same. At the moment we are a soft touch and that cannot be allowed to continue.

Sovereign immunity has a totally unacceptable effect on revenues and public expenditure in terms of National Health Service employees, hospitals, schools and housing. It also distorts the market in equities if the playing field is slanted in favour of a few selected and, indeed, self-selecting players. It has dire implications for the control of British industry when an organisation such as the Kuwait Investment Office has shares of between 5 per cent and 25 per cent in 30 or more British companies. Unless the Government can assure us that they will plug the glaring anomaly, we must conclude that this is the cut-price coupon on their "Britain for sale" policy.

The hon. Member for Bournemouth, West (Mr. Butterfill) asked about the gains. If hon. Members take that view, why do we not extend the cup-price coupon to everybody? Why not let everybody come and escape tax?

Mr. Butterfill: I do not think that anyone is seriously suggesting that sovereign immunity should be extended. Indeed, I am sure that many Conservative Members will sympathise with the proposition that it should be examined closely to find whether it benefits the country or whether it is a cost to the British public, as the hon. Gentleman suggests.

It is right that the hon. Gentleman should ask questions, but I take issue with his suggestion that sovereign immunity should be stopped in all cases. Some considerable benefits have or may have derived from the continuation of the policy. If, on balance, it can be shown to have been beneficial to the British public, it would be like shooting oneself in the foot to change it merely for the sake of the principle that the hon. Gentleman espouses.

Mr. Andrew Smith: I look forward to the hon. Gentleman and his honourable Friends supporting our amendments. I did not say that it should be abolished completely.

[*Hon. Members: "You did".*]

No, I did not. I said that we must differentiate between genuine governmental organisations, which incidentally realise profits and those that are clearly in it for commercial gain. I pointed out that if the United States and our other industrial competitors can do it, why can we not do it? Given the scale of the tax-free profits being made by the Kuwait Investment Office and the many others that we do not yet know about—we are only scratching the surface of this issue—the Minister owes it to the Committee and the House to tell us the cost to the British taxpayer. The scale of the handouts to very powerful, wealthy international organisations is totally and rightly unacceptable to the British public. They will demand with us that the Government act now.

Mr. Campbell-Savours: It will be interesting to know whether any aspects of the Al-Fayed tax affairs are linked to the principle of sovereign immunity. That would answer the questions being put by Mr. Tiny Rowlands in his articles in *The Observer*. He maintains that sovereign money was used to purchase Harrods. We must be indebted to my hon. Friend the Member for Dunfermline, East (Mr. Brown) for tabling the amendment, because it gives us the opportunity to discuss not only the Kuwait Investment Office but other issues that are worrying hon. Members.

It is significant that the Kuwait Investment Office is not resisting the suggestions made in the *Sunday Times* article. The Kuwaitis may think that they are having a pretty good time at Britain's expense. They may now accept that the game is up and that it is time that they paid their dues to society. I should not be surprised if they had someone present at our proceedings today, as they knew that my hon. Friend was tabling the amendment and was likely to raise that matter.

It may also be that when the BP share flotation was seen to be at risk in its early days, the Chancellor or his officials gave a nod and a wink to the Kuwait Investment Office. It may have been suggested that if they picked up those shares to prevent the bottom falling out of the market, and therefore to prevent the Bank of England from having to move in with the floor price, no movement would be made on that front during this financial year or for several future financial years.

10 pm

I do not expect the Minister of State to give me an answer to that question tonight, but it may well have been a consideration in their minds when they moved in to save the Government the embarrassment of picking up BP shares in a collapsed market when that flotation took place.

I refer now to an issue that I raised immediately prior to the recess—the issue of Westminster cemeteries and its links with matters that we are debating today. The clause deals with the migration of companies, and the amendment tabled by my hon. Friend the Member for Dunfermline, East is one on which I can safely raise the issue of Chelwood Holdings Ltd., a company which I might say fits the Bill. The amendment says:

> "A company . . . not incorporated in the United Kingdom, which is not ultimately managed and controlled in the United Kingdom shall, in respect of business activity conducted in the United Kingdom of a type specified in Regulations to be made by the Board and subject to an affirmative resolution of the House of Commons be within the charge to corporation tax on income and gains arising directly or indirectly from such activity."

I can inform the Committee that Chelwood Holdings is precisely such a company.

I want to draw the attention of the Committee to the activities of Chelwood Holdings and to an interview between a journalist on the *Guernsey Evening Press and Star*, Mr. Timothy Earl, and Mr. Rodney Hylton-Potts, a solicitor acting for Chelwood Holdings. I have a transcript of the interview, which took place on 1 June at 3.30 pm. The conversation went as follows:

> "A company bought some cemeteries for 15p, Chelwood"—

that is, the company that bought the cemeteries after they had been purchased from Cemetery Assets UK, which in turn had purchased them for 15p from Westminster city council—

> "bought them for a very substantial price"—

the 15p cemeteries were sold collectively for £1 and were sold by Chelwood for £300,000—

> "and just sold them on to a somebody called Wisland".

[*Interruption.*]

This is real. Wisland is registered in Panama and trades in Switzerland. I am sure that it fits the amendment very neatly—

> "and the only involvement of the Jersey people is the normal running of an offshore company in a nominee capacity".

Mr. Hylton-Potts was asked.

> "Does that go for all the Jersey people?"

He said: "Yes" and was asked: "Including Mr. Hurley?"

Mr. Hurley was the person who owned 94 per cent of the shares in Chelwood Holdings. He was the man whom I indentified on an earlier occasion as the beneficial owner of the cemeteries which cost 15p and were sold to him for £300,000. I must apologise to the Committee and confess that I was wrong. Mr. Hurley

[Mr. Campbell-Savours.]

appears not to be the beneficial holder. He was simply a nominee, and behind him lurks another person. That person is a resident of the United Kingdom who sought to arrange his affairs so that he would avoid paying a very substantial amount of money. During the course of the conversation, Mr. Hylton-Potts said:

"What is quite clear is that Mr. Hurley was not benefiting. All he was doing was doing his boring routine job running a company which I expect he does for 1,000 clients. That's all it is."

Those 1,000 clients will be the very companies which fit so neatly in the amendment moved by my hon. Friend the Member Dunfermline, East. The transcript continues:

"I do not know why that is. You will have to ask him. It is a good point actually please ask him. We just run these for clients and we leave it to the Jersey Trust Company and lawyers just to get on with it."

Later in the interview he said:

"I don't act for Mr. Hurley but he has got nothing to worry about"—

That was after the Inland Revenue investigation which the Minister referred to on a previous occasion, was drawn to his attention—

"because he did not make anything out of it. It is nothing to do with him. He just ran a company on a nominee basis so it is all a bit of a damp squib. You must print whatever you think print-worthy".

Mr. Hylton-Potts was asked:

"Do you know if the company is a Corporation Tax company"—

Now we are getting to the hub—

"or does it pay normal tax?"

He replied:

"I think from memory, and it is from memory, it is an offshore . . . It is one of these companies which pays £500 a year."

The transcript continued:

"Ah that is Corporation Tax."

Mr. Hylton-Potts said:

"Yes. I think that is what it is, there are lots and lots of them."

When asked who the beneficial owners were, he replied:

"Of course not. What a funny question. Of course I can't, I'm a solicitor but it certainly isn't Mr. Hurley. He's a nominee."

These people in Guernsey seem to run businesses selling shell companies to any Tom, Dick or Harry from the United Kingdom wanting a quick tax dodge. In this case, the tax dodge was on a capital gain of £900,000 which took place within a matter of days. Will tax on that £900,000 be paid by anyone linked with Chelwood Holdings? It may seem a lot of money, but it was only part of a transfer pricing transaction. Chelwood Holdings then sold on the cemeteries for £1.25 million to the company called Wisland from Switzerland. We do not know who the beneficial owners of that company are. Wisland has placed a value of between £5.5 million and £10 million on the cemeteries. Now that Westminster city council has decided to repurchase the cemeteries, it may have to pay between £5.5 million and £10 million for them.

Chelwood Holdings, a company registered in Guernsey, has made a capital gain of £900,000, yet it will not pay the princely sum of £500 corporation tax on it. A company in Switzerland will then make another £5 million or even £9 million out of it. I cannot imagine how much tax that compnay will pay—probably nothing at all. The people who will lose out will be people like me, the poor ratepayers of Westminster. My rates bill will have subsidised this negligence by Lady Porter and her acolytes on Westminster city council.

We should have answers to these matters tonight. If the Minister cannot give us answers, the Committee should accept the amendment moved by my honourable Friend the Member for Dunfermline, East. At least it would give the British taxpayer an opportunity of seeing such profits repatriated.

If the Minister will not accept the amendment and the Committee, by majority, also refuses to accept it, perhaps he will consider the following proposition. The Minister might seek to interview, by agreement, those people whom I identified on a previous occasion—Mr. Ernest Francis Hurley, who is the 94 per cent nominee owner of the company, Miss Marie Moss, Mr. Stephen Sydney Moss, Miss Joan Margaret Hurley or Miss Jane Elizabeth Hurley. All of those people are nominee directors of the shell company that made a substantial profit. The Minister might ask them straight out to tell us who the beneficial owner of the cemeteries is today. The ratepayers in Westminster desperately want to know. They want to know where the money has gone, and why someone can be allowed to make such a substantial profit, while the Government, in this case, open up the doors to even further abuse, by removing the permission required from the Treasury for migration of companies. I think that there may be a link between the case that I put tonight, and the original proposition in the clause.

The individuals in Guernsey who are being used by British tax dodgers must understand that their responsibility goes far wider than Guernsey, that they are being used, and that the people of Britain object.

A report has been produced by the States Financial Services Commission, which sat in Guernsey to consider these matter. It resolved to take no action. It gave some lame excuse on the basis that it has no right to restrict the operation of companies operating within its territories. That Commission has a great responsibility to the British public. Those individuals in Guernsey have no right to offer themselves up in that way, when the British taxpayer, and in this case, the British ratepayer, lose out.

Mr. Alistair Darling (Edinburgh, Central): I thank the Committee for its good wishes earlier, and in recognition of that, I shall be brief.

Our amendment goes to the heart of a problem that faces Britain—the temptation, which the Government encourage, for companies abroad to make raids on the British economy, and also, for people who were based in Britain to move abroad to operate, so that they do not have the disadvantage of paying tax here. The problem raised by my honourable Friend the Member for Workington (Mr. Campbell-Savours) seems to highlight that point. I declare an interest as a ratepayer in Westminster, and I wish my honourable Friend well in his inquiries. I say only that if Westminster was a Labour-controlled authority, I am sure that there would not have been the same silence from the Conservative Benches.

Our problem is that people can hide behind the veil of corporate identity to carry out their various activities. Sometimes, it is difficult to see who is really hiding behind a front company. My honourable Friend the Member for Dunfermline, East (Mr Brown) has dwelt at some length on the operation of the Kuwaiti oil company and sovereign immunity. I hope that the minister takes those points seriously, because it would not take too much imagination for a country such as Switzerland—which appears to be operated for the benefit of the companies that function within it—to establish some sort of state company that might get the benefit of sovereign immunity to avoid paying taxes here. That is important when we consider Swiss companies' raiding activities in Britain.

My main point is about residence. It is becoming increasingly obvious that Britain is open to bids from companies based abroad. Because the seat of a corporation, the ultimate control, is abroad, Britain has no say in how companies that used to be based here are run. That means that the guts of this country are being controlled from abroad—sometimes thousands of miles away, and the Government seem content to let that happen.

There have been two newspaper articles recently. Sir Hector Laing wrote one in *The Times*. I do not usually praise him and Opposition Members do not agree with him about much, but he wrote an excellent article drawing attention to the fact that this country was being exposed to raids by companies—he referred in this case to the bid for Rowntree. He said that companies based abroad were able to operate with comparatively little control, and apparently little interest, from the Government.

Another article in the Lombard column of *The Financial Times* yesterday again emphasised that control was vitally important, especially if one was seeking to direct the way in which an economy develops or to control social conditions. I hope that the Minister accepts that our amendment was tabled in an attempt to get the Government to recognise that there is a genuinely serious problem that there has not been for a long time. We find that the country's affairs are being dictated behind either a corporate veil or, alternatively, a sovereign veil, and the Government seem happy to ignore that.

10.15 pm

Mr. Butterfill: Does the hon. Gentleman agree that it would be dangerous to allow xenophobia to run away with us, considering that in terms of external investment Britain is second only to Japan? In reality, the boot is very much on the other foot. We control many other companies in overseas territories. There would be a danger of recriprocal action being taken against us.

Mr. Darling: I am not xenophobic but I feel that it is only right that the Government of this country have control over the economic affairs of this country which, for example, means being able to maintain the major influence on, say, British Petroleum, our largest company. That is crucial. It seems to be the utmost folly to hand over substantial control to a sovereign company that has a vested interest in manipulating North sea oil prices to look after its investments and its oil elsewhere. Perhaps the hon. Gentleman will tell the Committee which other country is laying its cupboard open to raids by foreign predators. There is no chance of British companies going into Switzerland in the same way that Swiss companies are coming here.

Mr. Chris Smith: Would the hon Member for Bournemouth, West (Mr. Butterfill) like to draw hon. Members' attention to the information given in the Red Book at the time of the Budget, which revealed that because of the fall in the value of the dollar Britain's overseas investments fell in value by £20 billion during last year? Is that a sound investment for this country?

Mr. Darling *rose—*

The Chairman: Before the hon. Gentleman replies, may I remind the Committee that we are in danger of widening the debate far beyond the scope of the amendment. It deals with tax liability: we cannot debate wider issues tonight.

Mr. Darling: I fully accept your ruling, Mr. Hunt. My hon. Friend made a point and nothing further need be added. The amendment seeks to provide that the Government take action to ensure that people who operate and trade in this country render unto the Government what is due to them and do not shelter abroad. It is a problem that the Government seem extremely loth to tackle. When the Minister replies, I hope that he will show that he has more interest in the country's affairs, especially taxpayers' affairs, than his colleague the Chancellor of the Duchy of Lancaster has shown in protecting the country's industry. The policy seems to be, "Come and get us. We'll do nothing to stop you." It is high time that that policy was reversed because the repercussions will be serious not only in areas that are removed from the south-east of England, where it is already causing great damage, it will cause problems throughout the country. When that happens, we will be unable to resist anyone's advances because we will be weakened by so much of our industry—certainly its crucial parts—being controlled from abroad that we shall lay ourselves open to manipulation by anyone who is in a position to manipulate us.

Mr. Rhodri Morgan (Cardiff, West): I have been told by Front Bench colleagues that I will not get a share of the "short money" unless I keep my speech short. I do not know on what authority they say that. They may be being premature. I shall do my best to abide

[Mr. Morgan.]

by their instructions, which I am sure will be universally popular with the Committee.

As to the revelations about the Kuwait Investment Office, there appear to be four categories of Government investment in this country to which we must have regard. First there is the original and legitimate function of the Government. Incidentally, capital gains will arise: they will be small and incidental, there will be windfalls and occasional gains. No doubt we all agree that it is legitimate to exempt those on the basis of sovereign immunity. Therefore the question of their being taxable does not arise.

10.20 pm

Sitting suspended for a Division in the House.

10.35 pm

On resuming—

Mr. Morgan: Other activities that are not so legitimate have become a problem which all Members of the Committee must consider. Governments play the market in another country, and that is not a proper function of Government. We should all be shocked if the British Government were found to be playing the market with its own tax revenues, however gained. The hon. Member for Bournemouth, West (Mr. Butterfill) pointed out that the Government encourage British citizens to invest abroad to build up revenues against the day when North sea oil runs out, but we should be shocked if our own Government were building up direct holdings of securities, assets or properties in another country. If they did, they should pay capital gains tax and be good citizens of that country. Taxpayers in Britain would not be happy if they thought that the Government were using revenue in that way.

There is sometimes confusion about whether the Government or the ruling family are investing. The article in last week's *Sunday Times* brought out the fact that the Kuwaiti royal family, the Saudi royal family and the Brunei royal family which are the Governments in their countries, invest surplus money abroad. It is difficult to work out the correct parallel and judge whether our royal family—which is not the Government—plays the market in another country. If it does should it behave as a good citizen of that country and pay capital gains tax?

The Chairman: Order. The amendment is not about playing the market but about tax liability.

Mr. Morgan: I am sorry, Mr. Hunt, I made the point precisely several times that if the Government or ruling family of this country played the market in another country, taxpayers of this country, would think that they should pay capital gains tax according to the practices and rules of that country. I do not wish to cross swords with you on that, Mr. Hunt, but I made that point clearly.

Finally, the other form of activity which borders on illegitimate is when the ruling family of another country is worried that it may not remain in that position forever and builds up substantial holdi[redacted] in this country against the day when it might fall as a Government. That scenario is likely in the Middle East where Governments fall—Governments that appear to be run by impregnable royal families such as the Libyan royal family, but Libya suddenly became a republic. The fallen Government finds it very handy to have a pile of money in Monte Carlo, London or wherever. In those circumstances capital gains tax liability is absolutely necessary. It was not a problem before 1973 when oil revenues suddenly started massively to rise to 10 or 12 times what they were before, giving rise to the hoard of money available to ruling Governments or ruling families in other countries. Should they pay tax on the enormous oil hoards that they have accrued since 1973? It was not a problem before 1973 because the sums were insignificant. The Kuwaiti and the Saudi royal families were not fabulously wealthy before 1973. Their wealth came from the rise in the price of oil from 50 cents in the late '60s to $2.50 just before the July 1973 oil price shock, $10 after that, then $30 to $40. It is now falling to what we hope is the stable price of about $18.

That those massive cash imbalances are now available and should be taxable. Our amendment would make them taxable. There should be general agreement on both sides of the House, Back Bench and Front Bench, that it is time to solve the problem. We did not want to do it immediately after 1973 out of sheer funk that we might offend the wealthiest sources of hot money in the world. We needed that hot money more than they needed us and we were desperate that it should remain in Britain rather than go to France, Germany, Italy or the USA.

It is high time that we dealt with this major problem of the hoards of oil money built up by the ruling families of countries such as Brunei, Kuwait or Saudi Arabia—we make no comment on the regimes, areas they come from, how they got their money or why they are the ruling families—that does not matter. The point is whether that money should be taxable when it is invested in massive quantities in this country. That distortion of the international flow of money—some of it taxable, but in this case untaxable—must be stopped. We hope that we will get a hint from the Minister to satisfy the fundamental objections of probably 90 per cent of the people of this country about this money being untaxed. The Government must deal with that soon.

Mr. Butterfill: Whatever the merits and demerits of the issue of sovereign immunity, the amendment would cut right across the tax treaties that this country has with other countries and in so doing undermine the basis on which one country deals with another on tax matters.

In response to the hon. Member for Workington (Mr. Campbell-Savours), I am sure that I am speaking for the majority, if not all, of Conservative members in saying that we view with repugnance the possibility that a United Kingdom resident was hiding behind Mr. Hurley and thereby breaching our tax laws. We hope that if what the hon. gentleman said can be substantiated it will be thoroughly and enthusiastically

investigated and if wrong-doing appears to have been done [redacted] a prosecution will result. If a conviction occurs [redacted] sentence should be exemplary and a deterrent to all others who may be tempted to pursue that course.

Ms Hilary Armstrong (Durham, North-West): My question arises from a situation in my constituency which Conservative Members will find peculiar for a Labour Member. A Saudi prince has acquired a grouse moor in my constituency. I am worried about the extent to which sovereign immunity is being used and therefore tax exemptions are being given for what are essentially commercial transactions. How much money do the Government think is involved and to what extent is sovereign immunity being used in this country as a cover for other activities?

Mr. Brooke: The hon. Member for Dunfermline, East (Mr. Brown), in moving the amendment, said that the Opposition accept the spirit of clause 64 and applauded its instinct. I did not catch echoes of that in the speeches of his hon. Friends, some of whom suggested that clause 64 would make easier some of the things to which they were objecting.

I shall not dwell on the words

"whether or not incorporated in the United Kingdom"

which appear in the first line of the amendment. Instead, I shall concentrate on the non-resident aspect.

10.45 pm

The hon. Member for Dunfermline, East asked about the difference between trading companies which operate through branches and agencies, and investment companies. He is correct in principle, because investment gains are charged at the basic rate of income tax and not through corporation tax, but that is a general tax principle and not specific to the clause. The hon. Gentleman then raised the question of non-residents dealing in shares. Where a non-resident company is dealing in shares, its profits will count as income for tax purposes, and if it is trading through a United Kingdom branch or agency it will be liable to tax here. The borderline between dealing activities and investment activities depends on the facts of each case and, of course, the Inland Revenue looks carefully at the circumstances of individual companies.

When the hon. Gentleman spoke on the general subject of sovereign immunity, he asked about the criteria, the dividing line and who monitored it. The provisions for sovereign immunity are operated by the Board of Inland Revenue, based on legal advice on the application of international law. Ministers are not involved in decisions on individual cases. The hon. Gentleman then referred to American practice in these matters. Briefly, the United States exempts income that foreign Governments derive from investments in the United States, which could include investment in a large United States corporation. The United States does not exempt income from commercial activities or from a trading company which the foreign Government effectively control. In that respect, therefore, I do not disagree with the hon. Gentleman's analysis.

The hon. Member for Dunfermline, East went on to speak at some length, as did some of his hon. Friends, about the Kuwait Investment Office. I must make it clear at the outset that I am unable to enter into any discussion about the tax status or tax affairs of an individual taxpayer. It is clear from my dealings with other regimes in other parts of the world, to which the hon. Gentleman referred in passing, that the distinction as to the confidentiality of individuals' tax affairs does not necessarily prevail in other countries, but it is highly desirable that it should prevail in this country.

The hon. Gentleman drew attention to the fact that sovereign immunity is a concept of very long standing. It has its origins in the general principle of international law that sovereigns and the public property belonging to them are treated as being not subject to the municipal laws of foreign states. In accordance with that principle, the income, profits and gains of sovereigns, foreign states and integral parts of foreign Governments arising in the United Kingdom are immune from United Kingdom tax. Again, I think that I have common cause with the hon. Gentleman. So far as we can trace, most other European countries, together with the United States, Canada and Japan, acknowledge the general principle which the hon. Gentleman adumbrated and which I have expanded, although its application may vary and is often not expressed in tax statutes. The hon. Gentleman was right to say that it is expressed in a tax statute in the United States, but it is not commonplace for it to be addressed in tax statutes in other countries. Most major countries provide similar exemption for the investment income and gains of foreign Governments, so there is a reciprocal benefit to the United Kingdom in relation to our actions outside the United Kingdom.

In answer to the question put to me by the hon. Member for Oxford, East (Mr. Smith), the fact that this is an immunity from tax, rather than a specific statutory exemption subject to a claim, means that the tax consequences of sovereign immunity cannot be estimated. Much wider issues are involved. For example, in so far as the income concerned is interest on Government securities, it may be exempt in any event in the hands of a non-resident. A number of gilts are not subject to tax—an exemption that was supported by the Labour Government, as it has been by this Government—and the Bank of England believes that it can price them more finely as a result. More important is a consideration of the benefits to the United Kingdom economy generated by this form of inward investment. It is another example of the strength of our economy that such investment is attracted here.

The hon. Member for Dunfermline, East asked about the Government's basic attitude to sovereign immunity. As I have said, we benefit from sovereign immunity under other countries' tax regimes, including the management of the foreign currency holdings that make up our own Reserves. Foreign investment in the United Kingdom and through United Kingdom financial institutions is certainly of benefit to us. If the sovereign bodies operate in the United Kingdom via companies resident here, those companies will of course be taxed in the normal way. Sovereign immunity applies only to the dividends and interest remitted abroad.

[Mr. Brooke.]

The hon. Member for Dunfermline, East went slightly over the top both on the radio this morning and with some of his hon. Friends this evening in his desire to replay the issue of the BP flotation last year. I should not have thought that the Opposition would be particularly keen to return to that. I was out of the country at he time, so I had the pleasure of reading the exchanges as a continuous narrative in *Hansard* whereas others lived through them at intervals. I thought that the score was five to my right honourable Friend the Chancellor of the Exchequer and nil to the right honourable and learned Member for Monklands, East (Mr. Smith), who at one stage was reduced to being an apologist for Goldman Sachs. The hon. Member for Workington referred to a nod and a wink on the part of the Government.

Mr. Gordon Brown: Can the Paymaster General assure us that in no discussions involving the Treasury or the Chancellor of the Exchequer with any official of the Kuwait Government or the Kuwait Investment Office was the issue of sovereign immunity discussed?

Mr. Brooke: That is the question that the hon. Gentleman said that he would ask my right honourable Friend the Chancellor today, but my right honourable Friend is in Toronto. The hon. Gentleman said that he would ask whether continued exemption from tax was discovered when, to use his words, the Kuwait Government

"bailed out Mr. Lawson over the question of the BP shares".

It is outrageous to suggest that any official or Minister would discuss the matter with the Kuwait Government, and I deny the allegation totally and absolutely.

As for the question asked by the hon. Member for Oxford, East, I have explained why it is difficult to estimate the consequences of sovereign immunity. We do no keep separate figures for investments made by particular agencies or individuals.

The hon. Member for Workington took us yet again through the narrative of the Westminster cemeteries. As with the Kuwait Investment Office, I cannot comment on the affairs of an individual taxpayer but it is clearly a matter that should appropriately be followed up by the Revenue. I will ensure that the hon. Gentleman's comments are put at the Revenue's disposal. I give the hon. Gentleman that assurance.

Mr. Campbell-Savours: Will the Minister accept my proposition that Chelwood Holdings, will pay £500 corporation tax on a profit of £900,000 on Westminster cemeteries, whereas if Chelwood Holdings had been registered in the United Kingdom as a company its tax liability would have been nearer £250,000? Does the Minister accept that these people have fiddled the taxman out of £250,000?

Mr. Brooke: I said that I could not comment on individual cases, and it would be wrong for me to comment on the hypothesis that the hon. Gentleman puts to me, but the narrative that the hon. Gentleman described predated the Government's decision to change the consent procedures under section 482. It therefore occurred under the previous regime and not under the regime that we seek to change in the clauses. I put it to the hon. Members for Workington and for Edinburgh, Central (Mr. Darling) that clause 64 strengthens our regime in this matter rather than weakening it.

The hon. Member for Durham, North-West (Ms Armstrong), drawing on the case of a grouse moor, asked me the same broad question that the hon. Member for Oxford, East asked. I cannot expand on my earlier remarks.

Mr. Gordon Brown: Before the Paymaster General finishes, will he agree with us that sovereign immunity, as presently defined, gives the Kuwait Investment Office, and perhaps other commercial organisations, huge advantages and benefits which set them apart from ordinary British investors or foreign companies? Will he consider the practice that appears to function in the United States where commercial operations are separated from the direct activities of Governments and are therefore taxed?

Mr. Brooke: There are differences between our arrangements and those of the United States in many areas. We have reasons for doing what we do, just as they have reasons for doing what they do.

The hon. Member for Oxford, East said that if the Government would not act today all kinds of apocalyptic consequences would follow. I assure the Opposition that all aspects of the tax system are kept under constant review. We are dealing with a regime that has operated for 70 years, so that constant review has taken place under Labour as well as Conservative Administrations. I give a pledge that the matter will continue to be reviewed—

[*Hon. Members: "Five-nil again!"*]

—within the spirit of the monitoring by the Inland Revenue—which I described earlier.

Mr. Gordon Brown: I am grateful to the Paymaster General for agreeing with us on some important issues about sovereign immunity. He agrees that the Kuwait Investment Office and other organisations are liable to be subject to sovereign immunity and that the advantages are considerable—they would not have to pay tax on dividends or corporation tax on capital gains. He agrees that they have advantages which do not accrue to foreign companies, British residents, or British companies, but he refuses to agree that since the issue has been exposed and the facts have become clear he should take steps to examine or rectify the position.

The Paymaster General failed to deal with the question of the scale of losses involved. The Treasury clearly has the figures. If it has to refund advance corporation tax payments, it has the figures and it knows how much is involved. The Paymaster General also failed to deal with the question of British Petroleum, which he barely mentioned in his remarks.

Mr. Brooke: The hon. Gentleman says that I did not deal with British Petroleum. Is he continuing to press the allegation that he made on the radio this morning?

Mr. Brown: I am happy to accept the assurance that the Paymaster General made, even though he was not in the country when the matter arose, but there are considerable worries about what is happening to BP. If the Government were sufficiently anxious to refer the issue of BP ownership by Kuwait to the Monopolies and Mergers Commission—that is currently under discussion—they should also be anxious about the scale of dividends payments and, later, of capital gains to the Government of Kuwait. It is unhealthy that by selling BP shares to the British public the Government have ended up with them being controlled by the Kuwait royal family.

Mr. Morgan: Wider share ownership.

11 pm

Mr. Brown: The problem is that in future privatisations—electricity, for example—the Kuwait Investment Office may not only buy up shares at the knock-down prices available to everyone else but do so in the knowledge that it will not be taxed on any of the dividends and that if it chooses to sell the shares or to play the stock exchange with them it will not have to pay corporation tax on the capital gains. It is a serious matter that the power enjoyed by one investor to play the market—free from the responsibility of paying tax—is so great when set against other institutions, especially ordinary British institutions and British investors. We may face the possibility of an energy empire being built up by the Kuwait Investment Office, including not only huge stakes in British Petroleum—it already has 22 per cent in Britain's largest company—but the electricity industry and, by implication, nuclear power stations.

Spain has had to recognise the problem and to act. The United States of America is aware of the problem and has acted in the taxation of commercial organisations. Sovereign immunity is not available in the same form in other countries of Europe. Why do the Government cling to an old-fashioned concept of sovereign immunity which allows tax-free profits to be made by what are clearly commercial organisations acting under the umbrella of a state but effectively operating as multinational holding companies? From the information available to us, it seems that the scale of losses to the Exchequer is now such that any Committee member would be failing in his or her duty in not asking what the Government intend to do about this. Bland assurances about keeping the matter under review are simply not enough. We want an assurance from the Paymaster General—Conservative Members would do us and the country a service if they also pressed for this—that an investigation will take place and that, if necessary, urgent action will be taken to deal with a problem that costs our country millions of pounds and thus deprives vital social services of money which they urgently need.

Question put, That the amendment be made:—

The Committee divided: Ayes 14, Noes 21.

AYES	
Armstrong, Ms Hilary	Ingram, Mr. Adam
Battle, Mr. John	Marek, Dr. John
Brown, Mr. Gordon	Morgan, Mr. Rhodri
Brown, Mr. Nicholas	Quin, Ms Joyce
Campbell-Savours, Mr. D. N.	Smith, Mr. Andrew
Darling, Mr. Alistair	Smith, Mr. Chris
Griffiths, Mr. Nigel	Worthington, Mr. Tony

NOES	
Arbuthnot, Mr. James	Jack, Mr. Michael
Boswell, Mr. Tim	Lamont, Mr. Norman
Bright, Mr. Graham	Lennox-Boyd, Mr. Mark
Brooke, Mr. Peter	Maples, Mr. John
Butterfill, Mr. John	Nicholson, Mr. David
Carrington, Mr. Matthew	Stern, Mr. Michael
Coombs, Mr. Anthony	Taylor, Mr. Ian
Davies, Mr. Quentin	Wardle, Mr. Charles
Favell, Mr. Tony	Watts, Mr. John
Howarth, Mr. Gerald	Widdecombe, Miss Ann
Hunter, Mr. Andrew	

Question accordingly negatived.

The Chairman: I call Mr. Brown—that is, Mr. Nicholas Brown—to move amendment No. 320.

Mr. Nicholas Brown: It is for the convenience of the Committee, Mr. Hunt, that Opposition spokesmen are called either Brown or Smith. No doubt that concession will be welcomed by all.

I beg to move amendment No. 320, in page 61, line 10, leave out from "which" to end of line 14 and insert

"was not resident in the United Kingdom immediately before that date".

The Chairman: With this, it will be convenient to take the following amendments:

No. 244, in page 61, line 16, at end insert—

"(2A) In relation to a company which carried on business at any time before the date of the coming into force of this section and which either—

(a) immediately before that date was not resident in the United Kingdom and was resident in a territory outside the United Kingdom;

or

(b) ceases to be resident in the United Kingdom on or after that date in pursuance of a Treasury consent and becomes resident in a territory outside the United Kingdom,

subsection (1) above shall not apply.".

No. 318, in page 61, line 16, at end insert —

"(2) Subject to subsection (2A) below in relation to a company which carried on business at any time before the date of the coming into force of this Section and which was not resident in the United Kingdom immediately before that date subsection (1) above shall not apply until the end of the period of five years beginning with that date.

(2A) Subsection (1) above shall not apply in relation to a company which carried on business at any time before the date of the coming into force of this Section and which in pursuance of Treasury consent either ceased to be resident in the United Kingdom before that date or ceases to be so resident after that date.".

I should tell the hon. Member for Basingstoke (Mr. Hunter) that, through a printer's quirk, his amendment No. 244 does not appear on today's Amendment Paper. It has, however, been selected, and it has been reprinted and is available on the Table.

Mr. Brown: Amendment No. 320 is a probing amendment and we need not spend much time on it, provided that we get a candid answer from the Government.

Mr. Brown: It is for the convenience of the Committee that the Opposition spokesmen are called either Brown or Smith.

The purpose of the amendment is to delete the second part of this clause which sets out the five-year period of grace. Regardless of the argument over how long the period should be, why should it operate for those who are already non-resident and also spell out a mechanism whereby others can take advantage of it? Why should the deadline not come in sooner?

Mr. Hunter: With near-equal brevity I shall speak to amendments Nos. 244 and 318. The essential point of clause 64 is to widen the definition of a company resident for tax purposes. The counterargument is that the formula that is contained within the clause is widening that definition too far. I am sure that my right honourable Friend the Paymaster General will not equate brevity with flippancy, because he is familiar with the essential arguments following correspondence that he has had with the CBI and meetings that I understand have taken place between the CBI and the Inland Revenue.

It is fine to seek to eliminate the nowhere companies and to discourage those that pay no tax anywhere and are incorporated in the United Kingdom only to give them a cloak of respectability. It is extremely probable that the overwhelming majority of companies that are incorporated in the United Kingdom but are tax-resident overseas will, within five years, be able to reorganise their affairs and not suffer adversely from the demands of clause 64. However, some companies may not be able so to reorganise their affairs. They will incur commercial risks and financial costs and may in some instances incur adverse political repercussions because often they operate in parts of the world descending from colonial or even imperial days and have relationships with the Governments there. The essential argument is that as it now stands, clause 64 lacks that flexibility and sensitivity to account for companies incorporated in the United Kingdom and tax-resident overseas—especially where that is done by treaty or with Treasury consent—which will find reorganisation a burdensome task and, arguably, counter to their commercial interests.

Mr. Gerald Howarth (Cannock and Burntwood): I endorse the points made by my hon. Friend the Member for Basingstoke (Mr. Hunter). He is right to say that there is unanimity across the Committee about the need to tackle some of the abuses. May we point out to Opposition Members who huffed and puffed that, once again, it is a Conservative Government who tackle abuses? Socialist Governments had the opportunity when they were in power and were unable to take advantage of it. But in essence, there has been some agreement across the Committee about this measure.

However, as my hon. Friend said, some problems arise out of the drafting of clause 64 which unilaterally changes the tax residence of companies—most importantly, of those companies which have changed the residence by Treasury consent for perfectly sound commercial reasons. Those are not the companies that Sergeant Bergerac from Workington was talking about in terms of cemeteries, hidden bodies and all sorts of weird and wonderful conspiracies which are the meat of the hon. Member's life in this House. We are not talking about such companies. We are talking about perfectly respectable honourable companies which have sought and obtained Treasury consent to move their residence for tax purposes. It is undesirable that some of those companies incorporated here which are tax-resident elsewhere will now have their tax position changed in this arbitrary and retrospective way. I understand that there has not been much consultation with the companies affected although, as my hon. Friend says, there has been consultation with the CBI.

Many of those companies will have to restructure to avoid these unplanned consequences. In a number of cases that will be extremely costly. Some companies may not be able to reorganise in the way that is necessary to avoid being caught by the new resident definition and some may have to resort to legislation. As we have seen on the Floor of the House over the past couple of weeks certain difficulties are associated with getting private business through this place. For some perfectly respectable companies incorporated under royal charter the only means of coping with this change may be to resort to a private Bill and they may be unable to get it through the House because of pressure on time.

Opposition Members have suggested that somehow there is only one way in which this proposal could promote the national interest, and that is to close loopholes and all the rest of it. It is important to bear in mind the fact that there are severe implications for a number of British companies which are incorporated in the United Kingdom but which operate principally in other parts of the world, particularly Commonwealth countries where over decades they have managed to establish a relationship. By moving their place of incorporation they may not only endanger their relationships with those Governments but may have to give up their shareholdings to the local companies. That would not be in the overall interest of the United Kingdom taxpayer.

In conclusion, I hope that my right honourable and hon. Friends will give careful consideration to the amendment proposed by my hon. Friend the Member for Basingstoke. Unless they are prepared to do that there could be serious adverse effects for major British companies which make an undoubted contribution to the British economy.

Mr. Brooke: The hon. Member for Newcastle upon Tyne, East (Mr. Brown) drew attention to the fact that all hon. Members on the Opposition Front Bench are named either Brown or Smith. I notice that they all come from eastern constituencies: Newcastle upon Tyne, East, Dunfermline, East, Monklands, East and East Kilbride. A strong easterly wind blows.

Mr. Andrew Smith: The east is red.

Mr. Brooke: With regard to the amendment moved by the hon. Member for Newcastle upon Tyne, East, at present transitional arrangements apply to existing United Kingdom incorporated companies that were not resident in the United Kingdom on Budget day under the old rules, and to companies which migrate from the United Kingdom on or after that date with the consent of the Treasury under section 482 or its successor. The amendment would restrict the transitional arrangements to the first category only.

Although the section 482 consent mechanism for company migration is being abolished for the future, we believe that the Treasury should continue to process applications for consent to migrate, that were submitted before Budget day but not processed by then. If we simply withdrew the provisions for migration with Treasury consent for all purposes as at Budget day, it would represent an unfair denial of the legitimate expectations of companies which had applications in the pipeline. I therefore encourage my hon. Friends to resist the amendment.

My hon. Friend the Member for Basingstoke mentioned the group of companies which had already received consent historically under section 482 or its successor. As he said, under the Bill as it stands they would become United Kingdom-resident, as would all United Kingdom companies after five years from Budget day.

In this instance, I am also replying to my hon. Friend the Member for Cannock and Burntwood (Mr. Howarth). Ministers are aware of the concern that has been expressed about clause 64 that in certain cases it may be unreasonable to make existing companies United Kingdom resident when they are incorporated here but not resident under the previous rules. We are considering various aspects of this problem, to which my hon. Friend alluded. I think that it is accepted by those making the representations—my hon. Friend quoted the CBI—that any provision in this area would have to include some conditions covering those companies for which a case has not been made out. The CBI acknowledges that there is such a category.

We are considering the matter carefully and hope to bring forward an amendment on report.

Amendment negatived.

Mr. Nicholas Brown: I beg to move amendment No. 321, in page 61, line 15, leave out "five years" and insert "one year".

The Chairman: With this it will be convenient to take amendment No. 322, in page 61, line 15, leave out "five years" and insert "six months".

Mr. Brown: Again, these are probing amendments which set out alternative periods of grace. We want the Government to explain why they are allowing a period of five years. That is a long planning period and presumably will give companies seeking to take advantage of these provisions a long time to plan their affairs in such a way as to maximise the advantage to themselves and minimise the advantage to the Exchequer. We are concerned about that. I cannot easily believe that it is the Government's intention to provide a route for tax avoidance, so perhaps the Paymaster General will tell us precisely why the Government are doing this.

Mr. Brooke: Clause 64(2) provides special arrangements for companies incorporated in the United Kingdom before Budget day but not resident at that date under existing law. The hon. Gentleman seeks to shorten the transitional arrangements under which they would have the chance to reorganise their affairs on becoming again subject to our jurisdiction.

We consider it reasonable to allow a fairly generous amount of time for such companies to conduct their affairs. I do not know how many Committee members have been engaged in organising an international structure of companies—

[*Hon. Members: "Hands up!"*]

I speak with limited experience myself, but it is complicated trying to do that with one's left hand while running a business and continuing the main operations of the company. Therefore, very much in the spirit of the remarks of my hon. Friend the Member for Basingstoke (Mr. Hunter) on the last amendment, we regard five years as a sensible allowance for that purpose.

Mr. Nicholas Brown: That is a wholly unconvincing explanation. The Government are being extremely generous to people in that position. Nevertheless, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Amendments made: No. 282, in page 61, line 21, leave out "Tax" and insert "Taxes".

No. 283, in page 61, line 23, leave out from first "up " to end of line 24 and insert "outside the United Kingdom".

No. 284 in page 61, line 28, leave out from "of" to end of line 29 and insert "a person exercising functions which, in the United Kingdom, would be exercisable by a liquidator".—[*Mr. Brooke.*]

Mr. Nicholas Brown: I beg to move amendment No. 323, in page 61, line 29, at end insert—

"(4A) subsection (4B) below shall have effect in relation to a company which becomes resident in the United Kingdom by virtue of subsection (2) or (3) above.

(4B) Where this subsection applies the company becoming resident in the United Kingdom shall not for any accounting period ending within the period of six years commencing with that event be:

(i) treated as a member of a group for the purposes of Chapter IV, Part X of the Income and Corporation Taxes Act 1988;

(ii) treated as a subsidiary for the purposes of S240 of the Income and Corporation Taxes Act 1988;

(iii) treated as a paying company for the purposes of S247 of the Income and Corporation Taxes Act 1988;

(iv) treated as a member of a group for the purpose of S273 of the Taxes Act 1970.".

[Mr. Nicholas Brown.]

I expected more cheerful "ayes" on the last amendment, but Committee members sounded disgruntled. We would not want defective legislation to become law.

Amendment No. 323 is more significant than the probing amendments that I discussed previously. It accords with the spirit of the clause as it seeks to block areas that we have identified as loopholes. I hope that the Governement will welcome our endeavours, which are intended to sit alongside what they proclaim to be their own. The Paymaster General may say that there is an imperfection in the way in which the amendment is drafted, and that the Government will cover the same point with the skills of the parliamentary draftsman. If so, we shall accept that, as we want the Government to accept the principle and are not concerned about the niceties of parliamentary draftsmanship.

The amendment deals with three issues. The first is the situation of a non-resident subsidiary company in a tax haven, which may have managed to gain a substantial pool of untaxed profit. We understand that if that subsidiary wants to repatriate capital by way of dividend, the dividend will be subject to corporation tax. Under the clause, however, because the subsidiary company is United Kingdom incorporated that money could simply be shipped back into the British tax net in five years' time. Could it not then be paid up entirely free of tax if the company made an election under section 247 of the Income and Corporations Taxes Act 1988? The amendment would prevent that from happening for the next six years.

The second isssue is trading profits and group relief. If an organisation brings back to the United Kingdom a net loss from a trading operation overseas and elects to use that loss against its United Kingdom profits, it would deprive the Revenue of tax due.

Thirdly, an offshore organisation may own assets which are expressed as capital losses off its trading profit or group relief. If it re-imports those into the United Kingdom and matches them against profits here, it would again deprive the Exchequer of tax due.

I have outlined our method of blocking those three loopholes and I look forward to hearing how the Government intend to deal with them.

Mr. Brooke: Under clause 64(2), United Kingdom incorporated companies which were not resident in the United Kingdom immediately before Budget day will become resident here after a five-year transitional period. Under clause 64(3), they will do so at an earlier date if they transfer their central management and control to the United Kingdom before then. An ample transitional period is necessary to allow companies to reorganise if they wish, and we shall look sympathetically at any types of company on which the provision may bear unduly harshly. Once resident, however, such companies should be treated exactly like all other United Kingdom resident companies. It is thus unreasonable to deprive them of the normal reliefs given to United Kingdom resident members of groups.

The hon. Member for Newcastle upon Tyne, East (Mr. Brown) referred to loss importation. I am not hiding behind the observation that the amendment is defective, but if its purpose is to discourage loss importation it is defective because it is not directed at companies which are not United Kingdom incorporated and which might seek to become resident in the United Kingdom to have their losses relieved here. There is at present no intention to legislate on the wider issues of loss importation as there is no evidence of a substantial increase in its incidence but, in familiar words, the Government will keep the matter under review.

Question put, That the amendment be made:

The Committee divided: Ayes 15, Noes 22.

AYES

Armstrong, Ms Hilary	Ingram, Mr. Adam
Battle, Mr. John	Marek, Dr. John
Brown, Mr. Gordon	Morgan, Mr. Rhodri
Brown, Mr. Nicholas	Quin, Ms Joyce
Campbell-Savours, Mr. D. N.	Smith, Mr. Andrew
Darling, Mr. Alistair	Smith, Mr. Chris
Griffiths, Mr. Nigel	Worthington, Mr. Tony
Henderson, Mr. Doug	

NOES

Arbuthnot, Mr. James	Jack, Mr. Michael
Boswell, Mr. Tim	Lamont, Mr. Norman
Bright, Mr. Graham	Lennox-Boyd, Mr. Mark
Brooke, Mr. Peter	Maples, Mr. John
Butterfill, Mr. John	Mitchell, Mr. Andrew
Carrington, Mr. Matthew	Nicholson, Mr. David
Coombs, Mr. Anthony	Stern, Mr. Michael
Davies, Mr. Quentin	Taylor, Mr. Ian
Favell, Mr. Tony	Wardle, Mr. Charles
Howarth, Mr. Gerald	Watts, Mr. John
Hunter, Mr. Andrew	Widdecombe, Miss Ann

Question accordingly negatived.

Amendment made: No. 285, in page 61, line 30, after first "section", insert—

" 'the Taxes Acts' has the same meaning as in the Taxes Management Act 1970;".—[*Mr. Brooke.*]

Mr. Hunter: I beg to move amendment No. 245, in page 61, line 33, at end insert—

"(5A) For the avoidance of doubt it is hereby declared that nothing in this section shall affect any arrangements made before 15 March 1988 with a view to affording relief from double taxation having effect under section 788 Taxes Act 1988 or section 497 Taxes Act 1970 or any earlier enactment corresponding thereto.".

I hope that my right honourble Friend the Paymaster General will accept the seriousness of the amendment even though I move it with great brevity. The key lines are lines 8 and 9 of clause 64, which state:

"If a different place of residence is given by any rule of law, that place shall no longer be taken into account for those purposes."

The essential argument is that we are not pursuing a course of treaty override or double taxation. The amendment seeks to make doubly sure that clause 64 is not intended either to override existing taxation treaties or to impose double taxation on United Kingdom companies.

Mr. Brooke: I hope that I can assure my hon. Friend that his fears are groundless. His amendment seeks to ensure that the new incorporation test cannot override

double taxation conventions in relation to company residence. I am advised that there is no treaty override in clause 64, but rather than ask him to accept my word for that, I shall explain briefly.

Worries have been expressed that the new incorporation test may override other residence tests

"given by any rule of law",

to use the words that my hon. Friend quoted from clause 64(1). It has been suggested that if a company incorporated in the United Kingdom were currently resident in another country for the purposes of the double taxation convention with that country, clause 64(1) would override that convention. We intended that the new incorporation test would override the existing case law test of residence, or refinement of it, of central management and control.

Clause 64(1) sets out a rule for determining the place of residence of a company for the purposes of the Taxes Acts. The rider, that if a different place is

"given by any rule of law",

or the first place no longer runs, is similarly limited in its scope. A place of residence is often given by a double taxation convention, for the purposes of that convention, but such conventions are not part of the Taxes Acts. Any such place cannot therefore be said to be given for the purposes of the Taxes Acts. The distinction between the two concepts—resident for the purposes of the Taxes Acts and resident for the purposes of a double taxation convention—is clear from new clause 31, which we shall reach shortly. So far from the first concept overriding the second concept, new clause 31 provides for a tax charge when the second concept comes into play. In the light of that, I hope that my hon. Friend will not press his amendment.

Mr. Hunter: In the light of those reassurances, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 64, as amended, ordered to stand part of the Bill.

Clause 99

CHARGE ON DEEMED DISPOSAL OF ASSETS

11.30 pm

Mr. Brooke: I beg to move amendment No. 201, in page 78, line 43, leave out

"where at any time ('the relevant time'), a company"

and insert

"to a company if, at any time ('the relevant time'), the company".

The Chairman: With this, it will be convenient to take Government amendments Nos. 202 to 206 and Government new clause 31—Deemed disposal of assets on company ceasing to be liable to United Kingdom tax.

Mr. Brooke: These technical amendments all depend on Government new clause 31. The changes to the wording of clauses 99 and 100 are all extremely minor, and are mainly stylistic points designed to assist the reader.

Amendment agreed to.

Amendment made: No. 202, in page 80, line 4 leave out "section" and insert

"sections (Deemed disposal of assets on company ceasing to be liable to UK tax) and".—[*Mr. Brooke.*]

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

Mr. Nicholas Brown: I have one brief point to make. Why have not the Government arranged for the introduction of a separate exit charge for individuals and trusts who can continue to avoid tax by transferring residence outside the United Kingdom. I understand the aims of the clause, but could not those be extended?

Mr. Brooke: To some extent I regret not having persisted in my original intention, which was, on clause 64, to take us through the seven clauses. The hon. Gentleman's proposition is not practical under the legislation.

Clause 99, as amended, ordered to stand part of the Bill.

Clause 100

POSTPONEMENT OF CHARGE ON DEEMED DISPOSAL

Amendments made:

No. 203, in page 80, line 7, leave out "the company" and insert

"a company to which this section applies by virtue of section 99 or (Deemed disposal of assets on company ceasing to be liable to UK tax) above ('the company')".

No. 204, in page 81, line 10, after "99(2)", insert

"or, as the case may be, section (Deemed disposal of assets on company ceasing to be liable to UK tax) (2)".

No. 205, in page 81, line 16, leave out

"in relation to a company".

No. 206, in page 81, line 17, at end insert—

" 'the relevant time' has the meaning given by section 99(1) or, as the case may be, section (Deemed disposal of assets on company ceasing to be liable to UK tax) (1) above;".—[*Mr. Brooke.*]

Mr. Brooke: I beg to move amendment No. 286, in page 81, leave out lines 18 and 19 and insert—

"(7) For the purposes of this section a company is a 75 per cent subsidiary of another company if and so long as not less than 75 per

[Mr. Brooke.]

cent of its ordinary share capital is owned directly by that other company.".

The clause allows a United Kingdom resident principal company and its 75 per cent subsidiary, when the latter migrates, to elect to postpone the clause 99 charge on deemed disposal of assets in relation to foreign assets of a foreign trade. The charge is later activated when, *inter alia,* the principal company sells shares in the migrating company and as a result the latter ceases to be a 75 per cent subsidiary.

When there is a vertical chain of subsidiaries, there can be more than one principal company within the meaning of the Bill's provisions. Both the migrant company's immediate parent, and that company's own parent, could be principal companies, because both of them may control 75 per cent of the ordinary shares of the migrating company—one doing so directly, and the other indirectly. In those circumstances, the amendment makes it clear that it is the immediate parent that holds shares in the migrating company which has to make the election.

Amendment agreed to.

Clause 100, as amended, ordered to stand part of the Bill.

Clause 122

PROVISIONS FOR SECURING PAYMENT BY COMPANY OF OUTSTANDING TAX

Mr. Brooke: I beg to move amendment No. 287, in page 95, line 18, leave out "that" and insert "the relevant".

The Chairman: With this it will be convenient to take Government amendment No. 288.

Mr. Brooke: The amendments make drafting improvements. There is another place in clause 122 where the expression "that time" appears—line 12 of page 95—but I am advised that it is not appropriate to alter that, as it appears in the same subsection as the original expression "the relevant time", to which it refers.

Amendment agreed to.

Amendment made: No. 288, in page 95, line 24, leave out first "that" and insert "the relevant".—[*Mr. Brooke.*]

Mr. Brooke: I beg to move amendment No. 289, in page 95, line 35, leave out "which is".

The Chairman: With this it will be convenient to take Government amendments Nos. 290 to 295.

Mr. Brooke: The amendments make minor drafting improvements aimed at removal of doubt. Unless it is of importance to the Committee, I shall not expand on that statement.

Amendment agreed to.

Amendment made: No. 290, in page 96, line 3, at end insert—

"(7A) In this section and section 124 below any reference to the tax payable by a company in respect of periods beginning before any particular time includes a reference to any interest on the tax so payable, or on tax paid by it in respect of such periods, which it is liable to pay in respect of periods beginning before or after that time.".—[*Mr. Brooke.*]

Clause 122, as amended, ordered to stand part of the Bill.

Clause 123

PENALTIES FOR FAILURE TO COMPLY WITH SECTION 122

Amendments made: No. 291, in page 96, line 12, after "is", insert "or will be".

No. 292, in page 96, line 13, leave out "remains unpaid" and insert "has not been paid."

No. 293, in page 96, line 25, after "is", insert "or will be".

No. 294, in page 96, line 26, leave out "remains unpaid" and insert "has not been paid".—[*Mr. Brooke.*]

Clause 123, as amended, ordered to stand part of the Bill.

Clause 124

LIABILITY OF OTHER PERSONS FOR UNPAID TAX

Amendment made: No. 295, in page 97, line 21, leave out from "amount" to "within" in line 23.—[*Mr. Brooke.*]

Mr. Brooke: I beg to move amendment No. 296, in page 97, line 46, leave out from "means" to end of line 48 and insert—

"(a) where the time when the migrating company ceases to be resident in the United Kingdom is less than 12 months after 15 March 1988, the period beginning with that date and ending with that time;"

The amendment is in response to representations from a number of bodies and produces a worthwhile relaxation in the provisions of clause 124. The clause empowers the Inland Revenue to have recourse to certain group companies and directors with that status within the 12 months before the date of a company's migration if it should default on its obligations to the Exchequer.

If a company were sold by its parent company before Budget day and migrated within 12 months of the sale, the former parent company and/or directors might become liable if it subsequently failed to pay its tax. That would be unreasonable because neither the former parent company nor the directors would have foreseen that possibility before the announcement of the new arrangements on Budget day. That element of retrospection has been removed by amending the definition of the relevant period so as to exclude any period before Budget day.

In the case of sales after Budget day, the parties involved will, of course, be aware of the risk of liability arising under clause 124 and can, if necessary, indemnify themselves against the possibility of default by the former subsidiary.

Amendment agreed to.

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

Mr. Howarth: Although I accept that we should take steps to ensure that any tax due from a migrating company is recovered, it is possible that the clause will go too far. For example, companies previously associated with a migrating company, and previous controlling directors of such a company, might be liable for tax due from the migrating company even though they had severed their links with that company. In short, the clause has certain undesirable prospective effects. The persons liable have no control over events subsequent to a sale.

Will the Paymaster General consider introducing a litigation provision under which taxpayers would not be liable if they were ignorant of a company's change of residence when it was sold, or if they made arrangements to meet tax liabilities arising?

Mr. Brooke: The amendment has some relevance to my hon. Friend's comment, but it would be difficult to argue that a group company or the controlling directors affected by the clause would be ignorant of the transaction. To be absolutely certain that my hon. Friend's question contains no substance that I have not already covered, I shall look at the issue, but with no commitment.

Clause 124, as amended, ordered to stand part of the Bill.

Clause 65

PRIORITY SHARE ALLOCATIONS FOR EMPLOYEES ETC

Mr. Worthington: I beg to move amendment No. 324, in page 61, line 46, at end insert

"except to the extent that any such benefit exceeds £2,500".

The Chairman: With this it will be convenient to take the following amendments:

No. 325, in page 61, line 46, at end insert

"except to the extent that any such benefit exceeds £2,000".

No. 326, in page 61, line 46, at end insert

"except to the extent that any such benefit exceeds £3,000".

No. 327, in page 621, line 46, at end insert

"except to the extent that any such benefit exceeds £4,000."

No. 328, in page 621, line 46, at end insert

"except to the extent that any such benefit exceeds £5,000".

Mr. Worthington: I can sense that we need brevity. I simply ask the Minister why he will not accept that there should be two extra provisos. First, there should be a monetary limit on the size of the benefit, and we offer a selection of such limits. Secondly, the terms of any such offer should be available to all on equal terms rather than on similar terms. The amendments are eminently reasonable. Will the Minister accept them?

Mr. Lamont: The clause deals with an exemption from income tax for the benefit arising from priority given to employees in the allotment of shares in a public offer. We are talking not about a discount, cheap shares or free shares but about priority in a public offer.

Before the hon. Member for Clydebank and Milngavie (Mr. Worthington) gets too excited, perhaps I should explain that it has always been believed that there is no liability to tax, so the Government are not making a sudden extension. We have merely put the law back to what it was thought to be.

Because we were advised that this benefit should be taxable as an emolument—I stress that we are talking about shares in a public offer, occurring probably once in a company's lifetime—we considered introducing a cap, as the hon. Member for Clydebank and MIlngavie proposed. However, that solution is not quite as simple as the hon. Gentleman suggested because we have to attempt to value the benefit obtained by the priority. We have to take into account the various methods by which shares are allocated when an offer is oversubscribed and these may make the assessment of the benefit extremely difficult. For example, if an employee received the full number of shares for which he applied and shares were allocated to members of the public by ballot, so that some people were allotted the full number for which they applied while others received none, or if in another offer there was a scaling down, it would be a complicated operation to calculate the value of the priority.

The hon. Member for Clydebank and Milngavie has perhaps not noticed that restrictions are built into the amount of benefit. The effect of the clause will be that individual benefit from the priority in allocation cannot be excessive. It includes special provision to restrict the number of shares that may be allocated to employees to 10 per cent or fewer of the shares subject to the offer. Priority must be given to employees on similar terms. Similar terms does not mean identical terms. The terms may take account of salary and length of service, but they cannot be confined to directors or higher-paid employees. There is a reasonable number of safeguards.

I emphasise that this is a once-in-a-lifetime event when a company comes on the market. I am not aware of the problems that have motivated the amendment. We have never had similar complaints when companies have given employees priority in shares, and I should have thought that most companies were anxious not to sour relationships with their work force. On simple common sense, balanced against the complexity involved, I advise that the amendment not be pressed.

11.45 pm

Mr. Worthington: I wanted to deal with this matter simply. Abuses have been brought to our notice. Only

[Mr. Worthington.]

last week the *Financial Times* reported on a survey that was conducted by Paisner and Co. It brought to our attention the case of Caradon, the plastics and valves manufacturing company, whose senior employees were allowed a share price of 7p but at the time of the flotation the value, based on the share price, was 250p. That is rapid inflation. Although companies frequently say that their reason for going on to the market is to widen their share ownership, this rarely occurs.

Mr. Lamont: The hon. Gentleman is probably talking about an option scheme, not the issue of shares at the time of the public offer to employees. That is completely different.

Mr. Worthington: I accept that, but there is a link with clause 66, which we are soon to debate. I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Mr. Worthington: I beg to move amendment No. 329, in page 62, line 6, leave out sub-paragraph (b) and insert

"(b) that all the employees are entitled to such an allocation and are entitled to it on equal terms;".

I should like to make a number of points on the growth of a number of schemes that help a privileged group of employees. I have spoken of the Paisner survey. Coopers and Lybrand's report of a survey of 1,000 companies showed that 67 per cent operated executive share option schemes. This rose to 84 per cent among the largest firms. The general profit-sharing schemes of employees were offered by only 16 per cent of the 1,000 companies.

The report of the Paisner survey in the *Financial Times* of 13 June stated that directors and senior executives of newly floated companies had been making massive tax shelter gains as a result of share options granted in the six to 12 months before they went public, with directors seeking to establish as low a price as possible because all subsequent gains were tax free. In the firm of Caradon, the directors established for themselves a price of 7p, although at the time of flotation the price was 250p.

The Chairman: Order. The hon. Member seems to be anticipating clause 66. We are still debating clause 65.

Mr. Worthington: I am sorry, Mr. Hunt. I thought that we were on clause 66.

The Chairman: No. We are debating amendment No. 329, which relates to clause 65.

Amendment negatived.

Clause 65 ordered to stand part of the Bill.

Clause 66

SHARE OPTIONS: LOANS

Mr. Worthington: I beg to move amendment No. 330, in page 62, line 32, at end, insert

"provided it does not diminish the value of the shares to which it relates".

The Chairman: With this it will be convenient to take amendment No. 331, in page 62, line 39, at end add

"provided it does not diminish the value of the shares to which it relates".

11.50 pm

Sitting suspended for a Division in the House.

12.5 am

On resuming—

Mr. Worthington: I have already stated our main objections to the clause. We fear that many of the schemes are abused through the setting of artificially low prices, and that a privileged group of employees benefit from them.

There is a further point on which I seek an answer from the Minister. The provision deals with loans to acquire option shares, but it does not seem to be limited to such loans. There is a possible loophole. An option holder might borrow money from a bank and the shares that are the subject of the option might be pledged. There is no requirement that the money so borrowed must be used only to acquire the option shares. It could be used to buy a car or to pay for a foreign holiday, which does not seem to have been the Government's intention.

Our main argument is the possible abuse of such schemes, but we thought that it might be useful to draw to the Government's attention a possible loophole.

Mr. Lamont: I shall study what the hon. Gentleman said about abuse of option schemes. I am not familiar with the cases that he mentioned, but I do not think that they pertain to the clause.

The purpose of the clause is to assist those who wish to exercise a share option. As the hon. Gentleman acknowledged, the shares to which options relate must not be subject to restrictions which do not attach to all shares of the same class. That is to avoid the problem of manipulation, to which the hon. Gentleman referred. The purpose is to protect employees by ensuring that they have a right to acquire genuine shares, and to prevent companies from artificially influencing the value.

A loan taken out by option holders to fund the exercise of their options could also be caught under the existing anti-avoidance and anti-manipulation provisions. If the shares were pledged as security for the loan, or if the employee was committed to disposing of some of the shares to finance repayment of a loan, his freedom to dispose of some of his shares would be restricted. The shares would thus be restricted shares within the meaning of the legislation, and option holders acquiring those shares would lose their entitlement to relief.

The clause removes that unnecessary consequence. It is not intended to catch people who are using a loan legitimately to exercise an option. I have never found the Inland Revenue to be other than vigilant towards abuse and manipulation. The Revenue has advised me that the circumstances envisaged in the amendment are extremely far-fetched and that it would be inappropriate to amend the legislation. I shall, however, study what the hon. Gentleman said, to reassure myself that we do not need to buttress the provisions. I hope that he will accept that it is appropriate to alter the anti-avoidance provisions to enable people to use loans for the exercise of options.

Mr. Worthington: We wanted to put on record our anxiety about possible abuses of the schemes and about the fact that benefits were going too exclusively to the top 2 or 3 per cent in any company. We also wanted to draw the Minister's attention to a possible abuse. The amendment was a probing one. Following our short exchange, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 66 ordered to stand part of the Bill.

Clause 67

CHARITIES: PAYROLL DEDUCTION SCHEME

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

Mr. Doug Henderson (Newcastle upon Tyne, North): I sense that the Committee would consider it wise if I truncated what I might have said.

There has been some criticism of the payroll scheme by the *Financial Times*, which described it as a disappointing start, the *Investors Chronicle* which noted that only 15,000 people in the United Kingdom were covered by the scheme and the "Panorama" survey last week which noted that only two executives had availed themselves of the opportunity to help charity in that way. That contrasts with some of the Government's statements, particularly those made by Economic Secretary on 25 November 1987 when he addressed the Westminster Committee for the Protection of Children.

I wish to put some straightforward questions to the Government in the interests of time. What are the latest estimates of the number of employees covered by the scheme? How much will the changes proposed by the Government cost the Inland Revenue? Can the Paymaster General assure us that charitable donations are not intended as a substitute for the welfare state? Will he acknowledge that there are better ways to help the voluntary sector, institutions such as hospices, and so on? Finally, is the Paymaster General as pleased with the scheme as the Economic Secretary was and what answers can he give to those who argue that it is not much more than a gimmick?

Mr. Brooke: I am embarrassed by the first question put by the hon. Member for Newcastle upon Tyne, North (Mr. Henderson) because I recently answered a parliamentary question on that issue but cannot remember the precise figure. However, I shall get an answer to him.

The cost of the change in the scheme was recorded in our own forecasts as negligible. The Government do not think that charities should be a substitute for the welfare state, but charitable giving, the work of charities and the voluntary sector represent an effective way of responding to a series of needs in different parts of society. That does not apply only to welfare needs but to needs met by organisations such as the Royal Society for the Protection of Birds. Help given to the voluntary sector overall is substantial and has grown, just as charitable giving has risen sharply in the past ten years.

The hon. Gentleman asked about the Government's reaction to the progress of the scheme. We are encouraged by the number of employers who have made the scheme available—2,700 schemes have already been set up. In the Civil Service, where the Government are the direct employer, 435,000 civil servants are now eligible and arrangements have been made for a further 161,000 to join.

I would be the first to acknowledge that the exercise of persuading employees to take part in the scheme is a marketing exercise which sets charities a new challenge because once the scheme is set up with an employer it is necessary to communicate with the employees. By definition, it is the charities which logically should do that as they will be the beneficiaries. How they get things moving is a new test for them.

The Government believe that collaborative discussion is needed between employers, charities and the Government about how that educational and marketing process can be carried forward. The Chancellor will conduct a seminar on 18 July to which representatives of all the groups that I have mentioned, including trade union leaders, have been invited. We can have a round table discussion about what the various interested parties might do to encourage people to take part as it is a worthwhile scheme and the first occasion in British tax history when it has been possible for an employee to make a contribution to charity as a direct deduction from his income.

12.15 am

The answer to the question asked by the hon. Member for Newcastle upon Tyne, North is that we are making progress but, we think that we could make better progress still. The answer to the question that he asked at the beginning is that at least 40,000 people already participate, as against the 15,000 that he cited. A great many more are eligible in that their employers are making schemes available.

Mr. Henderson: If the Paymaster General had made that contribution at the Conservative party conference it would have been seen as a motion seeking the remission of the substantive motion. There are gaps in the Government's answer. I am glad that the Paymaster General was eventually able to give me some figures on the number of employees covered by the scheme. He raised the point about the number of employers who had agreed to take part in the scheme. He also

[Mr. Henderson.]

acknowledges that the real challenge is not to get the employers, although it is interesting that employers are prepared to make facilities available for their employees but not to dig into their own pockets.

Mr. Brooke: The hon. Gentleman has no grounds for that observation. The amount of contribution from employers and companies to charities has grown sharply in the past ten years.

Mr. Henderson: According to the "Panorama" survey and others, individual directors do not seem to be making the same contributions that they expect their employees to make. The Paymaster General's answer shows that the Government need to look again at the whole scheme to make sure that it works. The Opposition want it to work. It would be wrong to put the onus on us to force a vote on the clause. The responsibility lies with the Government to withdraw it and consider it at a later stage in the Bill.

Question put and agreed to.

Clause 67 ordered to stand part of the Bill.

Clause 68

ENTERTAINMENT OF OVERSEAS CUSTOMERS

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

Mr. Campbell-Savours: Very briefly, I should like to know the cost of the concession, particularly to industry. I may have misunderstood the effects of the clause, but there are a number of buying houses in London which represent many industries in the United Kingdom and act as centres to which overseas companies can send representatives to see ranges of British goods. Very often they have to entertain these overseas customers. Although they handle a vast amount of business, their turnovers may be small. A large propeotion of their turnover may be involved in entertaining customers from overseas. I do not know whether any representations have been made by such buying houses or how many there are, but when I used to visit them years ago they were doing extensive business and many British companies relied on their activities. Have they made representations? They may be major sufferers under the arrangement, unless I have misunderstood the position.

Mr. Nicholas Brown: the British Exporters Association has made representations to members of the Committee. Its letter to me begins:

"I am sure you must have been as concerned as I was to hear last Thursday that our current account deficit in the First Quarter 1988 was actually *a staggering £2.8 billion.*

The deficit on visible trade was *£4 billion.*

What is the Chancellor doing about it?"

The letter continues to indict the government. It was written by Mr. I. J. Campbell, chairman of the British Exporters Association. He sets out the experience of his company in making the case for the continuing tax relief as follows:

"The major element of my marketing expenditure, apart from the costs of frequent and regular visits to my customers, is entertaining them when they visit the United Kingdom (since, in many cases, restricted foreign exchange availability in their home country would prevent such travel) and carefully chosen, small personal gifts at Christmas, at the Eid, on birthdays, on the occasion of weddings.

Under your proposed changes, these items no longer class as tax deductible. On the other hand, I could commission a major advertising campaign—costing several thousands of pounds—to put my company's name on every roadside hoarding in Lagos, which would not bring me one extra Naire's worth of business and yet would be fully allowable against my profits and therefore tax deductible. Can you explain to me the logic behind this?"

It is only right that the Government should answer that question.

Mr. Howarth: In reply to the hon. Member for Newcastle upon Tyne, East (Mr. Brown), no British exporter doing business with Nigeria has ever been able to give a small Christmas present, but I do not want to open that can of worms because we may get into difficult territory.

Representations made to me by the banking community suggest that an overseas branch of a British bank may be liable for tax on its entertaining in the overseas country. According to the rules of that overseas country, the entertainment may be deductible from the bank's profits. Under the clause, that may be written back into the parent bank's overall tax position. British banks and British branches of British companies may then be uncompetitive overseas. That is not just a theoretical point.

In Germany, entertainment costs are fully deductible and in the United States of America, 80 per cent of costs are deductible, so a British branch of a United Kingdom company may have to operate at a substantial competitive disadvantage. The issue is not the entertaining of overseas customers in the United Kingdom, but entertaining by British branches overseas. Will my right honourable Friend the Minister comment on that?

Mr. Lamont: The clause gives effect to the proposal in the Budget to withdraw special relief for the costs that businesses incur in providing entertainment and gifts to overseas customers. The cost of providing business entertainment and gifts was originally allowable as a deduction from profits for tax purposes, just like other business expenses. Following widespread abuse, relief for that expenditure was generally withdrawn in 1965, but an exception was made for the costs of entertainment and gifts for overseas customers.

We firmly believe that such special reliefs are no longer appropriate following the tax reforms and reductions in the rates of corporation tax and income tax. We have one of the lowest corporation tax rates in the world. The yield will be about £5 million. We have had representations from many organisations—not from the firms described by the hon. Member for Workington (Mr. Campbell-Savours), but from the British Exporters Association, as the hon. Member for Newcastle upon Tyne, East (Mr. Brown) said, and also from the British Bankers Association.

The hon. Member for Newcastle upon Tyne, East referred to the argument that it would be cheaper to give gifts than to advertise. I do not find that a persuasive argument. Entertainment relief was originally abolished in 1965 because it was being widely abused. It is quite appropriate for firms to advertise and the scope for abuse is not available to the same extent.

The British Bankers Association, about which my hon. Friend the Member for Cannock and Burntwood (Mr. Howarth) asked, has solemnly made a representation to us that the relief should be continued for expenditure incurred by overseas branches of United Kingdom businesses, but that would defeat the whole purpose of the clause. The association argues that the clause will make it more likely that firms will choose to operate abroad through subsidiaries rather than branches, but I believe that that greatly overstates the likely effect on businesses' commercial decisions. As I have said before, we want to remove special reliefs of this kind and we should take account of the fact that this country has one of the lowest corporation taxes. That suggestion should therefore be thoroughly rejected.

Question put and agreed to.

Clause 68 ordered to stand part of the Bill.

Clause 69 ordererd to stand part of the Bill.

Clause 70

PREMIUMS FOR LEASES ETC

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

Mr. Campbell-Savours: Perhaps I am a bit thick, but I do not understand what clause 70 means. Will the Minister explain?

Mr. Lamont: This clause goes with other clauses relating to top-slicing relief. It removes a tax relief of limited application which is no longer necessary now that income tax rates are reduced to the levels proposed in the current Finance Bill.

The relief was originally introduced in 1963, when taxes were very much higher, to mitigate the effect of the very high top rate of income tax on premiums for short leases and certain other payments received in connection with leases. I shall explain what that involves.

If a landlord lets property for a period of 50 years or less and charges a premium, the premium—or part of it—is charged to income tax under schedule A in the year in which the lease is granted. Any part of a premium not charged to tax under schedule A falls to be taxed as a capital gain, or in some circumstances as a trading receipt.

If premiums for short leases were not charged to income tax, landlords could reduce their income tax liability on rents by charging artifically low rents and artificially high premiums. The schedule A rules counter that by treating part of the premium as though it were rent. Where the lease is for less than two years, the whole of the premium is taxed as rent. For longer leases—up to 50 years—there is a sliding scale and the amount chargeable is reduced by 2 per cent for each full year after the first for which the lease runs.

Where part of a premium is treated for tax as though it were rent, the landlord is, in effect, assessed on what is notionally more than one year's income—that is, a string of rental payments—in one year. That can have the effect of making the landlord liable to tax on that part of the premium at higher rates than those at which he would have been liable if the premium had been spread evenly over a period of years. We are doing away with a top-slicing relief which was introduced to soften that effect by enabling a landlord to claim that the tax on the premium was to be calculated at the rate or rates of tax which would have applied if he had received only one year's part of the premium in the year in which the lease was granted. Now that we have made dramatic reductions and there is to be only one top rate of income tax, such top-slicing provisions are no longer appropriate.

Question put and agreed to.

Clause 70 ordered to stand part of the Bill.

12.30 am

Clauses 71 to 85 ordered to stand part of the Bill.

Clause 86

SALES WITHOUT CHANGE OF CONTROL

Mr. Hunter: I beg to move amendment No. 342, in page 72, line 43, leave out "after the sale" and insert

"after the end of the accounting period in which the sale took place".

The Chairman: With this it will be convenient to take amendment No. 343, in clause 87, page 73, line 15, leave out "after that time" and insert

"after the end of the accounting period in which the succession took place".

Mr. Hunter: Amendment No. 342 is a probing amendment. It would alter the new two-year time limit within which claims have to be made by taxpayers to treat transfers of assets at their tax written down value. My right honourable Friend the Financial Secretary will be aware of the supporting arguments.

Amendment No. 343, which is also a probing amendment, would alter the new two-year time limit within which claims have to be made by connected taxpayers with capital allowances on machinery and plant to be treated on a continuing basis as though there had been no change in ownership of the relevant trade. Again, my right honourable Friend will be aware of the supporting arguments. I am sure that he will respond warmly to these probing amendments.

Dr. John Marek (Wrexham): If the Minister is minded to accept the spirit of the amendment, the Opposition would like the two years reduced to one year.

Mr. Lamont: We are all indebted to my hon. Friend the Member for Basingstoke (Mr. Hunter) for his vigilance in continuing to probe late into the night. I shall explain the effect of the clause before responding to the amendments.

The clause is essentially tidying-up legislation. There is nothing new about the capital allowance provision which permits an election for continuation treatment where the parties to a sale of assets are associated. Where there is a transfer of assets between two connected persons, the person to whom the transfer is made is able to stand in the shoes of the person who had the original capital allowance. The view taken hitherto has been that since an election must be followed by a claim to capital allowances, the time limit has to be that for such a claim. This is strictly the 30-day time limit for a return although, in practice, it has been extended up to the time when the relevant assessment becomes final and conclusive. Providing for a two-year time limit has two advantages. First, a specific statutory time limit will make for greater certainty in the matter. Secondly, two years is the time laid down elsewhere in capital allowance legislation within which elections have to be made.

The aim of amendment No. 343 is to enable the time limit to run from the end of the accounting period in which the sale takes place rather than from the date of the sale itself. I appreciate that that might be administratively more convenient for taxpayers and their advisers, but it overlooks the point that we are dealing with the affairs not of one taxpayer but of both parties to the transaction. It is not unknown for people who are connected to have different tax advisers and different chargeable periods. Where an election needs to be made jointly by both parties to a transaction, it is logical for the time limit to run from the date of the event, which will be known to all the parties concerned. That is the general pattern adopted in capital allowance legislation in dealing with elections affecting the liability of more than one person.

Amendment No. 343 would allow the two-year limit to run from the end of the accounting period in which the event—in this instance, the succession to the trade—takes place rather than from the date of the event itself. I cannot recommend that the Committee accept that. The general pattern of time limits for election for capital allowances is to allow two years from the end of the chargeable period in which the event occurs where only one person is involved, but not where there are two sides to the transactions, as in the case of successions to trade. Logic and equity demand that in such circumstances the time limit should run from the date of the event. The arguments on the second amendment are similar to those on the first.

Mr. Hunter: In the light of those comments, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 86 ordered to stand part of the Bill.

Clauses 87 to 90 ordered to stand part of the Bill.

Further consideration adjourned.—[*Mr. Lennox-Boyd.*]

Adjourned accordingly at twenty-five minutes to One o'clock till Thursday 23 June at half-past Four o'clock.

THE FOLLOWING MEMBERS ATTENDED THE COMMITTEE:

Hunt, Mr. John *(Chairman)*
Arbuthnot, Mr.
Armstrong, Ms
Battle, Mr.
Boswell, Mr.
Bright, Mr.
Brooke, Mr.
Brown, Mr. Gordon
Brown, Mr. Nicholas
Butterfill, Mr.
Campbell-Savours, Mr.
Carrington, Mr.
Coombs, Mr. Anthony
Darling, Mr.
Davies, Mr. Quentin
Favell, Mr.
Forman, Mr.
Griffiths, Mr. Nigel
Henderson, Mr.
Howarth, Mr. Gerald
Hunter, Mr.
Ingram, Mr.
Jack, Mr.
Lamont, Mr. Norman
Lennox-Boyd, Mr.
Lilley, Mr.
Major, Mr.
Maples, Mr.
Marek, Dr.
Mitchell, Mr. Andrew
Morgan, Mr.
Nicholson, Mr. David
Quin, Ms
Shaw, Mr. David
Smith, Mr. Andrew
Smith, Mr. Chris
Stern, Mr.
Taylor, Mr. Ian
Wallace, Mr.
Wardle, Mr. Charles
Watts, Mr.
Widdecombe, Miss
Worthington, Mr.

PS/Chancellor

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Standing Committee A

FINANCE (NO. 2) BILL

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

Tenth Sitting
Tuesday 21 June 1988
[*Part II*]

CONTENTS

SCHEDULE 6, as amended, agreed to.
CLAUSE 64, as amended, agreed to.
CLAUSES 65 to 90 agreed to.
CLAUSES 99, 100 and 122 to 124, as amended, agreed to.
Adjourned till Thursday 23 June at half-past Four o'clock.

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Standing Committee A

Tuesday 21 June 1988

[*Part II*]

[MR. JOHN HUNT *in the Chair.*]

Finance (No. 2) Bill

(except clauses 22, 23, 26 to 28, 31, 42, 49, 91, 98, 127 and 128, and schedule 7)

[*continuation from c. 556*]

9.15 pm

On resuming

Mr. Arbuthnot: I beg to move amendment No. 250, in page 133. line 37, at end insert—

"or (d) he became entitled to occupy the commercial woodland on or after 15 March 1988 on the death of his spouse and that spouse satisfied the conditions of this sub-paragraph;".

The amendment is designed to allow the transitional relief under paragraph 4 to apply if a spouse inherits woodlands during the transitional period, which ends on 5 April 1993. The transitional relief allows a person in occupation of commercial woodlands on Budget day to be taxed under schedule D until 1993. If he sells the land, disposes of it, or gets a new grant for it, that relief is lost. In the case of death when the land is passed on to a spouse, that could be a little harsh. There are other examples of reliefs being preserved when property passes between spouses on death, such as agriculture property relief and capital gains tax retirement relief. I ask my right honourable Friend the Minister to consider whether this should not be another such case.

Mr. Lamont: My hon. Friend is suggesting that the continuation of tax relief for a transitional period for expenses incurred should be available not only to those in occupation—those who planted the trees on Budget day—but also, if they die, to their widows for the transitional period. My hon. Friend has made an important point, which had not occurred to me. We may accept the amendment, or include the proposals in another form. I am seriously interested in the issue and if my hon. Friend will seek leave to withdraw the amendment I undertake to reply on Report.

Mr. Arbuthnot: On that basis, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Amendments made: No. 299, in page 133, line 47, leave out from "1979" to end of line 48 and insert

"or section 2 (1)(e) of the Forestry Act (Northern Ireland) 1953 with respect to the land;".

No. 300, in page 133, line 50, at end insert

"or, in Northern Ireland, by the Department of Agriculture".

No. 301, in page 134, line 1, leave out sub-paragraph (4).

No. 302, in page 134, line 8, at beginning insert

"Subject to sub-paragraph (5A) below."

No. 303, in page 134, line 12, leave out "as respects" and insert "in relation to".

No. 304, in page 134, line 13, leave out "as respects" and insert "in relation to".

No. 305, in page 134, line 16, leave out

"and for the purposes of paragraph (c) above" and insert—

"(5A) An election made under sub-paragraph (1) above in respect of any commercial woodlands shall not have effect in relation to any chargeable period if before the beginning of that period a relevant grant has been made with respect to any land which comprises woodlands on the same estate.

(5B) For the purposes of sub-paragraphs (5) and (5A)".

No. 306, in page 134, line 18, leave out "ten" and insert "two".

No. 307, in page 134, line 23, at end insert—

"(6A) In this paragraph and paragraph 5 below 'relevant grant' means a grant under section 1 of the Forestry Act 1979 or section 2(1)(e) of the Forestry Act (Northern Ireland) 1953 which—

(a) is made on terms and conditions first published after 15 March 1988; and

(b) is not made by way of supplement to a grant made on terms and conditions first published before that date."

No. 308, in page 134, line 26, leave out from beginning to "in" in line 27 and insert

"For any chargeable period in relation to which an election made under paragraph 4(1) above by any person has effect."

No. 309, in page 134, line 30, leave out "that Schedule" and insert "Schedule D".

No. 310, in page 134, line 31, leave out "and" and insert—

"(aa) in computing those profits or gains or losses, no account shall be taken of any relevant grant and no deduction shall be made for any expenditure in respect of which any such grant was made; and".

No. 311, in page 134, line 47, leave out

"the year of assessment 1992–93"

and insert

"a year of assessment".

No. 312, in page 134, line 48, leave out "and" and insert—

"(aa) that year of assessment is the final year of assessment for which that sub-paragraph, as it so applies, has effect as respects that person's occupation of those woodlands; and".

[Mr. Arbuthnot.]

No. 313, in page 134, line 49, leave out

"basis period for the relevant year and 6th April 1993"

and insert

"relevant basis period and the beginning of the next following year of assessment".

No. 314, in page 135, line 4, leave out " 'year' and insert

'basis period', in relation to a year of assessment".

No. 315, in page 135, line 5, leave out "the year 1992–93" and insert "that year of assessment".

No. 316, in page 135, line 7, after "1988" insert "the basis period for".

No. 317, in page 135, line 9, leave out "year 1993–94" and insert

"basis period for the next following year of assessment".—[*Mr. Lamont.*]

Mr. Boswell: I beg to move amendment No. 251, in page 135, line 13 at beginning insert—

"5A.—(1) Where, on or after 6th April 1988, a person incurs qualifying expenditure on woodlands in the United Kingdom of which he is the occupier, he may take a claim under this paragraph.

(2) This paragraph shall not apply in any year in which paragraph 4 of the Schedule applies.

(3) If a person makes a claim under this paragraph, any qualifying expenditure incurred by that person in the year of which the claim is made may be deducted from and may accordingly reduce any agricultural income of that person of that year which would otherwise be chargeable to income tax or corporation tax:
Provided that where the qualifying expenditure exceeds the agricultural income, the excess of qualifying expenditure shall not be deducted but shall instead be carried forward and added to any qualifying expenditure incurred in the next subsequent year.

(4) A claim under this paragraph shall be by notice in writing delivered to the inspector not later than two years after the end of the year of assessment to which the claim applies.

(5) In this paragraph—

(a) 'qualifying expenditure' means the amount by which expenditure wholly and exclusively incurred in respect of planting, replanting, maintaining and managing woodlands exceeds the aggregate of—

(i) income from such woodlands, and

(ii) grants receivable in respect of such woodlands.

(b) 'agricultural income' means either—

(i) income chargeable under Schedule A in respect of land, houses or other buildings in the United Kingdom occupied wholly or mainly for the purposes of husbandry, or

(ii) income chargeable under Schedule D in respect of farming or market gardening in the United Kingdom.

(c) a person who, in connection with any trade carried on by him, has the use of any woodlands wholly or mainly for the purposes of—

(i) felling, processing or removing timber; or

(ii) clearing or otherwise preparing the lands, or any part of them, for replanting;

shall not be treated as the occupier of the woodlands for the purposes of this paragraph.".

The amendment is perhaps the most substantial of the series on forestry topics—

[*Interruption.*]

—from the Conservative Benches. As we had a full debate on the subject, I wish, if possible, to avoid going over the same ground—

[*Hon. Members: "Hear, hear."*]

I am grateful to my hon. Friends and hon. Gentlemen for their encouragement.

Perhaps I may briefly remind the Committee of the significant and substantial characteristics of woodland enterprises. The first factor is their intimate relationship with agricultural land in many instances. The second is the long duration of the production cycle. The third is that recurrent maintenance costs are incurred.

As drafted, the Bill would produce a philosophy which leads to a planting ground at the beginning, no income support through the life of the woodland project—except perhaps some income from commercial thinnings, about one third of the way along the life cycle—and a commercial return at the end. But, as that return is well into the distance, forest owners will inevitably have to find their recurrent maintenance costs out of capital. That applies especially to broadleaves—for the reasons which were explored earlier—which have a longer life cycle.

When my hon. Friends and I tabled the amendment, we had in mind several different problems on which I wish to sound out my right honourable Friend the Financial Secretary this evening and which must be put right in good time before the end of the transitional period, if not with the immediacy of the earlier debate. Clearly, the earlier we know, the better.

The first problem relates to farm forestry. I declare an interest as a farmer, with a few trees. I do not have any fancy forests which would save me a great deal of tax. I have a few trees, however, and am well aware of the thrust of Government policy—I believe that it is supported on both sides of the House—to encourage farm-forestry enterprises. I see an administrative problem in the clear distinction between taxable farm activities and out-of-tax forests, and that is how they will be kept separate, administratively speaking. I fear especially that a zealous inspector or, indeed, one zealous accountant will reprove the farm forester, who may not be very sophisticated and is reluctant to involve himself in forestry, and say to him, "We notice that you have a few trees, Mr. Boswell. We should like some time sheets. How much time did you spend in your woods? How much time did your men spend down there? What equipment was used? Have you attempted to apportion the use of your capital equipment between the two uses?" The Revenue will have to adopt Nelson's eye. If not, there could be some embarrassing and, I believe, counter-productive unstitching later. Will my right honourable Friend the Financial Secretary comment on that?

Representations about the second problem have been made by the Historic Houses Association and other representative bodies. They feel strongly about heritage

woodlands which accompany a park. Earlier, we discussed what was or was not commercial. A traditional estate would have a big house, a park, parkland, amenity woods close to home and perhaps home farms in support, as well as some let farms. Traditionally, they have been run as part of the estate enterprise. If money has come in from timber, it has been taxed, and probably under schedule D. But that has hardly been the centre part of the activity. We are anxious that legitimate and public purposes, which, in many instances, are recognised by the heritage arrangements now in place, are not frustrated by the change.

The third subset of concern is that of existing woodland owners, which will often be the same as that of the traditional estate owners already mentioned. Those with a predominantly broadleaved species wood that is now 30 or 40 years old may be 50, 60, 70 or even 100 years away from commercialisation of that property. They cannot possibly obtain planting grants on the old or the new scales because the woods already exist. They will not get a commercial return for at least two generations and they face the considerable costs of running the wood for the time being. Those costs include thinning, pruning, maintenance of fences, anti-deer precautions and precautions against grey squirrels, which are extremely important in broadleaved woods.

I emphasise again that the main thrust of our concern is towards broadleaved woods because of their long timespan and the difficulty of making anything of them at the best of times, and certainly in the short term. However, the amendment is not confined to broadleaved trees, important though they are, because there are also significant forestry interests.

Those of us who have begun to learn a little about trees in the recent past have become aware of the need for much more active silvicultural management than has traditionally been practised in this country by, for example, the Forestry Commission. It is no use just shoving the trees in and coming back 60 years later to see whether they have grown. We must be prepared to do pre-commercial thinning, early pruning and so forth, which cost money. It is not easy to carry out those activities without some acknowledgement of running costs and some cash flow.

I have adverted briefly to New Zealand and will do so just once more. New Zealanders practise very active silviculture and prune more than any other country. They produce some of the highest quality commercial softwood timber, and we could do the same if we were prepared to put the effort into management. I fear that in commercial forestry the scales will be tipped against us and that in traditional broadleaf forestry many estates will leave their woods to carry on as they are in the hope of getting a bit more out of them one day.

In introducing the amendment, I must make it clear that there is no question of grants exceeding 100 per cent of the costs of establishment, which rather gives the lie to what Opposition Members said in an earlier debate. The costs extend over perhaps a 10-year period before the weeding and brushing off are done and the trees are fairly launched on their future career. My understanding of the planting scheme is that roughly 55 to 60 per cent of establishment costs will be met by the new grants, leaving about 40 per cent in the planters' hands. That result may be right, but it means that planters will have to find subsequent expenditure on maintenance out of their capital, with a long timespan still to go.

Amendment No. 251 is rather long, but its effects would be relatively straightforward. It may be wise if I first give an estimate of cost. On the basis that the abolition of schedule B will yield £10 billion a year, or that it will build up to such a yield, we estimate that my proposals would cost about £2 million per annum, which we regard as a very limited relief. All reliefs must be carefully considered and justified, but we consider that this is a sensible way to achieve our objectives.

Paragraphs (1) and (2) of the amendment would introduce the new relief on 6 April 1988, but it could not be claimed in any year to which the proposed transitional arrangements applied. Under paragraph (3), which contains the substantive point, the excessive expenditure incurred over income and grants could be set off against any schedule A income from agricultural property or farming income. I shall return to this aspect later. The set-off could not create a loss. We are not in the business of reintroducing the old tax reliefs or tax shelters.

Paragraph (5) of the amendment would define "qualifying expenditure" and "agricultural income". The concept is established in revenue law. The proposals would mean that losses could not be set off against other forms of income such as television appearance fees or pop star appearance money. It would not be of any significant benefit to absentee owners or to commercial woodlands. On reflection, I would be prepared to consider a definition which confined it to land occupied as part of an agricultural estate, so there would be no question of buying a free-standing forest with which one had no local connection. We want to avoid that kind of weakness.

9.30pm

I hope that my right hon. Friend the Financial Secretary will consider the genuine economic problem of such a planting effort, especially for the broadleaves and the lowlands, because of the long lead times involved between planting grant and commercialisation. I hope that he will examine our proposals with an open mind and be ready to consider all representations, bearing in mind that they have the bulk of forestry opinion behind them. If possible, I hope that he will give an assurance that he will reflect carefully on this matter, tune up the new proposals and improve them in good time, well before the end of the transitional period.

Mr. Chris Smith: The amendment moved by the hon. Member for Daventry (Mr. Boswell) was proposed by the Country Landowners Association and the Historic Houses Association, among others. The Opposition have no objection to the principle of ensuring and facilitating the good and sound management of existing woodlands, which is the stated aim of the amendment, but we do not believe that introducing a further tax relief schedule is a sensible way of going about it.

[Mr. Chris Smith.]

We have two specific complaints about the amendment. One has already been touched on by the hon. Gentleman himself. As the amendment stands, a farmer farming in Gloucestershire would be able to claim relief against the establishment of woodlands in the Flow country of Caithness and Sutherland. That is not the purpose of the amendment, but it is an effect that we could not possibly support. In addition, the effect of the amendment is not tailored to maintenance operations but would include other forestry operations such as planting. That is not an effective targeting of the proposals. We should prefer a proper grant system for the good, sound maintenance of existing woodlands, especially to help farmers with small areas of woodland and the owners of properties with woodlands attached to them. The amendment is not a sensible way of going about that.

Mr. Lamont: My hon. Friend the Member for Daventry (Mr. Boswell) has identified the problem of maintenance. He is saying, in effect, "You have taken them out of tax—that system is equitable and you have given planting grants, but how is the single forester or the small person not part of the large estate to deal with the cash flow problem of maintaining the estate?" I remind my hon. Friend—not that he needs reminding—that the unsatisfactory feature of the present situation is that it allows full tax relief for expenditure while not imposing any tax charge on profits. My hon. Friend's proposal would structurally cut right across the solution that we have adopted. That is not acceptable.

I have some sympathy with the point made by the hon. Member for Islington, South and Finsbury (Mr. Smith). If there is a problem with maintenance it would probably be better tackled through the grant system. My hon. Friend the Member for Daventry (Mr. Boswell) is well aware that part of the grant provision that we have introduced is for maintenance and that some of the largest maintenance costs in the life of a tree occur in the early years. That is catered for in the existing grants.

I am not saying that the solution that we have arrived at must endure for ever, but we want to see how the changes that we have made work out. I understand that the problem of maintenance and yearly upkeep worries people, but the amendment cuts across the tax changes that we have made and there are other ways of tackling the problem. Nevertheless, we will bear it in mind and examine the effects.

Mr. Boswell: I am grateful to my right honourable Friend the Financial Secretary for his comments and in no sense am I setting myself against those of the hon. Member for Islington, South and Finsbury (Mr. Smith). The important point is that the Committee sees that there is a problem. My right honourable Friend has said that he is prepared to consider the matter, but I am still concerned about the timescale because there was some implication that this would have to wait until the new arrangements were firmly in place. That is for interpretation, however, and I hope that my right honourable Friend will be able to consider representations from all sides in the interim period before the transitional arrangement applies. Subject to that and the spirit of my right honourable F[illegible]d's comments, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Schedule 6, as amended, agreed to.

Clause 64

COMPANY RESIDENCE

The Paymaster General (Mr. Peter Brooke): I beg to move amendment No. 281, in page 61, line 6, leave out "Tax" and insert "Taxes".

The Chairman: With this it will be convenient to take Government amendments Nos. 282 and 285.

Mr. Brooke: These are minor amendments intended to put beyond doubt that the provisions of clause 64 apply for all purposes of the Taxes Acts including the Taxes Management Act 1970.

Amendment agreed to.

Mr. Gordon Brown (Dunfermline, East): I beg to move amendment No. 319, in page 61, line 8, at end insert—

"(1)(A) A company, whether or not incorporated in the United Kingdom, which is not ultimately managed and controlled in the United Kingdom shall, in respect of business activity conducted in the United Kingdom of a type specified in Regulations to be made by the Board and subject to an affirmative resolution of the House of Commons be within the charge to corporation tax on income and gains arising directly or indirectly from such activity.

(1)(B) The Regulations referred to above shall have regard to the scale of investment and related activity conducted in the United Kingdom by non resident entities and their influence on specific areas of economic activity in the United Kingdom.".

The amendment seeks to draw attention to anomalies that we believe are at the heart of the taxation system for non-resident companies. I say immediately that we accept the general point behind the Government's proposal in clause 64 that companies incorporated in the United Kingdom should, for tax purposes, be regarded as resident in the United Kingdom. We hope that the Minister will accept our amendment to advance the date on which that will happen and thus minimise the scope for tax avoidance by companies which would otherwise immediately be affected by the clause.

Amendment No. 319 seeks to draw attention to the anomalous treatment of three types of non-resident companies. First, there are non-resident companies which are commercial operations and deemed to be trading operations, where tax is paid both on income and on capital gains if trading through a branch in the United Kingdom. Secondly, there are non-resident commercial operations which are deemed to be investment operations, subject only to income tax at the basic rate and not subject to corporation tax, and which as a result have differential advantages.

Thirdly, there is the special type of operation—I hope that the Minister will use this opportunity to answer

questions about this—with sovereign immunity, which is enjoyed by non-resident commercial operations and about which there is much concern.

The distinction between trading operations and investment operations forms part of our concern in moving amendment No. 319. Although there is plenty of case law surrounding the distinction between trading and investment, the distinction becomes more blurred when we examine share operations. There is absolutely no doubt that a company which actively deals in shares may be deemed to be investing in those shares and thus escape liability for corporation tax on its capital gains. This is not purely a problem that affects non-resident companies. We believe that the time is ripe for a review to end a practice that has caused a considerable loss of revenue to the Exchequer.

Secondly, I wish briefly to express our concern about non-resident commercial operations which are covered by sovereign immunity. While a number of organisations or Governments may be covered under the term sovereign immunity, it is clear to us—and to everyone else—that the scale of operations involved in the Kuwait Investment Office is such that some action needs to be considered. The Kuwait Investment Office is said to have a £15 billion share portfolio in the United Kingdom. It has stakes in 30 or more companies amounting to 5 per cent or more of the share capital as well as stakes in a large number of other companies. It has a property arm and trades on the stock exchange, both buying and selling. In the famous Exco case £6 million was made in a period of a few days. Also, of course, there is the major investment in Britain's largest company—British Petroleum—in which the Kuwait Investment Office now has a 22 per cent stake.

It is reported that the profits of Kuwait Investment Office operations in the United Kingdom amounted to more than £1,000 million last year. It is further reported that the tax due on dividends alone should have been £250 million or more, but that no tax is paid due to sovereign immunity. It is ironic that the Government's failure to close this tax loophole in a Budget that was supposed to close tax loopholes means that the biggest beneficiaries of the Budget are not the British people, no matter how rich, or even the Kuwaiti people, but the Kuwaiti royal family who pay no tax on their dividends and no corporation tax on capital gains made by dealing on the stock exchange.

The question is whether sovereign immunity should extend to what is clearly a commercial operation. Sovereign immunity as we understand it has no basis in international law or in statute. It is a concept based on reciprocal arrangements between countries and thus on good will, but it was developed in the 19th century for circumstances entirely different from those which govern the highly commercialised, active and aggressive operations of the Kuwait Investment Office. Sovereign immunity appears to give the Kuwait Investment Office exemption from tax on dividends gained from its investments in the United Kingdom. As the tax paid is refunded, the Minister must be able to tell us the amount involved. Sovereign immunity also gives the Kuwait Investment Office exemption from corporation tax on capital gains. In other words, the Kuwait Investment Office has advantages which are available to no other non-resident commercial organisation that we can detect and which are far superior to those available to any British company or investor.

The main advantage to the Kuwait Investment Office has been in the past few months. The end result of the fiasco over the British Petroleum sale is that the Government spent £18 million on advertising and £73 million in underwriting fees, only to hand over most of the shares that were on offer to the Kuwait Investment Office. The Government then had to pay back the £30 million tax paid on the first instalment of dividends to the Kuwait Investment Office. The net result was not just the transfer of a company in public hands to private hands but from British to foreign hands. As a result, no tax will be paid on dividends and if the shares are sold no corporation tax will be paid either. That could affect not just BP but other privatisation issues. Whereas it is possible for investors in this country to buy shares offered at knock-down prices, British investors and British companies cannot buy shares at knock-down prices—for example, in the electriciy industry when it is sold—and escape paying tax on the dividends and on share transactions.

9.45 pm

It is clearly in the national interest that that should not continue. The Minister must answer the following questions today. What are the criteria whereby sovereign immunity is granted? Where is the dividing line between the activities of a state and those of a highly commercialised operation which is clearly the equivalent of a multi-national holding company? Who monitors the activities carried out under sovereign immunity? We know that BP shares were bought by the Kuwait Investment Office, that the Treasury met Kuwait officials and that on 28 January the Chancellor met the Kuwait oil minister. Was sovereign immunity and its continuation any part of those discussions? Given that Kuwait bailed the Government out and saved the Chancellor's face, the Paymaster General should tell us today whether sovereign immunity was discussed, what was agreed, and what has been the result.

The benefits of sovereign immunity to a few people and organisations have been great and they seem to be given on a far more flexible basis in Britain than in other countries. We do not suggest ending a situation where there is scope for sovereign immunity and for reciprocal agreements to be made, but when clearly commercial operations are making profits out of activities in the United Kingdom we should operate the practice which appears to be current in the United States of America, where such commercial operations are deemed to be commercial and taxed appropriately.

The Paymaster General may say that because sovereign immunity has lasted 70 or 100 years or more this is not the time to do anything about it, but it is because it has lasted so long that it is no longer a suitable instrument to deal with the commercial operations of a highly aggressive multi-national holding company in the United Kingdom. He may say that no previous Government acted on this, but it is only now that the scale of the operations and the losses involved to the Exchequer have become known. For those

[Mr. Brown.]

reasons, any Government concerned about equity should act on the matter immediately.

We know that £250 million or more may have been lost this year in advanced corporation tax on dividends alone. The total may be more than £1,000 million just for the 1980s. We also know what that money could do in employing nurses, building hospitals, repairing schools, improving our welfare state and avoiding social security changes. All the cuts could have been avoided if we had received that taxation revenue this year.

Mr. Butterfill: Has the hon. Gentleman made an estimate of the benefit that may have accrued to the United Kingdom economy as a result of the billions of pounds of investment made by the Kuwait Investment Office and how many jobs may have been created by that investment?

Mr. Brown: I hope that the Minister will answer that question. If Britain's future is to be based on giving tax immunity to commercial operations in this country, the Exchequer will be extremely poor. I estimate that, for the £1,000 million that we may have lost in tax revenues during the 1980s, the Government could have created many jobs, particularly in the National Health Service and in education.

We are continuously told that the Bill seeks to simplify taxation and to stop tax loopholes. That is one tax loophole that the Government are duty-bound to examine, now that it has been mentioned. In Spain, where the activities of the Kuwait Investment Office are being monitored, action is already being taken. The Government owe the Committee an explanation of what has happened, a commitment that they will examine what has gone wrong, and an explanation of what they will do to resolve such problems in the future. I hope that the Minister will respond favourably to the points that we have raised, as the matter affects large tax revenues which should be available to the British people.

Mr. Andrew Smith (Oxford, East): In concurring with the comments of my hon. Friend the Member for Dunfermline, East (Mr. Brown) in support of the extension of tax liability to companies incorporated in this country, I shall speak principally in support of the amendment. It proposes that companies carrying out business here, but not incorporated, managed or controlled here, should be liable to corporation tax on the profits arising from their activities.

As my hon. Friend said, and as revealed in *The Sunday Times*. Insight article last Sunday, which has done us all a service, it is scandalous that organisations like the Kuwait Investment Office, which operate under liberally interpreted and out-dated sovereign immunity conventions, can rip off the British taxpayer and the public services for which he pays.

The sums involved are very large: an estimated £250 million each year in advance corporation tax is paid back to the Kuwait Investment Office, and a further £260 million worth of capital gains tax each year are not paid. As my hon. Friend the Member for Dunfermline, East said, it is a commercial organisation with a total portfolio in this country of some £15 billion and annual profits estimated at between £1,000 billion and £1,500 billion.

It is equally scandalous that the amount that that is costing the country has not yet been made known. How many other overseas Governments' organisations, royal families, sheiks and assorted potentates are on to that massive rip-off? The Committee, the House and the general public have a right to know how much it is costing us. I believe that some Conservative Members will support our demand that that drain on the public purse be identified, quantified, itemised and stopped.

How much is sovereign immunity costing the country in repaid corporation tax advance payments and foregone capital gains tax? Furthermore, how is that amount broken down between what might be described as genuine governmental organisations and commercial front organisations, such as the Kuwait Investment Office?

As my hon. Friend the Member for Dunfermline, East said, this country is particularly liberal in its interpretation of the sovereign immunity convention. Bodies such as the Kuwait Investment Office are, by no stretch of the imagination, anything other than commercial organisations. As such, they should be assessed and taxed on the same basis as commercial organisations incorporated here. They should not be able to hide behind an interpretation of sovereign immunity, which would not stand up in other countries. It does not stand up in the United States, where the internal revenue service has made it clear that it distinguishes between Government organisations that are in for a profit and those that incur a profit on genuine business. There is no reason why Britain cannot do the same. At the moment we are a soft touch and that cannot be allowed to continue.

Sovereign immunity has a totally unacceptable effect on revenues and public expenditure in terms of National Health Service employees, hospitals, schools and housing. It also distorts the market in equities if the playing field is slanted in favour of a few selected and, indeed, self-selecting players. It has dire implications for the control of British industry when an organisation such as the Kuwait Investment Office has shares of between 5 per cent and 25 per cent in 30 or more British companies. Unless the Government can assure us that they will plug the glaring anomaly, we must conclude that this is the cut-price coupon on their "Britain for sale" policy.

The hon. Member for Bournemouth, West (Mr. Butterfill) asked about the gains. If hon. Members take that view, why do we not extend the cup-price coupon to everybody? Why not let everybody come and escape tax?

Mr. Butterfill: I do not think that anyone is seriously suggesting that sovereign immunity should be extended. Indeed, I am sure that many Conservative Members will sympathise with the proposition that it should be examined closely to find whether it benefits the country or whether it is a cost to the British public, as the hon. Gentleman suggests.

It is right that the hon. Gentleman should ask questions, but I take issue with his suggestion that sovereign immunity should be stopped in all cases. Some considerable benefits have or may have derived from the continuation of the policy. If, on balance, it can be shown to have been beneficial to the British public, it would be like shooting oneself in the foot to change it merely for the sake of the principle that the hon. Gentleman espouses.

Mr. Andrew Smith: I look forward to the hon. Gentleman and his honourable Friends supporting our amendments. I did not say that it should be abolished completely.

[*Hon. Members: "You did".*]

No, I did not. I said that we must differentiate between genuine governmental organisations, which incidentally realise profits and those that are clearly in it for commercial gain. I pointed out that if the United States and our other industrial competitors can do it, why can we not do it? Given the scale of the tax-free profits being made by the Kuwait Investment Office and the many others that we do not yet know about—we are only scratching the surface of this issue—the Minister owes it to the Committee and the House to tell us the cost to the British taxpayer. The scale of the handouts to very powerful, wealthy international organisations is totally and rightly unacceptable to the British public. They will demand with us that the Government act now.

Mr. Campbell-Savours: It will be interesting to know whether any aspects of the Al-Fayed tax affairs are linked to the principle of sovereign immunity. That would answer the questions being put by Mr. Tiny Rowlands in his articles in *The Observer*. He maintains that sovereign money was used to purchase Harrods. We must be indebted to my hon. Friend the Member for Dunfermline, East (Mr. Brown) for tabling the amendment, because it gives us the opportunity to discuss not only the Kuwait Investment Office but other issues that are worrying hon. Members.

It is significant that the Kuwait Investment Office is not resisting the suggestions made in the *Sunday Times* article. The Kuwaitis may think that they are having a pretty good time at Britain's expense. They may now accept that the game is up and that it is time that they paid their dues to society. I should not be surprised if they had someone present at our proceedings today, as they knew that my hon. Friend was tabling the amendment and was likely to raise that matter.

It may also be that when the BP share flotation was seen to be at risk in its early days, the Chancellor or his officials gave a nod and a wink to the Kuwait Investment Office. It may have been suggested that if they picked up those shares to prevent the bottom falling out of the market, and therefore to prevent the Bank of England from having to move in with the floor price, no movement would be made on that front during this financial year or for several future financial years.

10 pm

I do not expect the Minister of State to give me an answer to that question tonight, but it may well have been a consideration in their minds when they moved in to save the Government the embarrassment of picking up BP shares in a collapsed market when that flotation took place.

I refer now to an issue that I raised immediately prior to the recess—the issue of Westminster cemeteries and its links with matters that we are debating today. The clause deals with the migration of companies, and the amendment tabled by my hon. Friend the Member for Dunfermline, East is one on which I can safely raise the issue of Chelwood Holdings Ltd., a company which I might say fits the Bill. The amendment says:

"A company . . . not incorporated in the United Kingdom, which is not ultimately managed and controlled in the United Kingdom shall, in respect of business activity conducted in the United Kingdom of a type specified in Regulations to be made by the Board and subject to an affirmative resolution of the House of Commons be within the charge to corporation tax on income and gains arising directly or indirectly from such activity."

I can inform the Committee that Chelwood Holdings is precisely such a company.

I want to draw the attention of the Committee to the activities of Chelwood Holdings and to an interview between a journalist on the *Guernsey Evening Press and Star*, Mr. Timothy Earl, and Mr. Rodney Hylton-Potts, a solicitor acting for Chelwood Holdings. I have a transcript of the interview, which took place on 1 June at 3.30 pm. The conversation went as follows:

"A company bought some cemeteries for 15p, Chelwood"—

that is, the company that bought the cemeteries after they had been purchased from Cemetery Assets UK, which in turn had purchased them for 15p from Westminster city council—

"bought them for a very substantial price"—

the 15p cemeteries were sold collectively for £1 and were sold by Chelwood for £300,000—

"and just sold them on to a somebody called Wisland".

[*Interruption.*]

This is real. Wisland is registered in Panama and trades in Switzerland. I am sure that it fits the amendment very neatly—

"and the only involvement of the Jersey people is the normal running of an offshore company in a nominee capacity".

Mr. Hylton-Potts was asked.

"Does that go for all the Jersey people?"

He said: "Yes" and was asked: "Including Mr. Hurley?"

Mr. Hurley was the person who owned 94 per cent of the shares in Chelwood Holdings. He was the man whom I indentified on an earlier occasion as the beneficial owner of the cemeteries which cost 15p and were sold to him for £300,000. I must apologise to the Committee and confess that I was wrong. Mr. Hurley

[Mr. Campbell-Savours.]

appears not to be the beneficial holder. He was simply a nominee, and behind him lurks another person. That person is a resident of the United Kingdom who sought to arrange his affairs so that he would avoid paying a very substantial amount of money. During the course of the conversation, Mr. Hylton-Potts said:

"What is quite clear is that Mr. Hurley was not benefiting. All he was doing was doing his boring routine job running a company which I expect he does for 1,000 clients. That's all it is."

Those 1,000 clients will be the very companies which fit so neatly in the amendment moved by my hon. Friend the Member Dunfermline, East. The transcript continues:

"I do not know why that is. You will have to ask him. It is a good point actually please ask him. We just run these for clients and we leave it to the Jersey Trust Company and lawyers just to get on with it."

Later in the interview he said:

"I don't act for Mr. Hurley but he has got nothing to worry about"—

That was after the Inland Revenue investigation which the Minister referred to on a previous occasion, was drawn to his attention—

"because he did not make anything out of it. It is nothing to do with him. He just ran a company on a nominee basis so it is all a bit of a damp squib. You must print whatever you think print-worthy".

Mr. Hylton-Potts was asked:

"Do you know if the company is a Corporation Tax company"—

Now we are getting to the hub—

"or does it pay normal tax?"

He replied:

"I think from memory, and it is from memory, it is an offshore . . . It is one of these companies which pays £500 a year."

The transcript continued:

"Ah that is Corporation Tax."

Mr. Hylton-Potts said:

"Yes. I think that is what it is, there are lots and lots of them."

When asked who the beneficial owners were, he replied:

"Of course not. What a funny question. Of course I can't, I'm a solicitor but it certainly isn't Mr. Hurley. He's a nominee."

These people in Guernsey seem to run businesses selling shell companies to any Tom, Dick or Harry from the United Kingdom wanting a quick tax dodge. In this case, the tax dodge was on a capital gain of £900,000 which took place within a matter of days. Will tax on that £900,000 be paid by anyone linked with Chelwood Holdings? It may seem a lot of money, but it was only part of a transfer pricing transaction. Chelwood Holdings then sold on the cemeteries for £1.25 million to the company called Wisland from Switzerland. We do not know who the beneficial owners of that company are. Wisland has placed a value of between £5.5 million and £10 million on the cemeteries. Now that Westminster city council has decided to repurchase the cemeteries, it may have to pay between £5.5 million and £10 million for them.

Chelwood Holdings, a company registered in Guernsey, has made a capital gain of £900,000, yet it will not pay the princely sum of £500 corporation tax on it. A company in Switzerland will then make another £5 million or even £9 million out of it. I cannot imagine how much tax that compnay will pay—probably nothing at all. The people who will lose out will be people like me, the poor ratepayers of Westminster. My rates bill will have subsidised this negligence by Lady Porter and her acolytes on Westminster city council.

We should have answers to these matters tonight. If the Minister cannot give us answers, the Committee should accept the amendment moved by my honourable Friend the Member for Dunfermline, East. At least it would give the British taxpayer an opportunity of seeing such profits repatriated.

If the Minister will not accept the amendment and the Committee, by majority, also refuses to accept it, perhaps he will consider the following proposition. The Minister might seek to interview, by agreement, those people whom I identified on a previous occasion—Mr. Ernest Francis Hurley, who is the 94 per cent nominee owner of the company, Miss Marie Moss, Mr. Stephen Sydney Moss, Miss Joan Margaret Hurley or Miss Jane Elizabeth Hurley. All of those people are nominee directors of the shell company that made a substantial profit. The Minister might ask them straight out to tell us who the beneficial owner of the cemeteries is today. The ratepayers in Westminster desperately want to know. They want to know where the money has gone, and why someone can be allowed to make such a substantial profit, while the Government, in this case, open up the doors to even further abuse, by removing the permission required from the Treasury for migration of companies. I think that there may be a link between the case that I put tonight, and the original proposition in the clause.

The individuals in Guernsey who are being used by British tax dodgers must understand that their responsibility goes far wider than Guernsey, that they are being used, and that the people of Britain object.

A report has been produced by the States Financial Services Commission, which sat in Guernsey to consider these matter. It resolved to take no action. It gave some lame excuse on the basis that it has no right to restrict the operation of companies operating within its territories. That Commission has a great responsibility to the British public. Those individuals in Guernsey have no right to offer themselves up in that way, when the British taxpayer, and in this case, the British ratepayer, lose out.

Mr. Alistair Darling (Edinburgh, Central): I thank the Committee for its good wishes earlier, and in recognition of that, I shall be brief.

Our amendment goes to the heart of a problem that faces Britain—the temptation, which the Government encourage, for companies abroad to make raids on the British economy, and also, for people who were based in Britain to move abroad to operate, so that they do not have the disadvantage of paying tax here. The problem raised by my honourable Friend the Member for Workington (Mr. Campbell-Savours) seems to highlight that point. I declare an interest as a ratepayer in Westminster, and I wish my honourable Friend well in his inquiries. I say only that if Westminster was a Labour-controlled authority, I am sure that there would not have been the same silence from the Conservative Benches.

Our problem is that people can hide behind the veil of corporate identity to carry out their various activities. Sometimes, it is difficult to see who is really hiding behind a front company. My honourable Friend the Member for Dunfermline, East (Mr Brown) has dwelt at some length on the operation of the Kuwaiti oil company and sovereign immunity. I hope that the minister takes those points seriously, because it would not take too much imagination for a country such as Switzerland—which appears to be operated for the benefit of the companies that function within it—to establish some sort of state company that might get the benefit of sovereign immunity to avoid paying taxes here. That is important when we consider Swiss companies' raiding activities in Britain.

My main point is about residence. It is becoming increasingly obvious that Britain is open to bids from companies based abroad. Because the seat of a corporation, the ultimate control, is abroad, Britain has no say in how companies that used to be based here are run. That means that the guts of this country are being controlled from abroad—sometimes thousands of miles away, and the Government seem content to let that happen.

There have been two newspaper articles recently. Sir Hector Laing wrote one in *The Times*. I do not usually praise him and Opposition Members do not agree with him about much, but he wrote an excellent article drawing attention to the fact that this country was being exposed to raids by companies—he referred in this case to the bid for Rowntree. He said that companies based abroad were able to operate with comparatively little control, and apparently little interest, from the Government.

Another article in the Lombard column of *The Financial Times* yesterday again emphasised that control was vitally important, especially if one was seeking to direct the way in which an economy develops or to control social conditions. I hope that the Minister accepts that our amendment was tabled in an attempt to get the Government to recognise that there is a genuinely serious problem that there has not been for a long time. We find that the country's affairs are being dictated behind either a corporate veil or, alternatively, a sovereign veil, and the Government seem happy to ignore that.

10.15 pm

Mr. Butterfill: Does the hon. Gentleman agree that it would be dangerous to allow xenophobia to run away with us, considering that in terms of external investment Britain is second only to Japan? In reality, the boot is very much on the other foot. We control many other companies in overseas territories. There would be a danger of recriprocal action being taken against us.

Mr. Darling: I am not xenophobic but I feel that it is only right that the Government of this country have control over the economic affairs of this country which, for example, means being able to maintain the major influence on, say, British Petroleum, our largest company. That is crucial. It seems to be the utmost folly to hand over substantial control to a sovereign company that has a vested interest in manipulating North sea oil prices to look after its investments and its oil elsewhere. Perhaps the hon. Gentleman will tell the Committee which other country is laying its cupboard open to raids by foreign predators. There is no chance of British companies going into Switzerland in the same way that Swiss companies are coming here.

Mr. Chris Smith: Would the hon Member for Bournemouth, West (Mr. Butterfill) like to draw hon. Members' attention to the information given in the Red Book at the time of the Budget, which revealed that because of the fall in the value of the dollar Britain's overseas investments fell in value by £20 billion during last year? Is that a sound investment for this country?

Mr. Darling *rose—*

The Chairman: Before the hon. Gentleman replies, may I remind the Committee that we are in danger of widening the debate far beyond the scope of the amendment. It deals with tax liability: we cannot debate wider issues tonight.

Mr. Darling: I fully accept your ruling, Mr. Hunt. My hon. Friend made a point and nothing further need be added. The amendment seeks to provide that the Government take action to ensure that people who operate and trade in this country render unto the Government what is due to them and do not shelter abroad. It is a problem that the Government seem extremely loth to tackle. When the Minister replies, I hope that he will show that he has more interest in the country's affairs, especially taxpayers' affairs, than his colleague the Chancellor of the Duchy of Lancaster has shown in protecting the country's industry. The policy seems to be, "Come and get us. We'll do nothing to stop you." It is high time that that policy was reversed because the repercussions will be serious not only in areas that are removed from the south-east of England, where it is already causing great damage, it will cause problems throughout the country. When that happens, we will be unable to resist anyone's advances because we will be weakened by so much of our industry—certainly its crucial parts—being controlled from abroad that we shall lay ourselves open to manipulation by anyone who is in a position to manipulate us.

Mr. Rhodri Morgan (Cardiff, West): I have been told by Front Bench colleagues that I will not get a share of the "short money" unless I keep my speech short. I do not know on what authority they say that. They may be being premature. I shall do my best to abide

[Mr. Morgan.]

by their instructions, which I am sure will be universally popular with the Committee.

As to the revelations about the Kuwait Investment Office, there appear to be four categories of Government investment in this country to which we must have regard. First there is the original and legitimate function of the Government. Incidentally, capital gains will arise: they will be small and incidental, there will be windfalls and occasional gains. No doubt we all agree that it is legitimate to exempt those on the basis of sovereign immunity. Therefore the question of their being taxable does not arise.

10.20 pm

Sitting suspended for a Division in the House.

10.35 pm

On resuming—

Mr. Morgan: Other activities that are not so legitimate have become a problem which all Members of the Committee must consider. Governments play the market in another country, and that is not a proper function of Government. We should all be shocked if the British Government were found to be playing the market with its own tax revenues, however gained. The hon. Member for Bournemouth, West (Mr. Butterfill) pointed out that the Government encourage British citizens to invest abroad to build up revenues against the day when North sea oil runs out, but we should be shocked if our own Government were building up direct holdings of securities, assets or properties in another country. If they did, they should pay capital gains tax and be good citizens of that country. Taxpayers in Britain would not be happy if they thought that the Government were using revenue in that way.

There is sometimes confusion about whether the Government or the ruling family are investing. The article in last week's *Sunday Times* brought out the fact that the Kuwaiti royal family, the Saudi royal family and the Brunei royal family which are the Governments in their countries, invest surplus money abroad. It is difficult to work out the correct parallel and judge whether our royal family—which is not the Government—plays the market in another country. If it does should it behave as a good citizen of that country and pay capital gains tax?

The Chairman: Order. The amendment is not about playing the market but about tax liability.

Mr. Morgan: I am sorry, Mr. Hunt, I made the point precisely several times that if the Government or ruling family of this country played the market in another country, taxpayers of this country, would think that they should pay capital gains tax according to the practices and rules of that country. I do not wish to cross swords with you on that, Mr. Hunt, but I made that point clearly.

Finally, the other form of activity which borders on illegitimate is when the ruling family of another country is worried that it may not remain in that position forever and builds up substantial holdings in this country against the day when it might fall as a Government. That scenario is likely in the Middle East where Governments fall—Governments that appear to be run by impregnable royal families such as the Libyan royal family, but Libya suddenly became a republic. The fallen Government finds it very handy to have a pile of money in Monte Carlo, London or wherever. In those circumstances capital gains tax liability is absolutely necessary. It was not a problem before 1973 when oil revenues suddenly started massively to rise to 10 or 12 times what they were before, giving rise to the hoard of money available to ruling Governments or ruling families in other countries. Should they pay tax on the enormous oil hoards that they have accrued since 1973? It was not a problem before 1973 because the sums were insignificant. The Kuwaiti and the Saudi royal families were not fabulously wealthy before 1973. Their wealth came from the rise in the price of oil from 50 cents in the late '60s to $2.50 just before the July 1973 oil price shock, $10 after that, then $30 to $40. It is now falling to what we hope is the stable price of about $18.

That those massive cash imbalances are now available and should be taxable. Our amendment would make them taxable. There should be general agreement on both sides of the House, Back Bench and Front Bench, that it is time to solve the problem. We did not want to do it immediately after 1973 out of sheer funk that we might offend the wealthiest sources of hot money in the world. We needed that hot money more than they needed us and we were desperate that it should remain in Britain rather than go to France, Germany, Italy or the USA.

It is high time that we dealt with this major problem of the hoards of oil money built up by the ruling families of countries such as Brunei, Kuwait or Saudi Arabia—we make no comment on the regimes, areas they come from, how they got their money or why they are the ruling families—that does not matter. The point is whether that money should be taxable when it is invested in massive quantities in this country. That distortion of the international flow of money—some of it taxable, but in this case untaxable—must be stopped. We hope that we will get a hint from the Minister to satisfy the fundamental objections of probably 90 per cent of the people of this country about this money being untaxed. The Government must deal with that soon.

Mr. Butterfill: Whatever the merits and demerits of the issue of sovereign immunity, the amendment would cut right across the tax treaties that this country has with other countries and in so doing undermine the basis on which one country deals with another on tax matters.

In response to the hon. Member for Workington (Mr. Campbell-Savours), I am sure that I am speaking for the majority, if not all, of Conservative members in saying that we view with repugnance the possibility that a United Kingdom resident was hiding behind Mr. Hurley and thereby breaching our tax laws. We hope that if what the hon. gentleman said can be substantiated it will be thoroughly and enthusiastically

investigated and if wrong-doing appears to have been done that a prosecution will result. If a conviction occurs the sentence should be exemplary and a deterrent to all others who may be tempted to pursue that course.

Ms Hilary Armstrong (Durham, North-West): My question arises from a situation in my constituency which Conservative Members will find peculiar for a Labour Member. A Saudi prince has acquired a grouse moor in my constituency. I am worried about the extent to which sovereign immunity is being used and therefore tax exemptions are being given for what are essentially commercial transactions. How much money do the Government think is involved and to what extent is sovereign immunity being used in this country as a cover for other activities?

Mr. Brooke: The hon. Member for Dunfermline, East (Mr. Brown), in moving the amendment, said that the Opposition accept the spirit of clause 64 and applauded its instinct. I did not catch echoes of that in the speeches of his hon. Friends, some of whom suggested that clause 64 would make easier some of the things to which they were objecting.

I shall not dwell on the words

"whether or not incorporated in the United Kingdom"

which appear in the first line of the amendment. Instead, I shall concentrate on the non-resident aspect.

10.45 pm

The hon. Member for Dunfermline, East asked about the difference between trading companies which operate through branches and agencies, and investment companies. He is correct in principle, because investment gains are charged at the basic rate of income tax and not through corporation tax, but that is a general tax principle and not specific to the clause. The hon. Gentleman then raised the question of non-residents dealing in shares. Where a non-resident company is dealing in shares, its profits will count as income for tax purposes, and if it is trading through a United Kingdom branch or agency it will be liable to tax here. The borderline between dealing activities and investment activities depends on the facts of each case and, of course, the Inland Revenue looks carefully at the circumstances of individual companies.

When the hon. Gentleman spoke on the general subject of sovereign immunity, he asked about the criteria, the dividing line and who monitored it. The provisions for sovereign immunity are operated by the Board of Inland Revenue, based on legal advice on the application of international law. Ministers are not involved in decisions on individual cases. The hon. Gentleman then referred to American practice in these matters. Briefly, the United States exempts income that foreign Governments derive from investments in the United States, which could include investment in a large United States corporation. The United States does not exempt income from commercial activities or from a trading company which the foreign Government effectively control. In that respect, therefore, I do not disagree with the hon. Gentleman's analysis.

The hon. Member for Dunfermline, East went on to speak at some length, as did some of his hon. Friends, about the Kuwait Investment Office. I must make it clear at the outset that I am unable to enter into any discussion about the tax status or tax affairs of an individual taxpayer. It is clear from my dealings with other regimes in other parts of the world, to which the hon. Gentleman referred in passing, that the distinction as to the confidentiality of individuals' tax affairs does not necessarily prevail in other countries, but it is highly desirable that it should prevail in this country.

The hon. Gentleman drew attention to the fact that sovereign immunity is a concept of very long standing. It has its origins in the general principle of international law that sovereigns and the public property belonging to them are treated as being not subject to the municipal laws of foreign states. In accordance with that principle, the income, profits and gains of sovereigns, foreign states and integral parts of foreign Governments arising in the United Kingdom are immune from United Kingdom tax. Again, I think that I have common cause with the hon. Gentleman. So far as we can trace, most other European countries, together with the United States, Canada and Japan, acknowledge the general principle which the hon. Gentleman adumbrated and which I have expanded, although its application may vary and is often not expressed in tax statutes. The hon. Gentleman was right to say that it is expressed in a tax statute in the United States, but it is not commonplace for it to be addressed in tax statutes in other countries. Most major countries provide similar exemption for the investment income and gains of foreign Governments, so there is a reciprocal benefit to the United Kingdom in relation to our actions outside the United Kingdom.

In answer to the question put to me by the hon. Member for Oxford, East (Mr. Smith), the fact that this is an immunity from tax, rather than a specific statutory exemption subject to a claim, means that the tax consequences of sovereign immunity cannot be estimated. Much wider issues are involved. For example, in so far as the income concerned is interest on Government securities, it may be exempt in any event in the hands of a non-resident. A number of gilts are not subject to tax—an exemption that was supported by the Labour Government, as it has been by this Government—and the Bank of England believes that it can price them more finely as a result. More important is a consideration of the benefits to the United Kingdom economy generated by this form of inward investment. It is another example of the strength of our economy that such investment is attracted here.

The hon. Member for Dunfermline, East asked about the Government's basic attitude to sovereign immunity. As I have said, we benefit from sovereign immunity under other countries' tax regimes, including the management of the foreign currency holdings that make up our own Reserves. Foreign investment in the United Kingdom and through United Kingdom financial institutions is certainly of benefit to us. If the sovereign bodies operate in the United Kingdom via companies resident here, those companies will of course be taxed in the normal way. Sovereign immunity applies only to the dividends and interest remitted abroad.

[Mr. Brooke.]

The hon. Member for Dunfermline, East went slightly over the top both on the radio this morning and with some of his hon. Friends this evening in his desire to replay the issue of the BP flotation last year. I should not have thought that the Opposition would be particularly keen to return to that. I was out of the country at he time, so I had the pleasure of reading the exchanges as a continuous narrative in *Hansard* whereas others lived through them at intervals. I thought that the score was five to my right honourable Friend the Chancellor of the Exchequer and nil to the right honourable and learned Member for Monklands, East (Mr. Smith), who at one stage was reduced to being an apologist for Goldman Sachs. The hon. Member for Workington referred to a nod and a wink on the part of the Government.

Mr. Gordon Brown: Can the Paymaster General assure us that in no discussions involving the Treasury or the Chancellor of the Exchequer with any official of the Kuwait Government or the Kuwait Investment Office was the issue of sovereign immunity discussed?

Mr. Brooke: That is the question that the hon. Gentleman said that he would ask my right honourable Friend the Chancellor today, but my right honourable Friend is in Toronto. The hon. Gentleman said that he would ask whether continued exemption from tax was discovered when, to use his words, the Kuwait Government

"bailed out Mr. Lawson over the question of the BP shares".

It is outrageous to suggest that any official or Minister would discuss the matter with the Kuwait Government, and I deny the allegation totally and absolutely.

As for the question asked by the hon. Member for Oxford, East, I have explained why it is difficult to estimate the consequences of sovereign immunity. We do no keep separate figures for investments made by particular agencies or individuals.

The hon. Member for Workington took us yet again through the narrative of the Westminster cemeteries. As with the Kuwait Investment Office, I cannot comment on the affairs of an individual taxpayer but it is clearly a matter that should appropriately be followed up by the Revenue. I will ensure that the hon. Gentleman's comments are put at the Revenue's disposal. I give the hon. Gentleman that assurance.

Mr. Campbell-Savours: Will the Minister accept my proposition that Chelwood Holdings, will pay £500 corporation tax on a profit of £900,000 on Westminster cemeteries, whereas if Chelwood Holdings had been registered in the United Kingdom as a company its tax liability would have been nearer £250,000? Does the Minister accept that these people have fiddled the taxman out of £250,000?

Mr. Brooke: I said that I could not comment on individual cases, and it would be wrong for me to comment on the hypothesis that the hon. Gentleman puts to me, but the narrative that the hon. Gentleman described predated the Government's decision to change the consent procedures under section [redacted]. It therefore occurred under the previous regime and not under the regime that we seek to change in the clauses. I put it to the hon. Members for Workington and for Edinburgh, Central (Mr. Darling) that clause 64 strengthens our regime in this matter rather than weakening it.

The hon. Member for Durham, North-West (Ms Armstrong), drawing on the case of a grouse moor, asked me the same broad question that the hon. Member for Oxford, East asked. I cannot expand on my earlier remarks.

Mr. Gordon Brown: Before the Paymaster General finishes, will he agree with us that sovereign immunity, as presently defined, gives the Kuwait Investment Office, and perhaps other commercial organisations, huge advantages and benefits which set them apart from ordinary British investors or foreign companies? Will he consider the practice that appears to function in the United States where commercial operations are separated from the direct activities of Governments and are therefore taxed?

Mr. Brooke: There are differences between our arrangements and those of the United States in many areas. We have reasons for doing what we do, just as they have reasons for doing what they do.

The hon. Member for Oxford, East said that if the Government would not act today all kinds of apocalyptic consequences would follow. I assure the Opposition that all aspects of the tax system are kept under constant review. We are dealing with a regime that has operated for 70 years, so that constant review has taken place under Labour as well as Conservative Administrations. I give a pledge that the matter will continue to be reviewed—

[*Hon. Members: "Five-nil again!"*]

—within the spirit of the monitoring by the Inland Revenue—which I described earlier.

Mr. Gordon Brown: I am grateful to the Paymaster General for agreeing with us on some important issues about sovereign immunity. He agrees that the Kuwait Investment Office and other organisations are liable to be subject to sovereign immunity and that the advantages are considerable—they would not have to pay tax on dividends or corporation tax on capital gains. He agrees that they have advantages which do not accrue to foreign companies, British residents, or British companies, but he refuses to agree that since the issue has been exposed and the facts have become clear he should take steps to examine or rectify the position.

The Paymaster General failed to deal with the question of the scale of losses involved. The Treasury clearly has the figures. If it has to refund advance corporation tax payments, it has the figures and it knows how much is involved. The Paymaster General also failed to deal with the question of British Petroleum, which he barely mentioned in his remarks.

Mr. Brooke: The hon. Gentleman says that I did not deal with British Petroleum. Is he continuing to press the allegation that he made on the radio this morning?

Mr. Brown: I am happy to accept the assurance that the Paymaster General made, even though he was not in the country when the matter arose, but there are considerable worries about what is happening to BP. If the Government were sufficiently anxious to refer the issue of BP ownership by Kuwait to the Monopolies and Mergers Commission—that is currently under discussion—they should also be anxious about the scale of dividends payments and, later, of capital gains to the Government of Kuwait. It is unhealthy that by selling BP shares to the British public the Government have ended up with them being controlled by the Kuwait royal family.

Mr. Morgan: Wider share ownership.

11 pm

Mr. Brown: The problem is that in future privatisations—electricity, for example—the Kuwait Investment Office may not only buy up shares at the knock-down prices available to everyone else but do so in the knowledge that it will not be taxed on any of the dividends and that if it chooses to sell the shares or to play the stock exchange with them it will not have to pay corporation tax on the capital gains. It is a serious matter that the power enjoyed by one investor to play the market—free from the responsibility of paying tax—is so great when set against other institutions, especially ordinary British institutions and British investors. We may face the possibility of an energy empire being built up by the Kuwait Investment Office, including not only huge stakes in British Petroleum—it already has 22 per cent in Britain's largest company—but the electricity industry and, by implication, nuclear power stations.

Spain has had to recognise the problem and to act. The United States of America is aware of the problem and has acted in the taxation of commercial organisations. Sovereign immunity is not available in the same form in other countries of Europe. Why do the Government cling to an old-fashioned concept of sovereign immunity which allows tax-free profits to be made by what are clearly commercial organisations acting under the umbrella of a state but effectively operating as multinational holding companies? From the information available to us, it seems that the scale of losses to the Exchequer is now such that any Committee member would be failing in his or her duty in not asking what the Government intend to do about this. Bland assurances about keeping the matter under review are simply not enough. We want an assurance from the Paymaster General—Conservative Members would do us and the country a service if they also pressed for this—that an investigation will take place and that, if necessary, urgent action will be taken to deal with a problem that costs our country millions of pounds and thus deprives vital social services of money which they urgently need.

Question put, That the amendment be made:—

The Committee divided: Ayes 14, Noes 21.

AYES

Armstrong, Ms Hilary	Ingram, Mr. Adam
Battle, Mr. John	Marek, Dr. John
Brown, Mr. Gordon	Morgan, Mr. Rhodri
Brown, Mr. Nicholas	Quin, Ms Joyce
Campbell-Savours, Mr. D. N.	Smith, Mr. Andrew
Darling, Mr. Alistair	Smith, Mr. Chris
Griffiths, Mr. Nigel	Worthington, Mr. Tony

NOES

Arbuthnot, Mr. James	Jack, Mr. Michael
Boswell, Mr. Tim	Lamont, Mr. Norman
Bright, Mr. Graham	Lennox-Boyd, Mr. Mark
Brooke, Mr. Peter	Maples, Mr. John
Butterfill, Mr. John	Nicholson, Mr. David
Carrington, Mr. Matthew	Stern, Mr. Michael
Coombs, Mr. Anthony	Taylor, Mr. Ian
Davies, Mr. Quentin	Wardle, Mr. Charles
Favell, Mr. Tony	Watts, Mr. John
Howarth, Mr. Gerald	Widdecombe, Miss Ann
Hunter, Mr. Andrew	

Question accordingly negatived.

The Chairman: I call Mr. Brown—that is, Mr. Nicholas Brown—to move amendment No. 320.

Mr. Nicholas Brown: It is for the convenience of the Committee, Mr. Hunt, that Opposition spokesmen are called either Brown or Smith. No doubt that concession will be welcomed by all.

I beg to move amendment No. 320, in page 61, line 10, leave out from "which" to end of line 14 and insert

"was not resident in the United Kingdom immediately before that date".

The Chairman: With this, it will be convenient to take the following amendments:

No. 244, in page 61, line 16, at end insert—

"(2A) In relation to a company which carried on business at any time before the date of the coming into force of this section and which either—

(a) immediately before that date was not resident in the United Kingdom and was resident in a territory outside the United Kingdom;

or

(b) ceases to be resident in the United Kingdom on or after that date in pursuance of a Treasury consent and becomes resident in a territory outside the United Kingdom,

subsection (1) above shall not apply.".

No. 318, in page 61, line 16, at end insert—

"(2) Subject to subsection (2A) below in relation to a company which carried on business at any time before the date of the coming into force of this Section and which was not resident in the United Kingdom immediately before that date subsection (1) above shall not apply until the end of the period of five years beginning with that date.

(2A) Subsection (1) above shall not apply in relation to a company which carried on business at any time before the date of the coming into force of this Section and which in pursuance of Treasury consent either ceased to be resident in the United Kingdom before that date or ceases to be so resident after that date.".

I should tell the hon. Member for Basingstoke (Mr. Hunter) that, through a printer's quirk, his amendment No. 244 does not appear on today's Amendment Paper. It has, however, been selected, and it has been reprinted and is available on the Table.

Mr. Brown: Amendment No. 320 is a probing amendment and we need not spend much time on it, provided that we get a candid answer from the Government.

Mr. Brown: It is for the convenience of the Committee that the Opposition spokesmen are called either Brown or Smith.

The purpose of the amendment is to delete the second part of this clause which sets out the five-year period of grace. Regardless of the argument over how long the period should be, why should it operate for those who are already non-resident and also spell out a mechanism whereby others can take advantage of it? Why should the deadline not come in sooner?

Mr. Hunter: With near-equal brevity I shall speak to amendments Nos. 244 and 318. The essential point of clause 64 is to widen the definition of a company resident for tax purposes. The counterargument is that the formula that is contained within the clause is widening that definition too far. I am sure that my right honourable Friend the Paymaster General will not equate brevity with flippancy, because he is familiar with the essential arguments following correspondence that he has had with the CBI and meetings that I understand have taken place between the CBI and the Inland Revenue.

It is fine to seek to eliminate the nowhere companies and to discourage those that pay no tax anywhere and are incorporated in the United Kingdom only to give them a cloak of respectability. It is extremely probable that the overwhelming majority of companies that are incorporated in the United Kingdom but are tax-resident overseas will, within five years, be able to reorganise their affairs and not suffer adversely from the demands of clause 64. However, some companies may not be able so to reorganise their affairs. They will incur commercial risks and financial costs and may in some instances incur adverse political repercussions because often they operate in parts of the world descending from colonial or even imperial days and have relationships with the Governments there. The essential argument is that as it now stands, clause 64 lacks that flexibility and sensitivity to account for companies incorporated in the United Kingdom and tax-resident overseas—especially where that is done by treaty or with Treasury consent—which will find reorganisation a burdensome task and, arguably, counter to their commercial interests.

Mr. Gerald Howarth (Cannock and Burntwood): I endorse the points made by my hon. Friend the Member for Basingstoke (Mr. Hunter). He is right to say that there is unanimity across the Committee about the need to tackle some of the abuses. May we point out to Opposition Members who huffed and puffed that, once again, it is a Conservative Government who tackle abuses? Socialist Governments had the opportunity when they were in power and were unable to take advantage of it. But in essence, there has been some agreement across the Committee about this measure.

However, as my hon. Friend said, some problems arise out of the drafting of clause 64 which unilaterally changes the tax residence of companies—most importantly, of those companies which have changed the residence by Treasury consent for perfectly sound commercial reasons. Those are not the companies that Sergeant Bergerac from Workington was talking about in terms of cemeteries, hidden bodies and all sorts of weird and wonderful conspiracies which are the meat of the hon. Member's life in this House. We are not talking about such companies. We are talking about perfectly respectable honourable companies which have sought and obtained Treasury consent to move their residence for tax purposes. It is undesirable that some of those companies incorporated here which are tax-resident elsewhere will now have their tax position changed in this arbitrary and retrospective way. I understand that there has not been much consultation with the companies affected although, as my hon. Friend says, there has been consultation with the CBI.

Many of those companies will have to restructure to avoid these unplanned consequences. In a number of cases that will be extremely costly. Some companies may not be able to reorganise in the way that is necessary to avoid being caught by the new resident definition and some may have to resort to legislation. As we have seen on the Floor of the House over the past couple of weeks certain difficulties are associated with getting private business through this place. For some perfectly respectable companies incorporated under royal charter the only means of coping with this change may be to resort to a private Bill and they may be unable to get it through the House because of pressure on time.

Opposition Members have suggested that somehow there is only one way in which this proposal could promote the national interest, and that is to close loopholes and all the rest of it. It is important to bear in mind the fact that there are severe implications for a number of British companies which are incorporated in the United Kingdom but which operate principally in other parts of the world, particularly Commonwealth countries where over decades they have managed to establish a relationship. By moving their place of incorporation they may not only endanger their relationships with those Governments but may have to give up their shareholdings to the local companies. That would not be in the overall interest of the United Kingdom taxpayer.

In conclusion, I hope that my right honourable and hon. Friends will give careful consideration to the amendment proposed by my hon. Friend the Member for Basingstoke. Unless they are prepared to do that there could be serious adverse effects for major British companies which make an undoubted contribution to the British economy.

Mr. Brooke: The hon. Member for Newcastle upon Tyne, East (Mr. Brown) drew attention to the fact that all hon. Members on the Opposition Front Bench are named either Brown or Smith. I notice that they all come from eastern constituencies: Newcastle upon Tyne, East, Dunfermline, East, Monklands, East and East Kilbride. A strong easterly wind blows.

Mr. Andrew Smith: The east is red.

Mr. Brooke: With regard to the amendment moved by the hon. Member for Newcastle upon Tyne, East, at present the transitional arrangements apply to existing United Kingdom incorporated companies that were not resident in the United Kingdom on Budget day under the old rules, and to companies which migrate from the United Kingdom on or after that date with the consent of the Treasury under section 482 or its successor. The amendment would restrict the transitional arrangements to the first category only.

Although the section 482 consent mechanism for company migration is being abolished for the future, we believe that the Treasury should continue to process applications for consent to migrate, that were submitted before Budget day but not processed by then. If we simply withdrew the provisions for migration with Treasury consent for all purposes as at Budget day, it would represent an unfair denial of the legitimate expectations of companies which had applications in the pipeline. I therefore encourage my hon. Friends to resist the amendment.

My hon. Friend the Member for Basingstoke mentioned the group of companies which had already received consent historically under section 482 or its successor. As he said, under the Bill as it stands they would become United Kingdom-resident, as would all United Kingdom companies after five years from Budget day.

In this instance, I am also replying to my hon. Friend the Member for Cannock and Burntwood (Mr. Howarth). Ministers are aware of the concern that has been expressed about clause 64 that in certain cases it may be unreasonable to make existing companies United Kingdom resident when they are incorporated here but not resident under the previous rules. We are considering various aspects of this problem, to which my hon. Friend alluded. I think that it is accepted by those making the representations—my hon. Friend quoted the CBI—that any provision in this area would have to include some conditions covering those companies for which a case has not been made out. The CBI acknowledges that there is such a category.

We are considering the matter carefully and hope to bring forward an amendment on report.

Amendment negatived.

Mr. Nicholas Brown: I beg to move amendment No. 321, in page 61, line 15, leave out "five years" and insert "one year".

The Chairman: With this it will be convenient to take amendment No. 322, in page 61, line 15, leave out "five years" and insert "six months".

Mr. Brown: Again, these are probing amendments which set out alternative periods of grace. We want the Government to explain why they are allowing a period of five years. That is a long planning period and presumably will give companies seeking to take advantage of these provisions a long time to plan their affairs in such a way as to maximise the advantage to themselves and minimise the advantage to the Exchequer. We are concerned about that. I cannot easily believe that it is the Government's intention to provide a route for tax avoidance, so perhaps the Paymaster General will tell us precisely why the Government are doing this.

Mr. Brooke: Clause 64(2) provides special arrangements for companies incorporated in the United Kingdom before Budget day but not resident at that date under existing law. The hon. Gentleman seeks to shorten the transitional arrangements under which they would have the chance to reorganise their affairs on becoming again subject to our jurisdiction.

We consider it reasonable to allow a fairly generous amount of time for such companies to conduct their affairs. I do not know how many Committee members have been engaged in organising an international structure of companies—

[*Hon. Members: "Hands up!"*]

I speak with limited experience myself, but it is complicated trying to do that with one's left hand while running a business and continuing the main operations of the company. Therefore, very much in the spirit of the remarks of my hon. Friend the Member for Basingstoke (Mr. Hunter) on the last amendment, we regard five years as a sensible allowance for that purpose.

Mr. Nicholas Brown: That is a wholly unconvincing explanation. The Government are being extremely generous to people in that position. Nevertheless, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Amendments made: No. 282, in page 61, line 21, leave out "Tax" and insert "Taxes".

No. 283, in page 61, line 23, leave out from first "up " to end of line 24 and insert "outside the United Kingdom".

No. 284 in page 61, line 28, leave out from "of" to end of line 29 and insert "a person exercising functions which, in the United Kingdom, would be exercisable by a liquidator".—[*Mr. Brooke.*]

Mr. Nicholas Brown: I beg to move amendment No. 323, in page 61, line 29, at end insert—

"(4A) subsection (4B) below shall have effect in relation to a company which becomes resident in the United Kingdom by virtue of subsection (2) or (3) above.

(4B) Where this subsection applies the company becoming resident in the United Kingdom shall not for any accounting period ending within the period of six years commencing with that event be:

(i) treated as a member of a group for the purposes of Chapter IV, Part X of the Income and Corporation Taxes Act 1988;

(ii) treated as a subsidiary for the purposes of S240 of the Income and Corporation Taxes Act 1988;

(iii) treated as a paying company for the purposes of S247 of the Income and Corporation Taxes Act 1988;

(iv) treated as a member of a group for the purpose of S273 of the Taxes Act 1970.".

[Mr. Nicholas Brown.]

I expected more cheerful "ayes" on the last amendment, but Committee members sounded disgruntled. We would not want defective legislation to become law.

Amendment No. 323 is more significant than the probing amendments that I discussed previously. It accords with the spirit of the clause as it seeks to block areas that we have identified as loopholes. I hope that the Governement will welcome our endeavours, which are intended to sit alongside what they proclaim to be their own. The Paymaster General may say that there is an imperfection in the way in which the amendment is drafted, and that the Government will cover the same point with the skills of the parliamentary draftsman. If so, we shall accept that, as we want the Government to accept the principle and are not concerned about the niceties of parliamentary draftsmanship.

The amendment deals with three issues. The first is the situation of a non-resident subsidiary company in a tax haven, which may have managed to gain a substantial pool of untaxed profit. We understand that if that subsidiary wants to repatriate capital by way of dividend, the dividend will be subject to corporation tax. Under the clause, however, because the subsidiary company is United Kingdom incorporated that money could simply be shipped back into the British tax net in five years' time. Could it not then be paid up entirely free of tax if the company made an election under section 247 of the Income and Corporations Taxes Act 1988? The amendment would prevent that from happening for the next six years.

The second isssue is trading profits and group relief. If an organisation brings back to the United Kingdom a net loss from a trading operation overseas and elects to use that loss against its United Kingdom profits, it would deprive the Revenue of tax due.

Thirdly, an offshore organisation may own assets which are expressed as capital losses off its trading profit or group relief. If it re-imports those into the United Kingdom and matches them against profits here, it would again deprive the Exchequer of tax due.

I have outlined our method of blocking those three loopholes and I look forward to hearing how the Government intend to deal with them.

Mr. Brooke: Under clause 64(2), United Kingdom incorporated companies which were not resident in the United Kingdom immediately before Budget day will become resident here after a five-year transitional period. Under clause 64(3), they will do so at an earlier date if they transfer their central management and control to the United Kingdom before then. An ample transitional period is necessary to allow companies to reorganise if they wish, and we shall look sympathetically at any types of company on which the provision may bear unduly harshly. Once resident, however, such companies should be treated exactly like all other United Kingdom resident companies. It is thus unreasonable to deprive them of the normal reliefs given to United Kingdom resident members of groups.

The hon. Member for Newcastle upon Tyne, East (Mr. Brown) referred to loss importation. I am not hiding behind the observation that the amendment is defective, but if its purpose is to discourage loss importation it is defective because it is not directed at companies which are not United Kingdom incorporated and which might seek to become resident in the United Kingdom to have their losses relieved here. There is at present no intention to legislate on the wider issues of loss importation as there is no evidence of a substantial increase in its incidence but, in familiar words, the Government will keep the matter under review.

Question put, That the amendment be made:

The Committee divided: Ayes 15, Noes 22.

AYES

Armstrong, Ms Hilary	Ingram, Mr. Adam
Battle, Mr. John	Marek, Dr. John
Brown, Mr. Gordon	Morgan, Mr. Rhodri
Brown, Mr. Nicholas	Quin, Ms Joyce
Campbell-Savours, Mr. D. N.	Smith, Mr. Andrew
Darling, Mr. Alistair	Smith, Mr. Chris
Griffiths, Mr. Nigel	Worthington, Mr. Tony
Henderson, Mr. Doug	

NOES

Arbuthnot, Mr. James	Jack, Mr. Michael
Boswell, Mr. Tim	Lamont, Mr. Norman
Bright, Mr. Graham	Lennox-Boyd, Mr. Mark
Brooke, Mr. Peter	Maples, Mr. John
Butterfill, Mr. John	Mitchell, Mr. Andrew
Carrington, Mr. Matthew	Nicholson, Mr. David
Coombs, Mr. Anthony	Stern, Mr. Michael
Davies, Mr. Quentin	Taylor, Mr. Ian
Favell, Mr. Tony	Wardle, Mr. Charles
Howarth, Mr. Gerald	Watts, Mr. John
Hunter, Mr. Andrew	Widdecombe, Miss Ann

Question accordingly negatived.

Amendment made: No. 285, in page 61, line 30, after first "section", insert—

" 'the Taxes Acts' has the same meaning as in the Taxes Management Act 1970;".—[*Mr. Brooke.*]

Mr. Hunter: I beg to move amendment No. 245, in page 61, line 33, at end insert—

"(5A) For the avoidance of doubt it is hereby declared that nothing in this section shall affect any arrangements made before 15 March 1988 with a view to affording relief from double taxation having effect under section 788 Taxes Act 1988 or section 497 Taxes Act 1970 or any earlier enactment corresponding thereto.".

I hope that my right honourble Friend the Paymaster General will accept the seriousness of the amendment even though I move it with great brevity. The key lines are lines 8 and 9 of clause 64, which state:

"If a different place of residence is given by any rule of law, that place shall no longer be taken into account for those purposes."

The essential argument is that we are not pursuing a course of treaty override or double taxation. The amendment seeks to make doubly sure that clause 64 is not intended either to override existing taxation treaties or to impose double taxation on United Kingdom companies.

Mr. Brooke: I hope that I can assure my hon. Friend that his fears are groundless. His amendment seeks to ensure that the new incorporation test cannot override

double taxation conventions in relation to company resid[illegible]. I am advised that there is no treaty override in clause 64, but rather than ask him to accept my word for that, I shall explain briefly.

Worries have been expressed that the new incorporation test may override other residence tests

"given by any rule of law",

to use the words that my hon. Friend quoted from clause 64(1). It has been suggested that if a company incorporated in the United Kingdom were currently resident in another country for the purposes of the double taxation convention with that country, clause 64(1) would override that convention. We intended that the new incorporation test would override the existing case law test of residence, or refinement of it, of central management and control.

Clause 64(1) sets out a rule for determining the place of residence of a company for the purposes of the Taxes Acts. The rider, that if a different place is

"given by any rule of law",

or the first place no longer runs, is similarly limited in its scope. A place of residence is often given by a double taxation convention, for the purposes of that convention, but such conventions are not part of the Taxes Acts. Any such place cannot therefore be said to be given for the purposes of the Taxes Acts. The distinction between the two concepts—resident for the purposes of the Taxes Acts and resident for the purposes of a double taxation convention—is clear from new clause 31, which we shall reach shortly. So far from the first concept overriding the second concept, new clause 31 provides for a tax charge when the second concept comes into play. In the light of that, I hope that my hon. Friend will not press his amendment.

Mr. Hunter: In the light of those reassurances, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 64, as amended, ordered to stand part of the Bill.

Clause 99

CHARGE ON DEEMED DISPOSAL OF ASSETS

11.30 pm

Mr. Brooke: I beg to move amendment No. 201, in page 78, line 43, leave out

"where at any time ('the relevant time'), a company"

and insert

"to a company if, at any time ('the relevant time'), the company".

The Chairman: With this, it will be convenient to take Government amendments Nos. 202 to 206 and Government new clause 31—Deemed disposal of assets on company ceasing to be liable to United Kingdom tax.

Mr. Brooke: These technical amendments all depend on Government new clause 31. The changes to the wording of clauses 99 and 100 are all extremely minor, and are mainly stylistic points designed to assist the reader.

Amendment agreed to.

Amendment made: No. 202, in page 80, line 4 leave out "section" and insert

"sections (Deemed disposal of assets on company ceasing to be liable to UK tax) and".—[*Mr. Brooke.*]

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

Mr. Nicholas Brown: I have one brief point to make. Why have not the Government arranged for the introduction of a separate exit charge for individuals and trusts who can continue to avoid tax by transferring residence outside the United Kingdom. I understand the aims of the clause, but could not those be extended?

Mr. Brooke: To some extent I regret not having persisted in my original intention, which was, on clause 64, to take us through the seven clauses. The hon. Gentleman's proposition is not practical under the legislation.

Clause 99, as amended, ordered to stand part of the Bill.

Clause 100

POSTPONEMENT OF CHARGE ON DEEMED DISPOSAL

Amendments made:

No. 203, in page 80, line 7, leave out "the company" and insert

"a company to which this section applies by virtue of section 99 or (Deemed disposal of assets on company ceasing to be liable to UK tax) above ('the company')".

No. 204, in page 81, line 10, after "99(2)", insert

"or, as the case may be, section (Deemed disposal of assets on company ceasing to be liable to UK tax) (2)".

No. 205, in page 81, line 16, leave out

"in relation to a company".

No. 206, in page 81, line 17, at end insert—

" 'the relevant time' has the meaning given by section 99(1) or, as the case may be, section (Deemed disposal of assets on company ceasing to be liable to UK tax) (1) above;". [*Mr. Brooke.*]

Mr. Brooke: I beg to move amendment No. 286, in page 81, leave out lines 18 and 19 and insert—

"(7) For the purposes of this section a company is a 75 per cent subsidiary of another company if and so long as not less than 75 per

[Mr. Brooke.]

cent of its ordinary share capital is owned directly by that other company.".

The clause allows a United Kingdom resident principal company and its 75 per cent subsidiary, when the latter migrates, to elect to postpone the clause 99 charge on deemed disposal of assets in relation to foreign assets of a foreign trade. The charge is later activated when, *inter alia,* the principal company sells shares in the migrating company and as a result the latter ceases to be a 75 per cent subsidiary.

When there is a vertical chain of subsidiaries, there can be more than one principal company within the meaning of the Bill's provisions. Both the migrant company's immediate parent, and that company's own parent, could be principal companies, because both of them may control 75 per cent of the ordinary shares of the migrating company—one doing so directly, and the other indirectly. In those circumstances, the amendment makes it clear that it is the immediate parent that holds shares in the migrating company which has to make the election.

Amendment agreed to.

Clause 100, as amended, ordered to stand part of the Bill.

Clause 122

PROVISIONS FOR SECURING PAYMENT BY COMPANY OF OUTSTANDING TAX

Mr. Brooke: I beg to move amendment No. 287, in page 95, line 18, leave out "that" and insert "the relevant".

The Chairman: With this it will be convenient to take Government amendment No. 288.

Mr. Brooke: The amendments make drafting improvements. There is another place in clause 122 where the expression "that time" appears—line 12 of page 95—but I am advised that it is not appropriate to alter that, as it appears in the same subsection as the original expression "the relevant time", to which it refers.

Amendment agreed to.

Amendment made: No. 288, in page 95, line 24, leave out first "that" and insert "the relevant".—[*Mr. Brooke.*]

Mr. Brooke: I beg to move amendment No. 289, in page 95, line 35, leave out "which is".

The Chairman: With this it will be convenient to take Government amendments Nos. 290 to 295.

Mr. Brooke: The amendments make minor drafting improvements aimed at removal of doubt. Unless it is of importance to the Committee, I shall not expand on that statement.

Amendment agreed to.

Amendment made: No. 290, in page 96, line 3, at end insert—

"(7A) In this section and section 124 below any reference to the tax payable by a company in respect of periods beginning before any particular time includes a reference to any interest on the tax so payable, or on tax paid by it in respect of such periods, which it is liable to pay in respect of periods beginning before or after that time.".—[*Mr. Brooke.*]

Clause 122, as amended, ordered to stand part of the Bill.

Clause 123

PENALTIES FOR FAILURE TO COMPLY WITH SECTION 122

Amendments made: No. 291, in page 96, line 12, after "is", insert "or will be".

No. 292, in page 96, line 13, leave out "remains unpaid" and insert "has not been paid."

No. 293, in page 96, line 25, after "is", insert "or will be".

No. 294, in page 96, line 26, leave out "remains unpaid" and insert "has not been paid".—[*Mr. Brooke.*]

Clause 123, as amended, ordered to stand part of the Bill.

Clause 124

LIABILITY OF OTHER PERSONS FOR UNPAID TAX

Amendment made: No. 295, in page 97, line 21, leave out from "amount" to "within" in line 23.—[*Mr. Brooke.*]

Mr. Brooke: I beg to move amendment No. 296, in page 97, line 46, leave out from "means" to end of line 48 and insert—

"(a) where the time when the migrating company ceases to be resident in the United Kingdom is less than 12 months after 15 March 1988, the period beginning with that date and ending with that time;"

The amendment is in response to representations from a number of bodies and produces a worthwhile relaxation in the provisions of clause 124. The clause empowers the Inland Revenue to have recourse to certain group companies and directors with tax status within the 12 months before the date of a company's migration if it should default on its obligations to the Exchequer.

If a company were sold by its parent company before Budget day and migrated within 12 months of the sale, the former parent company and/or directors might become liable if it subsequently failed to pay the tax. That would be unreasonable because neither the former parent company nor the directors would have foreseen that possibility before the announcement of the new arrangements on Budget day. That element of retrospection has been removed by amending the definition of the relevant period so as to exclude any period before Budget day.

In the case of sales after Budget day, the parties involved will, of course, be aware of the risk of liability arising under clause 124 and can, if necessary, indemnify themselves against the possibility of default by the former subsidiary.

Amendment agreed to.

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

Mr. Howarth: Although I accept that we should take steps to ensure that any tax due from a migrating company is recovered, it is possible that the clause will go too far. For example, companies previously associated with a migrating company, and previous controlling directors of such a company, might be liable for tax due from the migrating company even though they had severed their links with that company. In short, the clause has certain undesirable prospective effects. The persons liable have no control over events subsequent to a sale.

Will the Paymaster General consider introducing a litigation provision under which taxpayers would not be liable if they were ignorant of a company's change of residence when it was sold, or if they made arrangements to meet tax liabilities arising?

Mr. Brooke: The amendment has some relevance to my hon. Friend's comment, but it would be difficult to argue that a group company or the controlling directors affected by the clause would be ignorant of the transaction. To be absolutely certain that my hon. Friend's question contains no substance that I have not already covered, I shall look at the issue, but with no commitment.

Clause 124, as amended, ordered to stand part of the Bill.

Clause 65

PRIORITY SHARE ALLOCATIONS FOR EMPLOYEES ETC

Mr. Worthington: I beg to move amendment No. 324, in page 61, line 46, at end insert

"except to the extent that any such benefit exceeds £2,500".

The Chairman: With this it will be convenient to take the following amendments:

No. 325, in page 61, line 46, at end insert

"except to the extent that any such benefit exceeds £2,000".

No. 326, in page 61, line 46, at end insert

"except to the extent that any such benefit exceeds £3,000".

No. 327, in page 621, line 46, at end insert

"except to the extent that any such benefit exceeds £4,000."

No. 328, in page 621, line 46, at end insert

"except to the extent that any such benefit exceeds £5,000".

Mr. Worthington: I can sense that we need brevity. I simply ask the Minister why he will not accept that there should be two extra provisos. First, there should be a monetary limit on the size of the benefit, and we offer a selection of such limits. Secondly, the terms of any such offer should be available to all on equal terms rather than on similar terms. The amendments are eminently reasonable. Will the Minister accept them?

Mr. Lamont: The clause deals with an exemption from income tax for the benefit arising from priority given to employees in the allotment of shares in a public offer. We are talking not about a discount, cheap shares or free shares but about priority in a public offer.

Before the hon. Member for Clydebank and Milngavie (Mr. Worthington) gets too excited, perhaps I should explain that it has always been believed that there is no liability to tax, so the Government are not making a sudden extension. We have merely put the law back to what it was thought to be.

Because we were advised that this benefit should be taxable as an emolument—I stress that we are talking about shares in a public offer, occurring probably once in a company's lifetime—we considered introducing a cap, as the hon. Member for Clydebank and MIlngavie proposed. However, that solution is not quite as simple as the hon. Gentleman suggested because we have to attempt to value the benefit obtained by the priority. We have to take into account the various methods by which shares are allocated when an offer is oversubscribed and these may make the assessment of the benefit extremely difficult. For example, if an employee received the full number of shares for which he applied and shares were allocated to members of the public by ballot, so that some people were allotted the full number for which they applied while others received none, or if in another offer there was a scaling down, it would be a complicated operation to calculate the value of the priority.

The hon. Member for Clydebank and Milngavie has perhaps not noticed that restrictions are built into the amount of benefit. The effect of the clause will be that individual benefit from the priority in allocation cannot be excessive. It includes special provision to restrict the number of shares that may be allocated to employees to 10 per cent or fewer of the shares subject to the offer. Priority must be given to employees on similar terms. Similar terms does not mean identical terms. The terms may take account of salary and length of service, but they cannot be confined to directors or higher-paid employees. There is a reasonable number of safeguards.

I emphasise that this is a once-in-a-lifetime event when a company comes on the market. I am not aware of the problems that have motivated the amendment. We have never had similar complaints when companies have given employees priority in shares, and I should have thought that most companies were anxious not to sour relationships with their work force. On simple common sense, balanced against the complexity involved, I advise that the amendment not be pressed.

11.45 pm

Mr. Worthington: I wanted to deal with this matter simply. Abuses have been brought to our notice. Only

[Mr. Worthington.]

last week the *Financial Times* reported on a survey that was conducted by Paisner and Co. It brought to our attention the case of Caradon, the plastics and valves manufacturing company, whose senior employees were allowed a share price of 7p but at the time of the flotation the value, based on the share price, was 250p. That is rapid inflation. Although companies frequently say that their reason for going on to the market is to widen their share ownership, this rarely occurs.

Mr. Lamont: The hon. Gentleman is probably talking about an option scheme, not the issue of shares at the time of the public offer to employees. That is completely different.

Mr. Worthington: I accept that, but there is a link with clause 66, which we are soon to debate. I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Mr. Worthington: I beg to move amendment No. 329, in page 62, line 6, leave out sub-paragraph (b) and insert

"(b) that all the employees are entitled to such an allocation and are entitled to it on equal terms;".

I should like to make a number of points on the growth of a number of schemes that help a privileged group of employees. I have spoken of the Paisner survey. Coopers and Lybrand's report of a survey of 1,000 companies showed that 67 per cent operated executive share option schemes. This rose to 84 per cent among the largest firms. The general profit-sharing schemes of employees were offered by only 16 per cent of the 1,000 companies.

The report of the Paisner survey in the *Financial Times* of 13 June stated that directors and senior executives of newly floated companies had been making massive tax shelter gains as a result of share options granted in the six to 12 months before they went public, with directors seeking to establish as low a price as possible because all subsequent gains were tax free. In the firm of Caradon, the directors established for themselves a price of 7p, although at the time of flotation the price was 250p.

The Chairman: Order. The hon. Member seems to be anticipating clause 66. We are still debating clause 65.

Mr. Worthington: I am sorry, Mr. Hunt. I thought that we were on clause 66.

The Chairman: No. We are debating amendment No. 329, which relates to clause 65.

Amendment negatived.

Clause 65 ordered to stand part of the Bill.

Clause 66

SHARE OPTIONS: LOANS

Mr. Worthington: I beg to move amendment No. 330, in page 62, line 32, at end, insert

"provided it does not diminish the value of the shares to which it relates".

The Chairman: With this it will be convenient to take amendment No. 331, in page 62, line 39, at end add

"provided it does not diminish the value of the shares to which it relates".

11.50 pm

Sitting suspended for a Division in the House.

12.5 am

On resuming—

Mr. Worthington: I have already stated our main objections to the clause. We fear that many of the schemes are abused through the setting of artificially low prices, and that a privileged group of employees benefit from them.

There is a further point on which I seek an answer from the Minister. The provision deals with loans to acquire option shares, but it does not seem to be limited to such loans. There is a possible loophole. An option holder might borrow money from a bank and the shares that are the subject of the option might be pledged. There is no requirement that the money so borrowed must be used only to acquire the option shares. It could be used to buy a car or to pay for a foreign holiday, which does not seem to have been the Government's intention.

Our main argument is the possible abuse of such schemes, but we thought that it might be useful to draw to the Government's attention a possible loophole.

Mr. Lamont: I shall study what the hon. Gentleman said about abuse of option schemes. I am not familiar with the cases that he mentioned, but I do not think that they pertain to the clause.

The purpose of the clause is to assist those who wish to exercise a share option. As the hon. Gentleman acknowledged, the shares to which options relate must not be subject to restrictions which do not attach to all shares of the same class. That is to avoid the problem of manipulation, to which the hon. Gentleman referred. The purpose is to protect employees by ensuring that they have a right to acquire genuine shares, and to prevent companies from artificially influencing the value.

A loan taken out by option holders to fund the exercise of their options could also be caught under the existing anti-avoidance and anti-manipulation provisions. If the shares were pledged as security for the loan, or if the employee was committed to disposing of some of the shares to finance repayment of a loan, his freedom to dispose of some of his shares would be restricted. The shares would thus be restricted shares within the meaning of the legislation, and option holders acquiring those shares would lose their entitlement to relief.

The clause removes that unnecessary consequence. It is not intended to catch people who are using a loan legitimately to exercise an option. I have never found the Inland Revenue to be other than vigilant towards abuse and manipulation. The Revenue has advised me that the circumstances envisaged in the amendment are extremely far-fetched and that it would be inappropriate to amend the legislation. I shall, however, study what the hon. Gentleman said, to reassure myself that we do not need to buttress the provisions. I hope that he will accept that it is appropriate to alter the anti-avoidance provisions to enable people to use loans for the exercise of options.

Mr. Worthington: We wanted to put on record our anxiety about possible abuses of the schemes and about the fact that benefits were going too exclusively to the top 2 or 3 per cent in any company. We also wanted to draw the Minister's attention to a possible abuse. The amendment was a probing one. Following our short exchange, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 66 ordered to stand part of the Bill.

Clause 67

CHARITIES: PAYROLL DEDUCTION SCHEME

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

Mr. Doug Henderson (Newcastle upon Tyne, North): I sense that the Committee would consider it wise if I truncated what I might have said.

There has been some criticism of the payroll scheme by the *Financial Times*, which described it as a disappointing start, the *Investors Chronicle* which noted that only 15,000 people in the United Kingdom were covered by the scheme and the "Panorama" survey last week which noted that only two executives had availed themselves of the opportunity to help charity in that way. That contrasts with some of the Government's statements, particularly those made by Economic Secretary on 25 November 1987 when he addressed the Westminster Committee for the Protection of Children.

I wish to put some straightforward questions to the Government in the interests of time. What are the latest estimates of the number of employees covered by the scheme? How much will the changes proposed by the Government cost the Inland Revenue? Can the Paymaster General assure us that charitable donations are not intended as a substitute for the welfare state? Will he acknowledge that there are better ways to help the voluntary sector, institutions such as hospices, and so on? Finally, is the Paymaster General as pleased with the scheme as the Economic Secretary was and what answers can he give to those who argue that it is not much more than a gimmick?

Mr. Brooke: I am embarrassed by the first question put by the hon. Member for Newcastle upon Tyne, North (Mr. Henderson) because I recently answered a parliamentary question on that issue but cannot remember the precise figure. However, I shall get an answer to him.

The cost of the change in the scheme was recorded in our own forecasts as negligible. The Government do not think that charities should be a substitute for the welfare state, but charitable giving, the work of charities and the voluntary sector represent an effective way of responding to a series of needs in different parts of society. That does not apply only to welfare needs but to needs met by organisations such as the Royal Society for the Protection of Birds. Help given to the voluntary sector overall is substantial and has grown, just as charitable giving has risen sharply in the past ten years.

The hon. Gentleman asked about the Government's reaction to the progress of the scheme. We are encouraged by the number of employers who have made the scheme available—2,700 schemes have already been set up. In the Civil Service, where the Government are the direct employer, 435,000 civil servants are now eligible and arrangements have been made for a further 161,000 to join.

I would be the first to acknowledge that the exercise of persuading employees to take part in the scheme is a marketing exercise which sets charities a new challenge because once the scheme is set up with an employer it is necessary to communicate with the employees. By definition, it is the charities which logically should do that as they will be the beneficiaries. How they get things moving is a new test for them.

The Government believe that collaborative discussion is needed between employers, charities and the Government about how that educational and marketing process can be carried forward. The Chancellor will conduct a seminar on 18 July to which representatives of all the groups that I have mentioned, including trade union leaders, have been invited. We can have a round table discussion about what the various interested parties might do to encourage people to take part as it is a worthwhile scheme and the first occasion in British tax history when it has been possible for an employee to make a contribution to charity as a direct deduction from his income.

12.15 am

The answer to the question asked by the hon. Member for Newcastle upon Tyne, North is that we are making progress but, we think that we could make better progress still. The answer to the question that he asked at the beginning is that at least 40,000 people already participate, as against the 15,000 that he cited. A great many more are eligible in that their employers are making schemes available.

Mr. Henderson: If the Paymaster General had made that contribution at the Conservative party conference it would have been seen as a motion seeking the remission of the substantive motion. There are gaps in the Government's answer. I am glad that the Paymaster General was eventually able to give me some figures on the number of employees covered by the scheme. He raised the point about the number of employers who had agreed to take part in the scheme. He also

[Mr. Henderson.]

acknowledges that the real challenge is not to get the employers, although it is interesting that employers are prepared to make facilities available for their employees but not to dig into their own pockets.

Mr. Brooke: The hon. Gentleman has no grounds for that observation. The amount of contribution from employers and companies to charities has grown sharply in the past ten years.

Mr. Henderson: According to the "Panorama" survey and others, individual directors do not seem to be making the same contributions that they expect their employees to make. The Paymaster General's answer shows that the Government need to look again at the whole scheme to make sure that it works. The Opposition want it to work. It would be wrong to put the onus on us to force a vote on the clause. The responsibility lies with the Government to withdraw it and consider it at a later stage in the Bill.

Question put and agreed to.

Clause 67 ordered to stand part of the Bill.

Clause 68

ENTERTAINMENT OF OVERSEAS CUSTOMERS

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

Mr. Campbell-Savours: Very briefly, I should like to know the cost of the concession, particularly to industry. I may have misunderstood the effects of the clause, but there are a number of buying houses in London which represent many industries in the United Kingdom and act as centres to which overseas companies can send representatives to see ranges of British goods. Very often they have to entertain these overseas customers. Although they handle a vast amount of business, their turnovers may be small. A large propeotion of their turnover may be involved in entertaining customers from overseas. I do not know whether any representations have been made by such buying houses or how many there are, but when I used to visit them years ago they were doing extensive business and many British companies relied on their activities. Have they made representations? They may be major sufferers under the arrangement, unless I have misunderstood the position.

Mr. Nicholas Brown: the British Exporters Association has made representations to members of the Committee. Its letter to me begins:

> "I am sure you must have been as concerned as I was to hear last Thursday that our current account deficit in the First Quarter 1988 was actually *a staggering £2.8 billion.*
>
> The deficit on visible trade was *£4 billion.*
>
> What is the Chancellor doing about it?"

The letter continues to indict the government. It was written by Mr. I. J. Campbell, chairman of the British Exporters Association. He sets out the experience of his company in making the case for the continuing tax relief as follows:

> "The major element of my marketing expenditure, apart from the costs of frequent and regular visits to my customers, is entertaining them when they visit the United Kingdom (since, in many cases, restricted foreign exchange availability in their home country would prevent such travel) and carefully chosen, small personal gifts at Christmas, at the Eid, on birthdays, on the occasion of weddings.
>
> Under your proposed changes, these items no longer class as tax deductible. On the other hand, I could commission a major advertising campaign—costing several thousands of pounds—to put my company's name on every roadside hoarding in Lagos, which would not bring me one extra Naire's worth of business and yet would be fully allowable against my profits and therefore tax deductible. Can you explain to me the logic behind this?"

It is only right that the Government should answer that question.

Mr. Howarth: In reply to the hon. Member for Newcastle upon Tyne, East (Mr. Brown), no British exporter doing business with Nigeria has ever been able to give a small Christmas present, but I do not want to open that can of worms because we may get into difficult territory.

Representations made to me by the banking community suggest that an overseas branch of a British bank may be liable for tax on its entertaining in the overseas country. According to the rules of that overseas country, the entertainment may be deductible from the bank's profits. Under the clause, that may be written back into the parent bank's overall tax position. British banks and British branches of British companies may then be uncompetitive overseas. That is not just a theoretical point.

In Germany, entertainment costs are fully deductible and in the United States of America, 80 per cent of costs are deductible, so a British branch of a United Kingdom company may have to operate at a substantial competitive disadvantage. The issue is not the entertaining of overseas customers in the United Kingdom, but entertaining by British branches overseas. Will my right honourable Friend the Minister comment on that?

Mr. Lamont: The clause gives effect to the proposal in the Budget to withdraw special relief for the costs that businesses incur in providing entertainment and gifts to overseas customers. The cost of providing business entertainment and gifts was originally allowable as a deduction from profits for tax purposes, just like other business expenses. Following widespread abuse, relief for that expenditure was generally withdrawn in 1965, but an exception was made for the costs of entertainment and gifts for overseas customers.

We firmly believe that such special reliefs are no longer appropriate following the tax reforms and reductions in the rates of corporation tax and income tax. We have one of the lowest corporation tax rates in the world. The yield will be about £5 million. We have had representations from many organisations—not from the firms described by the hon. Member for Workington (Mr. Campbell-Savours), but from the British Exporters Association, as the hon. Member for Newcastle upon Tyne, East (Mr. Brown) said, and also from the British Bankers Association.

The hon. Member for Newcastle upon Tyne, East referred to the argument that it would be cheaper to give gifts than to advertise. I do not find that a persuasive argument. Entertainment relief was originally abolished in 1965 because it was being widely abused. It is quite appropriate for firms to advertise and the scope for abuse is not available to the same extent.

The British Bankers Association, about which my hon. Friend the Member for Cannock and Burntwood (Mr. Howarth) asked, has solemnly made a representation to us that the relief should be continued for expenditure incurred by overseas branches of United Kingdom businesses, but that would defeat the whole purpose of the clause. The association argues that the clause will make it more likely that firms will choose to operate abroad through subsidiaries rather than branches, but I believe that that greatly overstates the likely effect on businesses' commercial decisions. As I have said before, we want to remove special reliefs of this kind and we should take account of the fact that this country has one of the lowest corporation taxes. That suggestion should therefore be thoroughly rejected.

Question put and agreed to.

Clause 68 ordered to stand part of the Bill.

Clause 69 ordererd to stand part of the Bill.

Clause 70

PREMIUMS FOR LEASES ETC

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

Mr. Campbell-Savours: Perhaps I am a bit thick, but I do not understand what clause 70 means. Will the Minister explain?

Mr. Lamont: This clause goes with other clauses relating to top-slicing relief. It removes a tax relief of limited application which is no longer necessary now that income tax rates are reduced to the levels proposed in the current Finance Bill.

The relief was originally introduced in 1963, when taxes were very much higher, to mitigate the effect of the very high top rate of income tax on premiums for short leases and certain other payments received in connection with leases. I shall explain what that involves.

If a landlord lets property for a period of 50 years or less and charges a premium, the premium—or part of it—is charged to income tax under schedule A in the year in which the lease is granted. Any part of a premium not charged to tax under schedule A falls to be taxed as a capital gain, or in some circumstances as a trading receipt.

If premiums for short leases were not charged to income tax, landlords could reduce their income tax liability on rents by charging artifically low rents and artificially high premiums. The schedule A rules counter that by treating part of the premium as though it were rent. Where the lease is for less than two years, the whole of the premium is taxed as rent. For longer leases—up to 50 years—there is a sliding scale and the amount chargeable is reduced by 2 per cent for each full year after the first for which the lease runs.

Where part of a premium is treated for tax as though it were rent, the landlord is, in effect, assessed on what is notionally more than one year's income—that is, a string of rental payments—in one year. That can have the effect of making the landlord liable to tax on that part of the premium at higher rates than those at which he would have been liable if the premium had been spread evenly over a period of years. We are doing away with a top-slicing relief which was introduced to soften that effect by enabling a landlord to claim that the tax on the premium was to be calculated at the rate or rates of tax which would have applied if he had received only one year's part of the premium in the year in which the lease was granted. Now that we have made dramatic reductions and there is to be only one top rate of income tax, such top-slicing provisions are no longer appropriate.

Question put and agreed to.

Clause 70 ordered to stand part of the Bill.

12.30 am

Clauses 71 to 85 ordered to stand part of the Bill.

Clause 86

SALES WITHOUT CHANGE OF CONTROL

Mr. Hunter: I beg to move amendment No. 342, in page 72, line 43, leave out "after the sale" and insert

"after the end of the accounting period in which the sale took place".

The Chairman: With this it will be convenient to take amendment No. 343, in clause 87, page 73, line 15, leave out "after that time" and insert

"after the end of the accounting period in which the succession took place".

Mr. Hunter: Amendment No. 342 is a probing amendment. It would alter the new two-year time limit within which claims have to be made by taxpayers to treat transfers of assets at their tax written down value. My right honourable Friend the Financial Secretary will be aware of the supporting arguments.

Amendment No. 343, which is also a probing amendment, would alter the new two-year time limit within which claims have to be made by connected taxpayers with capital allowances on machinery and plant to be treated on a continuing basis as though there had been no change in ownership of the relevant trade. Again, my right honourable Friend will be aware of the supporting arguments. I am sure that he will respond warmly to these probing amendments.

Dr. John Marek (Wrexham): If the Minister is minded to accept the spirit of the amendment, the Opposition would like the two years reduced to one year.

Mr. Lamont: We are all indebted to my hon. Friend the Member for Basingstoke (Mr. Hunter) for his vigilance in continuing to probe late into the night. I shall explain the effect of the clause before responding to the amendments.

The clause is essentially tidying-up legislation. There is nothing new about the capital allowance provision which permits an election for continuation treatment where the parties to a sale of assets are associated. Where there is a transfer of assets between two connected persons, the person to whom the transfer is made is able to stand in the shoes of the person who had the original capital allowance. The view taken hitherto has been that since an election must be followed by a claim to capital allowances, the time limit has to be that for such a claim. This is strictly the 30-day time limit for a return although, in practice, it has been extended up to the time when the relevant assessment becomes final and conclusive. Providing for a two-year time limit has two advantages. First, a specific statutory time limit will make for greater certainty in the matter. Secondly, two years is the time laid down elsewhere in capital allowance legislation within which elections have to be made.

The aim of amendment No. 343 is to enable the time limit to run from the end of the accounting period in which the sale takes place rather than from the date of the sale itself. I appreciate that that might be administratively more convenient for taxpayers and their advisers, but it overlooks the point that we are dealing with the affairs not of one taxpayer but of both parties to the transaction. It is not unknown for people who are connected to have different tax advisers and different chargeable periods. Where an election needs to be made jointly by both parties to a transaction, it is logical for the time limit to run from the date of the event, which will be known to all the parties concerned. That is the general pattern adopted in capital allowance legislation in dealing with elections affecting the liability of more than one person.

Amendment No. 343 would allow the two-year limit to run from the end of the accounting period in which the event—in this instance, the succession to the trade—takes place rather than from the date of the event itself. I cannot recommend that the Committee accept that. The general pattern of time limits for election for capital allowances is to allow two years from the end of the chargeable period in which the event occurs where only one person is involved, but not where there are two sides to the transactions, as in the case of successions to trade. Logic and equity demand that in such circumstances the time limit should run from the date of the event. The arguments on the second amendment are similar to those on the first.

Mr. Hunter: In the light of those comments, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Clause 86 ordered to stand part of the Bill.

Clauses 87 to 90 ordered to stand part of the Bill.

Further consideration adjourned.—[*Mr. Lennox-Boyd.*]

Adjourned accordingly at twenty-five minutes to One o'clock till Thursday 23 June at half-past Four o'clock.

THE FOLLOWING MEMBERS ATTENDED THE COMMITTEE:

Hunt, Mr. John *(Chairman)*
Arbuthnot, Mr.
Armstrong, Ms
Battle, Mr.
Boswell, Mr.
Bright, Mr.
Brooke, Mr.
Brown, Mr. Gordon
Brown, Mr. Nicholas
Butterfill, Mr.
Campbell-Savours, Mr.
Carrington, Mr.
Coombs, Mr. Anthony
Darling, Mr.
Davies, Mr. Quentin
Favell, Mr.
Forman, Mr.
Griffiths, Mr. Nigel
Henderson, Mr.
Howarth, Mr. Gerald
Hunter, Mr.
Ingram, Mr.
Jack, Mr.
Lamont, Mr. Norman
Lennox-Boyd, Mr.
Lilley, Mr.
Major, Mr.
Maples, Mr.
Marek, Dr.
Mitchell, Mr. Andrew
Morgan, Mr.
Nicholson, Mr. David
Quin, Ms
Shaw, Mr. David
Smith, Mr. Andrew
Smith, Mr. Chris
Stern, Mr.
Taylor, Mr. Ian
Wallace, Mr.
Wardle, Mr. Charles
Watts, Mr.
Widdecombe, Miss
Worthington, Mr.