

Treasury Committee

Oral evidence: The work of the Chancellor of the Exchequer, HC 424

Wednesday 25 April 2018

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Members present: Nicky Morgan (Chair); Rushanara Ali; Mr Simon Clarke; Charlie Elphicke; Stephen Hammond; Stewart Hosie; Mr Alister Jack; Alison McGovern; Catherine McKinnell; John Mann; Wes Streeting.

Questions 107-263

Witnesses

I: Rt Hon Philip Hammond MP, Chancellor of the Exchequer, and Sir Tom Scholar, Permanent Secretary, HM Treasury



Examination of witnesses

Rt Hon Philip Hammond MP and Sir Tom Scholar

Q107 **Chair:** Thank you both very much indeed for coming in this afternoon. I am not going to ask you to introduce yourselves. I think if we don't know you by now for the record then we never will. Anything you want to share from the Brexit war cabinet, Chancellor?

Mr Philip Hammond: No, thank you.

Q108 **Chair:** I thought it was worth asking. I do want to start on the issue of Brexit, which won't surprise you. We have had a letter in, following some questions we asked Robert Chote when he was last before us, about the OBR preparing a forecast on the withdrawal agreement before Parliament has the final vote. Chancellor, when you were last before us I think you committed to put the maximum amount of analysis, as you said it, in the public domain before Parliament comes to vote on the withdrawal agreement. I would be grateful if you could take us through your thinking on what that analysis might be, particularly around the timing. As you will have seen, perhaps, in Robert Chote's letter, there is the issue of the ability for them to produce separate forecasts or how that ties in with a likely budget timetable.

Mr Philip Hammond: Yes. First of all I thought that Robert Chote's letter to you set out very clearly and sensibly some of the issues here and I think a lot of colleagues in Parliament got into a groove of saying, "We will get the OBR to produce analysis for us" and perhaps had in mind a big piece of comparative analysis of the likely consequences of different outcomes. I think Robert Chote is explaining very clearly here why that is not likely to be something that they could realistically do. I haven't set a date for the autumn Budget yet but I can reveal that it will be in the autumn.

Q109 **Chair:** That is quite a loose term though for Government, isn't it?

Mr Philip Hammond: It is a pretty loose term, yes. I think that means sometime between the beginning of the short session in September and the Christmas recess.

The other thing we don't know is when the meaningful vote will be held in Parliament. What I said to you the last time I was before you was in relation to work that the Government are doing, the Treasury and other Departments are doing, which we do not feel it appropriate to make public at the moment because of the confidentiality considerations around the negotiations. Once we get to a point where there is an agreement, and it is being put before Parliament, the concerns about negotiating confidentiality melt away and it would be appropriate. There would be no reason not to make that information available to Parliament and indeed it would be very helpful for Parliament to have it. I have made a commitment to you, which I will reiterate today, to maximum possible transparency on our data and modelling once we get to that point where



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we have a deal and we are putting it before Parliament to deliver a meaningful vote on.

Q110 **Chair:** Is it too early to say at the moment what that information is likely to consist of? Will it include economic and fiscal consequences of the withdrawal agreement and on what basis? Would it examine the future relationship or is it just too early to say?

Mr Philip Hammond: I think it is too early to say with any precision. The Committee will understand the kind of things that are likely to be covered. Of course the other thing that we don't know at this stage is the degree of detail that there will be in the future framework document published alongside the withdrawal agreement, so the extent that it will be possible to model, even in our internal terms—certainly not the OBR's rather more formal terms—the consequences of the future framework that is set out.

Q111 **Chair:** Yesterday the Comptroller and Auditor General, Sir Amyas Morse—who I think Mr Scholar had the pleasure of appearing in front of although he didn't say anything at the hearing of the Public Accounts Committee on Monday—appearing before us. The National Audit Office has done a report on the financial settlement as far as it can at the moment. We debated with him about whether those payments had to be paid, irrespective of whether there is a trade agreement between the UK and the EU. What is your interpretation of when that financial settlement has to be paid and when it would not be paid?

Mr Philip Hammond: The UK has always taken the position that we are a rule of law state. We always respect of our obligations and if we have obligations we will meet them. It is clear that we do have our obligations under the multiannual financial framework of the European Union and arguably obligations beyond that.

The approach that has been taken in this negotiation is to look at the claims from the European Union side, to analyse them carefully and to challenge them. A long process of challenge has gone on but in the end we have taken a view that in order to facilitate the progress of negotiations there would be a set of principles that we could agree. At the margin there will necessarily be some uncertainty about whether more would have been included or perhaps slightly less would have been included if this had ultimately not been agreed and had gone through some form of legal tribunal to determine.

Much of the legal basis is quite novel. This is not the sort of thing that is determined in the courts every day and it is clear that there are areas at the margin, but in the grand scheme of things, and in the interests of moving forward and looking at the relative scale of the financial settlement and the likely economic and fiscal impacts of the difference between getting a good deal and getting a less good deal, we have taken a view that this is a sensible and pragmatic approach and a sensible way to go forward.



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Q112 **Chair:** I think Stewart is going to ask you a question in a moment about some little bits around the edges. When Robert Chote came before us recently he said that, "The direct costs arising from the financial settlement will be dwarfed by the wider economic impact of Brexit on the public finances". Do you agree with that?

Mr Philip Hammond: I think that in the grand scheme of things much larger numbers are in play when we look at the potential economic costs and benefits of different outcomes and the consequent fiscal costs and benefits.

Q113 **Stewart Hosie:** Chancellor, can you confirm that the Government's estimate of £35 billion to £39 billion for the financial settlement, the divorce cost, includes payments from the EU direct to the UK private sector?

Mr Philip Hammond: Yes, it does. Yes, it is in that figure.

Q114 **Stewart Hosie:** Is it not the case that stripping out these payments that is focusing on the cost to the public finances would result in a higher figure for the financial settlement?

Mr Philip Hammond: Technically you are correct, but I don't understand the point. We have made a commitment to support certain kinds of EU funding in the UK after 2019: funding for projects that have been approved by the European Union, which fit within our criteria, funding for the agriculture sector and, therefore, if that funding was not forthcoming from the European Union it would be a direct cost to the UK Exchequer. On the basis of the guarantees, underwritings and commitments that we have made, not the EU but to our own citizens, this is a net figure because every pound that the EU continues to pay, for example to British agriculture, is a pound that we don't have to pay in order to make good on our commitments.

Q115 **Stewart Hosie:** That is exactly the point. The implication there is that during the period of divorce when the settlement figure was made those payments from the EU will continue to be made from the EU. Is that the case? Is that the working assumption?

Mr Philip Hammond: During the implementation period they will continue to be made.

Q116 **Stewart Hosie:** We understand that the final figure that the UK will have to pay during some kind of prolonged transition while the new framework is arranged could be higher. Is it the UK Government's intention to continue to fund or to match the funding that will be lost from the EU to the private sector in full?

Mr Philip Hammond: Part of the point of leaving the EU is that Parliament will make the decisions about what we do with our money in the future instead of sending it to Brussels so that Brussels can decide what to do with it. We have announced the creation of the UK Shared Prosperity Fund but the exact amounts and the allocation between



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different sectors, different uses of that money, will be a matter for the UK Parliament.

Q117 Stewart Hosie: I understand the philosophical argument that the UK Parliament will decide or the Government will decide where funding will be allocated, but the answer is vague in the sense that it leaves those businesses, farmers and others who currently receive payments in a bit of a limbo, uncertain as to what the future might hold given there is pretty decent certainty where the EU would put its money in the next five to 10 years, does it not?

Mr Philip Hammond: I think we have moved swiftly after the referendum in 2016 to provide certainty and particularly to the agricultural sector, which knows with certainty what it will be receiving through to at least the end of the implementation period. But of course we have to have a debate domestically about our future policies, including in relation to agriculture, and it would be wrong, at this stage, to make rigid commitments before we know the full shape of the deal that we are going to do and what the implications are likely to be for the wider UK economy. It seems to me quite sensible that we maintain the flexibility to have that debate domestically once we understand what shape and size of our economy will be going forward. But I do take your point that there must be a certain amount of forward notice and there will come a point when it becomes necessary for the UK Parliament, the Government, to reach decisions about these things in order to allow people operating in different sectors of the economy to have appropriate foresight of what their position is going to be.

Q118 Stewart Hosie: But given this funding could effectively end at the end of the implementation or transition period, advance notice needs to be given very quickly indeed if there are sectors who are depending on some of the £7 billion or so a year still being there in three years, four years or five years' time. When would a decision be taken? When would that advice be given to the private sectors who are currently in receipt of direct payments from the EU? I think it is only fair and proper that those business sectors understand what the financial framework might look like.

Mr Philip Hammond: Yes. I have it in my mind that we have made a commitment during 2018 to begin the consultation on future agricultural arrangements. That is a DEFRA lead obviously. I will confirm that to the Committee but that is what I have in the back of my mind that we have said during 2018 we will begin that process.

Q119 Stewart Hosie: That would be most helpful and when you are confirming that to the Committee, if you could confirm the same would apply to the other sectors who are in receipt of that cash, it would also be helpful if that was to come forward.



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Mr Philip Hammond: Yes. I am not sure we have made similar commitments in all sectors but agriculture, of course, is probably the largest single recipient of EU funding flows.

Stewart Hosie: You have the opportunity to make a firm commitment right now.

Q120 **Chair:** That invitation has not been accepted, I don't think. Chancellor, the other thing that Sir Amyas Morse said yesterday is that he is assuming the rebate will not be there anymore after the withdrawal agreement. I think he said that after the implementation period has ended, in order to honour future obligations, the rebate that we have relied on as a country for many years would not be part of the calculations. Is that something the Treasury has looked at?

Sir Tom Scholar: One of the key determinants of what we pay post 2020 is our financing share and the financing share is calculated taking the average of what it turned out to be from 2014 to 2020 and that does incorporate the rebate within it because it is based on—

Q121 **Chair:** That is expected to go on until future payments are no longer owed.

Sir Tom Scholar: The financing share will then be fixed at the end once the figures for 2020 are known and that financing share will apply to all future payments.

Q122 **Chair:** Let me move on to sanctions and Russia, which obviously has also been very much in the news. In an article from *The Telegraph* of this month the FCA have been talking about the floatation of EN so we consulted with the relevant authorities according to the usual protocols. Is the Treasury's Office for Sanctions Implementation part of those usual protocols?

Mr Philip Hammond: I am sorry. I am not sure I understand the question. Whose usual protocols?

Chair: Presumably there is a company such as EN, which wanted to float or did float on the London Stock Exchange. Where there are national security interests there is a set of protocols where various relevant people are consulted. Is the Treasury's Office for Sanctions Implementation part of that discussion?

Mr Philip Hammond: There are two separate issues here I think. There is, first of all, the responsibility of the listing authorities and the Financial Conduct Authority, both of which are independent of Government, and then there is Government's review and how we look at these things internally. It would normally be the National Security Adviser that would lead such a process. The Treasury would certainly be included in that consultation and I imagined, within the machinery of the Treasury, the Office of Financial Sanctions would have an interest in that.



Sir Tom Scholar: Yes. They lead on anything to do with implementation of sanctions.

Q123 **Chair:** The reason I am asking is because VTB was very involved in the outcome of the floatation which is the bank currently affected by sanctions. It might be something that you want to write to the Committee about, but in the floatation of EN, VTB, which is the bank currently affected by sanctions—this is something that has come up in front of the Foreign Affairs Select Committee—may very well have benefited from the floatation and that may not be something that the Office for Sanctions Implementation would have wanted. Perhaps you could—

Mr Philip Hammond: I will certainly look at it. If an entity is sanctioned there will be restrictions on what that entity can do but we do have—and I think this is sometimes not appreciated in some of the things I read about sanctions—a rule of law based system. People don't just get sanctioned because we don't like the look of them. Sanctions are based on very clear criteria. They are open to challenge in the courts and all of this is done according to very strict rules. If there is an entity that is sanctioned and there are restrictions on it being involved, for example, in a listing process of another entity, we would enforce those restrictions.

Q124 **Chair:** The US imposed some additional sanctions within the last couple of weeks. Is that something that the UK is intending to mirror or the UK has been discussing with EU counterparts in terms of mirroring?

Mr Philip Hammond: We welcomed the action that the United States has taken and we very much appreciate the support for our position in the wake of the Salisbury attack in particular, which we have had from the US and many other countries. We have two bases in the UK for sanctions. Almost exclusively they are either based on UN resolutions, which are binding automatically on all member states of the United Nations, or they are based on European Union measures. While we are still members of the European Union we do not have, with some very narrow exceptions, an independent sanctioning capability. We are discussing with European Union partners the measures that the US and others have taken.

I think it is probably fair to say that there are varying degrees of appetite within the European Union for further pressure on this group of individuals and one of the challenges of working within the European Union is that in these areas such as foreign policy, one is required to build a consensus of 28, which means operating frankly at the lowest common denominator quite often.

Chair: I will not say that applies to building a consensus in Cabinet but others can draw their own conclusions. We are going to move to fiscal targets.

Q125 **Alison McGovern:** Before I do, with your forbearance, Chair, I just wanted to follow up, Chancellor, on one thing that you said earlier on Brexit. If I heard you correctly, you said that compared to the Brexit bill



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that Stewart was asking about, much larger numbers are in play when we think about the wider impacts. Do you think those much larger numbers, the potential cost to our country, might be ameliorated if we remained in the customs union?

Mr Philip Hammond: You are putting words into my mouth. I didn't talk about costs. I said much larger numbers in either costs or benefits of various different scenarios that people are discussing. That would include potential reductions in trade with the European Union. It would include potential increases in trade with countries beyond the European Union. It would include the impacts of frictional costs on any given level of trade between us and the European Union. The point I am simply making is that over a reasonable period of time, 10 to 15 years—and we are talking about the settlement costs being spread over a long period of time—the potential economic and even the potential fiscal costs will be orders of a magnitude bigger than these.

Q126 **Alison McGovern:** It is precisely those costs and benefits that we will have to weigh when we consider the Government's—

Mr Philip Hammond: I think that would be the right thing for Parliament to do, to look at the stream of costs and benefits, some are monetisable and some are not. There are clearly consequences of leaving the European Union and different forms that Brexit might take, which are not readily monetisable but will, nonetheless, have impact and people will want to make at least qualitative assessments of the value of those outcomes.

Q127 **Alison McGovern:** To come to the Charter for Budget Responsibility, which at the moment states that, "The Treasury's objective for fiscal policy is to return the public finances to balance at the earliest possible date in the next Parliament". Of course that statement is made somewhat ambiguous by the fact that we have had an election. Are you going to update the charter?

Mr Philip Hammond: I have not announced any plans to do so. It remains our policy intention to move towards a balanced balance in the mid-2020s. We have intermediate measures that bite in 2021.

Q128 **Alison McGovern:** Don't you think that it is ambiguous leaving it uncertain in that way?

Mr Philip Hammond: What is uncertain? In 2021 we will have debt falling and we will have a structurally adjusted deficit below 2% of GDP as a milestone on the way to the ambition to have a balanced budget in the mid-2020s. That doesn't seem to be ambiguous to me at all.

Q129 **Alison McGovern:** The mid-2020s I guess could be like your description of autumn earlier, somewhat here or there.

Mr Philip Hammond: Fiscal forecasting is perhaps not a precise science, more an art. I think the mid-2020s is a term that most people would understand pretty well.



Q130 **Alison McGovern:** That brings me to my last question on this issue. When you look back on the missed deficit target of the Parliament 2010 to 2015, what lesson do you draw from that?

Mr Philip Hammond: What target are you talking about?

Alison McGovern: The target that the incoming Chancellor, after the 2010 general election, set himself.

Mr Philip Hammond: The then Chancellor set out a set of targets to be delivered within the 2010 to 2015 Parliament and he subsequently adjusted those targets to set a 2018 fiscal target date. When I became Chancellor I decided that in the circumstances that we then faced, with the uncertainty that had been created by the referendum decision and the likely impact on business investment and consumer confidence, it would be more sensible to give ourselves a little more headroom in the management of the economy, even though that meant delaying the achievement of the deficit reduction target. I am very satisfied with the trajectory that we have seen. We have seen borrowing last year return to pre-crisis levels. We have seen the OBR forecast that this year our debt will begin to fall as a share of GDP for the first time in 17 years, which points to an economy that is moving in the right direction. I think we are moving, first of all, in the right direction and I think we are moving at the right pace for the circumstances we currently face.

Q131 **Alison McGovern:** But none of the targets were met, were they?

Mr Philip Hammond: I have set targets in relation to 2020 to 2021 and an ambition for a balanced budget in the mid-2020s. That is what I am working to.

Q132 **Charlie Elphicke:** Chancellor, I want to ask you about the potential impact on the likelihood of the public finances returning to balance as growth seems to have been higher in recent times than was perhaps previously forecast by the Treasury, notably before the referendum. Do you think that that is going to have an impact on the public finances?

Mr Philip Hammond: Growth outturn to date clearly will have had an impact on the public finances and one of the factors delivering a better fiscal performance in 2017 to 2018 than was forecast will have been the higher growth in 2017 and 2018 than was forecast. The challenge that we face is not just the hopefully short term and soon to be alleviated problem of uncertainty around the Brexit negotiations but also the downgrade of our productivity growth trend, which ultimately is one of the main drivers of the forecast growth of the economy. One of the big challenges for the UK going forward is that we are now looking at a broadly flat 1.5%-ish forward forecast of economic growth and we clearly need to increase that. The only sustainable way to do that is to raise our productivity performance and that is why much of the Government's economic policy and the industrial strategy is focused on raising our productivity performance.



Q133 **Charlie Elphicke:** I noticed that it was reported recently that UK labour productivity is rising at the fastest rate since the financial crisis in the second half of 2017. Did it surprise you that despite Brexit productivity seems to have been increasing?

Mr Philip Hammond: I am the first person to rush to the opportunity to take credit for something, but I think we should remind ourselves that in economic reporting two quarters do not make a summer. Although these productivity figures are good and give us some cause for optimism, some of the drivers of that productivity improvement—in the last quarter it was largely a fall in hours worked that drove the increase in labour productivity. I think we need to be cautious. We will be watching carefully. If we get another two quarters of similar figures I think we will be able to start to draw some positive conclusions but I want to be quite cautious at this stage.

Q134 **Charlie Elphicke:** Would you say that the growth success that we seem to continue to have and indeed the promising, I want to say, green shoots potentially on productivity is attributable to having a clear and very detailed long-term economic plan?

Mr Philip Hammond: I think it is certainly a consequence of the Government's focus on raising productivity, the deliberate decision we made in the autumn statement of 2016 where we moved the fiscal target and used the headroom that was thus created to borrow more money for investment in economic infrastructure. The clear intention was that that would feed through into a better productivity performance of the economy. Clearly, there is a lag. We are optimistic that we are starting to see the benefit of that and other initiatives on skills and education are also starting to show up.

Q135 **Alison McGovern:** To turn to the fuel duty freeze, Chancellor, who in our country benefits from that freeze?

Mr Philip Hammond: People who consume fuel and drive cars.

Q136 **Alison McGovern:** Who are they?

Mr Philip Hammond: Who are they? Well, they are—

Alison McGovern: What are they like? Where are they from? Are they men? Are they women?

Mr Philip Hammond: They will be both. Last time I pulled into a petrol station I can confidently confirm that there were both men and women filling up. It will be people who use transport that will benefit, not only private transport because obviously the cost of fuel duty feeds through into the cost of public transport as well. This has been a very fiscally expensive measure that the Government has taken to try to ease the pressure on families during this period of time by maintaining fuel duties at a lower level than the previous escalator forecast to the extent of around £850 per motorist since 2010.



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Q137 **Alison McGovern:** But, Chancellor, given how expensive you have just said it is, don't you think that the Treasury's analysis could go a little further than, "It benefits people who drive cars"? Don't you think we ought to know some sort of distributional impact? Don't you think we should—

Mr Philip Hammond: Yes, we will certainly have some distributional analysis of this and if it is not already published, I am happy to share it with the Committee.

Q138 **Alison McGovern:** Okay. When asking about the impacts of taxation changes, we are often pointed to the TIINs, the Tax Information and Impact Notes. I have the TIINs note for the stamp duty, land tax relief for first home buyers here and just looking at the inequalities impacts section on it it says, "This measure is likely to benefit younger people due to the fact that first time buyers are likely to be younger and this measure is not expected to have an impact on any other legally protected equality groups". But that is problematic, isn't it, because that says we don't think it will have an impact on protected groups but it doesn't tell us who benefits? It doesn't tell us who loses or who benefits. That is a cursory bit of analysis, isn't it, in the terms of that?

Mr Philip Hammond: I would have thought it was pretty obvious who benefits from the first time buyer stamp duty relief. It will be first time buyers. They are overwhelmingly young and they will be people who are buying houses. I can do that.

Q139 **Alison McGovern:** Sure, but don't you think the Treasury has a little more responsibility to describe the impacts on the population of our country of the changes to fiscal policy that it is making than it will assist first time buyers?

Mr Philip Hammond: We look at the impacts after every fiscal event overall, so the aggregate impacts, and we publish a distributional analysis. We publish it in a form now that is the form that this Committee requested. I changed the format specifically at the request of this Committee and I hope the Committee finds that useful.

What I think would not be particularly helpful is focusing on the impact of a single measure because a budget or a fiscal event is made up of a pack of measures. We obviously look very carefully at the overall distribution of the impact of a package of measures but there will be individual measures within any budget or fiscal event that have skewed impacts across the income distribution, across different groups, across regions even. The important thing is to make a balanced budget package that overall is fair in its impact.

Q140 **Alison McGovern:** To come back to the fuel duty freeze, there hasn't been a tax impact information note on that. Why not?

Mr Philip Hammond: No. There will have been internal advice in the formulation of every single individual policy in the Budget but what we



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do, as we are putting a budget together, is run a constantly updating distributional analysis of the measures and there will be measures that will offer greater balance in one area of the distribution or another. We are trying to put a budget together that overall produces a fair and equitable result. I know that my predecessor was also very focused on ensuring that overall the impact of measures in a budget, taken together, was fair and appropriate.

Q141 Chair: Just for information, the Committee requested apparently a return to the old format, which the Treasury agreed. I think the new format made it less comparable and the Government response to the budget report said that, "2016, 51% of cars were registered to a male keeper, 34% to a female keeper"—it sounds like a zoo keeper—"and the remainder either registered to a company, to a person whose gender is unknown or between keepers", so I think that is the point that—

Mr Philip Hammond: Yes. I think you have to read through. That is an interesting piece of data but I am not sure it is terribly definitive because the cost of making journeys, whether in private or public transport, is impacted by fuel duty. Who is the registered keeper of the vehicle does not tell you who is driving it. It does not tell you who is conveyed in it when it moves and it certainly does not tell you anything about public transport and the cost of public transport. I think if you wanted to analyse this it would be a little bit more of a complex challenge than simply looking at who the registered keepers of vehicles was.

Chair: I think that the Committee has been asking the Treasury to do that analysis. We are going to move on to housing.

Q142 Rushanara Ali: Good afternoon, Chancellor. I have a cough so I hope you have some cough sweets in case you are interrupted.

Mr Philip Hammond: Always.

Rushanara Ali: I did not want to stay away from this session. I have some questions on housing. We have covered some ground in the past on this but I wanted to focus on the response to this Committee's conclusions from your Department that stated that, "The Government will monitor how local authorities respond to the opportunity of an additional £1 billion of borrowing headroom and consider whether any further action is needed". What level of response from the scheme would make you consider expanding the cap by more than £1 billion?

Mr Philip Hammond: Offering to relax the cap in respect of what we would call authorities in high pressure areas.

Rushanara Ali: My local authority.

Mr Philip Hammond: Yes, for example, is one of the ways that we can support the delivery of affordable housing. Obviously what we are constantly looking to do in relation to affordable housing is to get the maximum amount of housing delivered for the available funding and that means optimising the channels and doing it through relaxing local



authority caps is one way. Local authorities will be bidding proposals for cap relaxation and they will be offering to deliver amounts of housing in exchange. That will allow us to assess the value for money of delivering through that particular channel a given amount of fiscal headroom. We will be rigorous about this because we need to use the available housing funding in the way that delivers the area adjusted maximum amount of housing. Clearly, you could get the maximum amount of housing by building everything in a very low cost area. That would not achieve our objectives. But adjusting for demand pressure and affordability pressures, we want to get the very best outcomes that we can.

- Q143 **Rushanara Ali:** How much progress has been made on the 300,000 a year targets? Do you think it is on track? Are you confident that we are going to get 300,000 a year?

Mr Philip Hammond: Yes, I am confident. I have spent a lot of time—

- Q144 **Rushanara Ali:** How many have been built?

Mr Philip Hammond: In 2016 to 2017, 217,000 net new dwellings were delivered, which is a significant increase over the pattern of the previous few years.

- Q145 **Rushanara Ali:** What proportion were for social housing and affordable housing?

Mr Philip Hammond: I cannot answer the question off the top of my head. Inspiration may come to me in just a moment. We have built 350,000 affordable homes since 2010 but I cannot give you a breakdown for 2016 to 2017 and it probably isn't useful to look at a single year anyway. But getting up to 300,000 by the middle of the next decade is a pretty challenging target. We have done a lot of work on disaggregating the different channels where additional increments of housing are going to be delivered with the various different types of funding that we have made available. I have a high degree of confidence that we will get there.

- Q146 **Rushanara Ali:** Yes, but do you think that you could relax the rules around the £1 billion making it easier for local authorities to be a genuine partner in hitting that 300,000 a year target particularly around social housing? It is not just specific to this Government but for a long time we have had challenges in meeting the housing shortage that, despite various efforts and various announcements, continues to be a challenge and you have admitted that to yourself. I think we have gone round this a few times and I think I raised some of these questions previously that local authorities do feel that they could play a bigger role and the £1 billion is not adequate in meeting the goals that they need to meet in addressing the social housing as well as affordable housing that is needed in constituencies like mine but in many other parts of the country.

Mr Philip Hammond: The straight answer to your question is of course we could but I do not want anybody to be left with the impression that increasing local authority borrowing caps is a cost free option for us. It is



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an alternative to channelling money through other routes. It has the same impact on public sector net borrowing. If we raise local authority caps by £1 billion, it is £1 billion we cannot give to housing associations for example and because housing associations borrow it from the private sector, outside the public sector ring-fence, it may well be that housing associations can deliver a greater leverage. Therefore, for a given amount of public money we can deliver more affordable and social housing through the use of housing association routes than we can through local authorities.

Q147 Rushanara Ali: Thank you. I am going to move on to the Help to Buy scheme. There have been reports that some of the properties that were bought through the Treasury scheme are now almost worthless in relation to the ones that have similar cladding to what was used for Grenfell. I understand there was a case reported today where the property was bought for £475,000, the Government provided £95,000 but it is worth £50,000 and the HCA has agreed for that person to pay £10,000 back, which means that the Treasury will have to cover the loss of £85,000.

What assessment has been done on the number of properties that are affected in this way? What it will cost if other properties have to be underwritten—the loans that are paid back because of the value now to do recladding and disputes between the property companies—in this case it was Galliard. What is going to be the cost to the taxpayer of having to underwrite those sorts of properties now?

Mr Philip Hammond: You are talking about the possibility that a Help to Buy loan has been extended to somebody who has bought a property that, for whatever reason, and it could be something else—it could be subsidence, it could be cladding—

Q148 Rushanara Ali: No. I am specifically talking about the news reports of properties that have Grenfell Tower style cladding, which is the subject of dispute. It is in *The Guardian* report today of one individual. It has been reported a few times but there are a number of properties, a few thousand, in the case of that block and there are Help to Buy properties that are affected.

Mr Philip Hammond: I am not aware of the issue. It is perfectly possible that a Help to Buy loan could have been extended to a property that has subsequently had a valuation difficulty but I would imagine it would be a very small percentage of Help to Buy loans. I think the overwhelming majority of Help to Buy loans have been made in respect of houses rather than flats and of course the loans are advanced on the basis that there is a provision for under-recovery. There is a margin built in to the structure to allow for the possibility that somebody will not repay.

Q149 Rushanara Ali: Could we have some facts behind this on how many are affected in this way and what it would cost from your Department? Perhaps somebody could write to us.



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Mr Philip Hammond: I am very happy to ask the HCA to share with the Committee whatever information they have but I suspect—

Q150 **Rushanara Ali:** You do not have to answer to it right now.

Mr Philip Hammond: We wouldn't necessarily have a comprehensive picture because HCA, I guess, would only become aware of a problem at the point where somebody was required to repay and couldn't. Bear in mind that these loans are not repayable in—

Q151 **Rushanara Ali:** Thank you. I have one more question on housing, which is related to Grenfell and the disaster. Seven out of 160 social housing blocks that are covered in dangerous cladding have been replaced and Ministers do not know how many private blocks are affected and, of course, in built-up areas, like in my borough, in my constituency, it is hundreds of blocks. Chancellor, you have said in the past that the Ministry of Housing, Communities and Local Government is responsible for making those payments to local authorities. For the last years there have been wranglings between local authorities saying they don't have the resources. Housing associations saying if they used the reserves and resources then it means less house building. There is a consequence. The response has constantly been, "CLG will deal with the applications but it is very difficult to access funds".

Given how few have had the work done, seven out of 160 is a worrying figure. In some estimates it will take years, up to 10 to 15 years, to correct this stuff. In my constituency 24/7 fire patrols have to be provided. Up and down the country it is the same. Don't you think that the Government should be making sure the work happens quickly, both in the social housing blocks and the private blocks, and that you underwrite that and give the public an assurance that the work will be done and the bills can be paid and worked out subsequently rather than leaving leaseholders in private blocks, and there are many cases like that, having to battle it out and legal battles with private owners of blocks of flats in order to work out who pays for what, which is what is happening up and down the country? Don't you think you should be doing that?

Mr Philip Hammond: I think, first of all we have a review of the building regulations going on, which is an important part of this equation. We have the inquiry into what happened at Grenfell going on and we will expect to receive information from both sources and both of those will help to inform how we approach this challenge. We have been clear that among local authorities and housing associations social landlords have a responsibility to ensure the safety of their buildings. That is part of their statutory duty and that we will ensure that lack of finance does not prevent urgently required safety work from being carried out.

Q152 **Rushanara Ali:** That is exactly what is happening.

Mr Philip Hammond: I think it is important just to note that lack of finance will not always be the constraint. There is a limited capacity for



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this recladding work and in some cases it will be capacity constraints in the industry that will limit the speed that work can be carried out.

Q153 **Rushanara Ali:** It will be both. Let's accept that it is both.

Mr Philip Hammond: But let's go back to the financing. In the case of housing associations where they have reserves and funding capacity—

Rushanara Ali: I know this, Chancellor. We know this.

Mr Philip Hammond: —they will be expected to use it. In the case of local authorities where they have access to reserves they will be expected to use it. It is a first duty of a landlord.

Q154 **Rushanara Ali:** Chancellor, the fact is that this is really worrying; seven out of 160 social housing blocks, not to mention the private blocks. The Government is shirking responsibility. The question is, Chancellor, are you going to be able to live with yourself if this happens again, when these properties haven't had the work done and the Government departments are not prepared to take the responsibility?

Mr Philip Hammond: If you have a specific example of a local authority or a registered social landlord who has approached the Ministry of Housing, Communities and Local Government because of an urgent fire safety investment need that means the fire safety investment need—

Q155 **Rushanara Ali:** The 153 that have dangerous cladding that hasn't been replaced is not serious enough and urgent enough?

Mr Philip Hammond: An urgent fire safety need will be a case where the relevant fire safety officer has declared that it needs to be done as a matter of urgency. Where that landlord cannot proceed because of financial constraints, the landlord should approach MHCLG and MHCLG will work out a solution to ensure that they can access funding. That may be relaxing caps in the case of a local authority or making additional borrowing capacity available.

Q156 **Rushanara Ali:** That is not what is happening. It is incredibly complacent, Chancellor, and I think you should discuss this with MHCLG to avoid another major fatality, because we shouldn't have to wait years before this work is done.

Mr Philip Hammond: I am very happy to look at any examples that you present to us. I know that the Secretary of State for Housing, Communities and Local Government is all over this issue. It is a very challenging issue and obviously these blocks need to be reclad. In some cases the work is urgent and it needs to be done urgently but we have to be led by the expert professional advice.

Q157 **Rushanara Ali:** The Government needs to be on the side of people who have to live in these properties. At the moment they don't feel they are on their side.

Mr Philip Hammond: I think that is unfair.



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Q158 Rushanara Ali: Not only on social housing but on private blocks where they have to get lawyers; they can't afford lawyers, where they are having to fight legal battles. It would be helpful if the Treasury could be on their side by making sure that they are providing guarantees of finance and that the Ministry of Housing, Communities and Local Government is on their side. That is what the public need. That is what the public don't have at the moment, Chancellor.

Mr Philip Hammond: I think the situation in relation to private blocks is more complicated—

Rushanara Ali: It is a massive problem.

Mr Philip Hammond: I accept that it is a challenge but there is only a certain amount of finance available and diverting public housing funding to leaseholders in private blocks would be a very significant decision.

Q159 Rushanara Ali: Why don't you go after the people who are responsible, as a government? Why don't you go after the private companies that are responsible for those blocks instead of leaving residents and leaseholders to have to fight those battles in order to live safely without fear of dying in fires like in Grenfell Tower?

Chair: Unfortunately we are going to have to move on, we have an awful lot and this is an incredibly important issue. I think what we will do is to accept your invitation, Chancellor. If there are specific examples, the Committee will be pleased to raise them with you as the Chancellor of the Exchequer and ask you to liaise with Sajid Javid and to reply to the Committee with specific answers about the specific problems. Is that helpful?

Mr Philip Hammond: Yes.

Q160 Stewart Hosie: I have a couple of small technical questions. In the Government's response to the Committee's recommendation to move indexation from RPI to CPI, things like the business rates multiplier, student loans and so on, the Government said that they had previously committed to reviewing the use of RPI for indirect taxes once their fiscal consolidation plans had been implemented. This remains Government policy. Can I ask how long has that policy been in place? When will we know the fiscal consolidation has been completed and when will the review start?

Mr Philip Hammond: The challenge that we have is moving from RPI to CPI in terms of indexation. It will have a physical cost and just because we are changing index doesn't close the gap. That means real money that has to be found from somewhere. What we are doing by moving from RPI to CPI is simply shifting the burden of taxation around between different groups of taxpayers.

It is sensible to look at moving to what is becoming a more widely used index. Although of course CPIH, we expect, will ultimately become the chosen index, the preferred index, but it is sensible to move in this



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direction but we cannot somehow write out of the picture the fiscal consequences. They have to be paid for. The Government's view is that at this stage in the fiscal consolidation it is not the moment on a wholesale basis to switch from RPI to CPI.

Q161 **Stewart Hosie:** In short, you are using RPI to raise revenue and to delay spending.

Mr Philip Hammond: It has different consequences in different parts of the system. Of course, in other areas uprating at RPI has a cost. In tax indexation uprating allowances in relation to RPI would have a cost obviously. It has different impacts in different parts of the system.

Q162 **Stewart Hosie:** Let me go back to another Government response to the student loans report and it is the same issue, where it was said, "The flaws in the RPI measure of inflation are well understood". If the flaws are well understood, why is it still being used for policies that affect household incomes?

Mr Philip Hammond: The direction of travel is to move away from RPI but there will be fiscal consequences in doing that and the speed we make that transition needs to take into account those fiscal consequences. In the case of student loans, which you have mentioned, it is an intentional design of the policy to ensure redistribution in the repayment of student loans. Students, graduates, who are higher earning will pay higher rates of interest. As they pay their accrued interest they are cross-subsidising those in lower-paid employment who will end up having parts of their loans written off. A system that delivers a higher interest rate but then writes off loans effectively redistributes from high earners to lower earners and that was always the intention of the student loan system.

Q163 **Stewart Hosie:** The threshold for repayment is well understood and that has precisely nothing to do with the student loan multiplier. However, let's just go back to what you said about CPIH—

Mr Philip Hammond: There are differential interest rates depending on income.

Q164 **Stewart Hosie:** Yes, but again that has nothing to do with the inflationary component of it. However, let's move back to what you said about CPIH. When the Government does switch from RPI, eventually, do you envisage there will be a move straight to CPIH or will it go to CPI first and then CPIH in the long run?

Mr Philip Hammond: No decision has been taken on that at this stage.

Q165 **Stewart Hosie:** Do you know when a decision may be reached? I looked at the formula this afternoon in terms of the real housing cost component and CPIH is a sensible thing to do. When will a decision be reached?



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Mr Philip Hammond: I can't answer that question at the moment. We haven't made a decision and we haven't set out a timetable for making that decision.

Q166 **Stewart Hosie:** When is it likely to be put on an agenda to make a decision?

Mr Philip Hammond: I can't answer that to you today. We have said that as we move towards completion of the fiscal consolidation would be the appropriate time to move away from RPI. You are asking me a secondary question: when will we make the decision whether we move via CPI or direct to CPIH? I think the Government has signalled that ultimately we would expect to move to CPIH but it has to establish itself as a robust statistical measure and I cannot, at this stage, answer the question whether we will need to go via CPI or direct to CPIH.

Stewart Hosie: We will not hold our breath. Hopefully, we will at least find a timetable in the last summer, autumn or early winter statement.

Q167 **Mr Simon Clarke:** Chancellor, I want to turn to Lycamobile and the allegations that BuzzFeed had raised around the decisions that were taken not to launch a UK investigation in response to the request from the French authorities. Just to quote the letter, which was from an unnamed HMRC official, "It is of note that they are the biggest corporate donor to the Conservative Party, led by Prime Minister Theresa May, and donated €1.25 million to the Prince Charles Trust in 2012". Was the Treasury ever involved in the decision or the question?

Mr Philip Hammond: No. The HMRC is operationally independent of the Treasury and very explicitly does not discuss matters relating to dealings with individual taxpayers, including requests from foreign authorities, with the Treasury. That is one of the rules that operate.

Q168 **Mr Simon Clarke:** How can we explain the tone adopted by the HMRC official in this case and the astonishing lack of regard that he or she showed for the rule of law?

Mr Philip Hammond: I don't think it is an astonishing lack of regard for rule of law. The decision not to provide the information that the French authorities requested was made on the basis of HMRC legal advice by HMRC lawyers because the French authorities had failed to provide sufficiently precise information to satisfy a UK judge that the relevant statutory criteria for issuing a search warrant had been met. That is the test that HMRC lawyers will apply. The decision was correctly made and had nothing to do with any wider issues about Lycamobile and what they did or did not do. The error was made by the official in communicating that information to convey completely extraneous information, which should never have been included, sends a very inappropriate message and was just completely wrong. It was an error.

Q169 **Mr Simon Clarke:** That was my point, actually. I was not suggesting that the decision had been influenced in this way. I was just saying that



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even thinking that this was pertinent material to this question seems to me to demonstrate a very, very flawed understanding of the nature of the legalities and the ethics of all of this. Does that lead to a question of the training of the people who are responsible for this kind of work? It is pretty bad.

Mr Philip Hammond: It represents a huge error of judgment and although I have not personally discussed it with HMRC senior management, I have no doubt that HMRC recognises it as a huge error of judgment and it will be a matter for HMRC how they address that with staff training. I am quite sure that they will be doing so.

Q170 **Mr Simon Clarke:** It is difficult for you to comment on the practices that Lycamobile has undertaken over the years, given that this is a subject pending legal action in France, but to follow the BuzzFeed report, you have couriers employed by Lycamobile driving to a company's east London depot every morning in an unmarked black people carrier and going to multiple post offices handing over sums of up to 240,000 over the counter. This is despite the fact that Lycamobile has an armoured and properly audited cash-in-transit service at their disposal. Do you think this begs the question as to whether our money laundering regulations are sufficiently robust?

Mr Philip Hammond: It would not be appropriate for me to comment on an individual taxpayer case especially when, as I understand it, there is a legal action pending, albeit in another jurisdiction.

Q171 **Mr Simon Clarke:** If that judgment were to find that there had been abuses committed in France, would that lead to lessons being looked at in the UK?

Mr Philip Hammond: Again, I can't refer to a specific case. That would be inappropriate, but in general the outcome of legal actions taken by HMRC or law enforcement authorities in the UK or elsewhere will always inform our approach to the enforcement of money laundering or tax avoidance regulations. Our policy officials will look carefully at judgments of any relevant courts.

Q172 **Wes Streeting:** Why are donations to the Conservative Party relevant to HMRC when considering whether to investigate companies?

Mr Philip Hammond: As I have just said, they are not.

Q173 **Wes Streeting:** They are evidently because—

Mr Philip Hammond: No, they are evidently not.

Q174 **Wes Streeting:** I am sorry, Chancellor, HMRC did deem them relevant in the case of Lycamobile when as Simon has already quoted, in its note to French officials it said, "It is of note that they are biggest corporate donor to the Conservative Party, led by Prime Minister Theresa May, and donated €1.25 million to the Prince Charles Trust in 2012". In the context of everything else in that note, someone at HMRC has deemed it



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relevant. Why on earth? What kind of culture is operating at HMRC where an HMRC official would deem that information relevant?

Mr Philip Hammond: The important thing, and to reassure the Committee, is that the decision was made correctly by HMRC lawyers on the basis of the proper assessment of whether the standard of evidence submitted by the French authorities was sufficient for a UK court to issue a search warrant and the decision was that it was not. How that information was then conveyed to the French authorities represents a gross error of judgment by an individual.

Q175 **Wes Streeting:** We will come back to the legal dimensions shortly. Have you ever had dinner with Allirajah Subaskaran? He is the owner of Lycamobile and he is part of your party's exclusive leaders group that dines privately with the Prime Minister and the Cabinet, according to—

Mr Philip Hammond: I am not aware of having done so but I will check my transparency disclosures, which would answer that question.

Q176 **Wes Streeting:** Thank you. It would be really interesting. If he is giving money to the Conservative Party and still not ending up having dinner with you he is obviously being short changed. What I would like to know is when did you know that HMRC was hindering the investigation into Lycamobile by the French authorities?

Mr Philip Hammond: HMRC is not and has not hindered an investigation. HMRC has to follow a very clear set of rules and in the case of—

Q177 **Wes Streeting:** When were you made aware that HMRC had reached a judgment that they would not co-operate with the French investigation?

Mr Philip Hammond: I think I first had this information last week.

Q178 **Wes Streeting:** Was that when HMT knew or did it take a while to move its way up the food chain?

Mr Philip Hammond: I can anticipate that it would have taken a day or two to filter through HMT, but I can check that, again, and let the Committee know. My recollection is that I was alerted to this early last week.

Q179 **Wes Streeting:** Moving to the correspondence between British and French officials dated 30 March 2017, that same note stated that, "Lycamobile is a large multinational company with vast assets as their disposal and would be extremely unlikely to agree to having their premises searched". This is at the heart of the problem, isn't it? On your watch with the framework that we currently have, HMRC quivers in front of multinational companies with vast assets when they should be pounding down the door to look at allegations of corruption and money laundering. That is what is happening.

Mr Philip Hammond: Fortunately, we live in a country that is governed by the rule of law and HMRC does not operate on the basis of pounding



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down the door because it does not like the look of somebody. It operates on the basis of evidence and the rigorous interpretation of legal rules. That is why we have lawyers in HMRC. Any information that is provided to HMRC will be acted upon but only if there is a legal basis to do so. I think HMRC in substance has acted correctly in this case, but clearly the communication that was issued by an individual demonstrated a complete lack of judgment by including completely extraneous material relating to Lycamobile's donations to a political party and to a charitable foundation, neither of which are relevant.

Q180 Wes Streeting: It is interesting you describe the kind of country we are because when asked by BuzzFeed whether or not this correspondence had existed, the HMRC press officer said, "No HMRC official would ever write such a letter. This is the United Kingdom, for god's sake, not some third world banana republic where the organs of state are in hock to some sort of kleptocracy". Putting aside some of the distasteful and colourful language, let's look at the substance here. Lyca was exposed in BuzzFeed as having funnelled money out of Sri Lanka by relatives of the deposed despot Mahinda Rajapaksa, whose government stands accused of very serious crimes and allegations of genocide in the Sri Lankan civil war. Its two French companies have been formally charged with money laundering and have been subject to a €20 million bail. I find totally unreassuring what you have just said about we are following the rules and the framework. Clearly they are not good enough and as much as I hate to talk down our own country when it comes comparisons with the French, it is very clear that the French have a legal framework that is able to call to account this kind of grubby practice but here you are hiding behind the rules for which you are responsible as the Chancellor, saying, "It is not my fault, it is the law of the land".

Mr Philip Hammond: The case in France will relate to the businesses operating in France and practices in France. I am sure that HMRC will be looking carefully at any decisions of French courts.

Q181 Wes Streeting: I am sorry to break this to you, Chancellor, but according to BuzzFeed Lycamobile services received payments totalling €75 million over a nine-month period in 2015 from 19 companies that the analyst noted in the report bore all the hallmarks of being shell companies. The invoices of these companies have been submitted to the banks from the telecoms company and analysts said they were manifestly fake. The funds that were apparently transferred into Lyca's offset network came via a bank account in London. When this city is still regarded as one of the money laundering capitals of the world, the idea that this has nothing to do with us is, frankly, laughable. You have come in front of the Committee this afternoon—and we know, because you were photographed walking into No. 10 with a note about Lyca earlier, unfortunately, and you must have known this would have come up this afternoon—telling us, "Don't worry, it is nothing to do with us". It evidently is to do with us and what you have told the Committee this afternoon is that we are ill equipped to deal with this kind of grubby



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practice in a way that French authorities are not. What are you going to do about it?

Mr Philip Hammond: I haven't told you that at all. We have different authorities, law enforcement agencies, tax enforcement agencies, that have powers and capabilities to deal with these kind of issues. What we do not do in the UK is have ministerial direction over the affairs of individual taxpayers.

Q182 **Wes Streeting:** No, I am talking about the legal framework for which you are responsible. That is what I am talking about. I am not expecting you, the Chancellor, to order officials into Lycamobile this afternoon. I am talking about the legal framework that, according to HMRC lawyers, clearly prevents HMRC going in to investigate this company and others.

Mr Philip Hammond: It is not about not expecting me to do it. It is about it would be completely wrong if I were able to do it. These issues, whether it is a tax-driven issue or a law enforcement issue, have to be managed by the proper authorities, independent decisions being made on the basis of proper legal advice by the prosecution authorities or whichever agency is specifically responsible. It is not something over which direct political control should be exercised. I do not agree with your assessment that we do not have adequate legal structures in the UK for dealing with money laundering or other irregular financial activities. We have a very large financial services sector in the UK, so you have to bear that in mind as the context for looking for individual examples of malpractice or misfeasance, but we will go after anyone who is abusing our laws or breaking our laws. We will pursue them and sometimes that will be HMRC, sometimes it will be the National Crime Agency. There are different agencies involved here, but I can assure you that the relevant agencies will be looking closely at the outcome of investigations in other countries. They will not be reporting the details of that work to Ministers, because that is not the way we operate in this country, but they will be doing their work diligently and using the frameworks of law that we have in place.

Q183 **Wes Streeting:** Have you asked HMRC to investigate in the case of this memo?

Mr Philip Hammond: In the case of the memo, HMRC is investigating the issue of the inappropriate choice of words in the memo.

Q184 **Wes Streeting:** Are you satisfied that the culture of HMRC is appropriate and effective and diligent enough for tackling money laundering?

Mr Philip Hammond: At the moment it appears that this is an isolated misjudgement by an individual but of course we will have to form a judgment in due course as to whether there is a more institutional problem of understanding about what is appropriate and what is not appropriate to include in a communication. But I have to repeat that the decision was made on the basis of a correct analysis of the facts by HMRC



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lawyers. What we are talking about here is an incorrect, inappropriate communication of that decision to authorities outside.

- Q185 **Wes Streeting:** What I am putting to you is that this is not about simply the judgment of individuals at HMRC. It is about whether you as Chancellor have put in place an adequate legal framework that empowers HMRC to clamp down on the money laundering and corrupt, grubby practice that still exists in this country that sees, according to Transparency International, £4.4 billion worth of money from suspicious wealth still flowing through this city. What you have said this afternoon is just so tiring, frankly, in terms of a pattern of behaviour from Ministers. When it comes to the Home Secretary, it is not her fault that Windrush has gone completely belly-up; it is the officials' fault. Now in this case it is not your fault that the legal framework is not correct; it is about how the lawyers have interpreted the law. When are any of you going to take responsibility for making sure the right framework is in place to tackle this kind of behaviour?

Mr Philip Hammond: The right framework is in place.

- Q186 **Wes Streeting:** If these were my constituents breaking HMRC's tax laws you can bet that HMRC would be breathing down the necks of small businesses in my constituency. When it comes to a big multinational company like Lyncamobile it is not just about lawyers saying, "We can't do this because of the law", it is HMRC officials putting in black and white that to HMRC size, wealth and refusal to co-operate with allowing people in to investigate are considered reasons and factors to consider in the case of whether or not to co-operate with the French authorities. That is the problem; it is the gross double standards and you are not accepting any responsibility for it.

Mr Philip Hammond: The question that was dealt with in HMRC was a very simple and specific one: a request for information.

Wes Streeting: It didn't even do that.

Mr Philip Hammond: The decision was made on legal advice that that request could not be met.

- Q187 **Wes Streeting:** Then get the law into the right place. That is your responsibility.

Mr Philip Hammond: I am afraid I think you are jumping too quickly to a decision that that information should have been supplied. It is very—

- Q188 **Wes Streeting:** Yes, because money laundering is a new problem, is it? We are jumping too quickly on money laundering; is that what you are saying? Economic crime, money laundering—we are jumping too quickly on that?

Mr Philip Hammond: No, I am not and I resent the tone of this questioning. We have robust money laundering laws in this country. They are not primarily the responsibility of HMRC.



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Wes Streeting: And they are not working either.

Mr Philip Hammond: HMRC's involvement in this particular case was dealing—

Wes Streeting: It was pathetic, wasn't it?

Mr Philip Hammond: You are not really doing justice to the gravity of the Committee's interest in this, come on. HMRC's involvement in this case was simply on the question of whether or not it could supply confidential documents to the French authorities. That decision has to be made on the basis of legal advice. It is the responsibility of other agencies within our system whether to pursue a money laundering issue if one were to arise. That is not primarily an HMRC responsibility.

Wes Streeting: It gets worse, doesn't it?

Chair: We are going to move on.

Q189 **John Mann:** Good afternoon, Chancellor.

Mr Philip Hammond: Good afternoon.

John Mann: Good afternoon, Sir Tom. No one wants to talk to you, Sir Tom, but I do want to bring you into proceedings. Jon Thompson and other senior HMRC officials told the Treasury Sub-Committee in recent meetings that there is no individual discretion, that when it comes to multinational companies it is teams rather than individuals and that individual discretion does not exist. Were they misleading us?

Sir Tom Scholar: I am sure they weren't.

Q190 **John Mann:** They are right in saying that when it comes to dealing with any multinational it is a team effort rather than an individual?

Sir Tom Scholar: With respect, that is a question for HMRC not for the Treasury. We do not have any involvement at all, as the Chancellor said, in anything to do with the affairs of individual taxpayers. We don't have any information either as to the legality.

Q191 **John Mann:** You have full confidence in what Mr Thompson and his senior officials have told us in several hearings, that it is not done by individuals. It is an area I have quizzed on, both formally and informally, a lot to clarify. When it comes to Lycamobile, it can only be the case that it was not an individual, it was HMRC as a unit that presented a case to the French.

Sir Tom Scholar: First of all, this was, as the Chancellor said, a response to a request from a French authority. It is not the implementation of UK tax, so it is a slightly different case.

Q192 **John Mann:** How we handle it is not different. Mr Thompson and others have been very clear that it is not an individual. There are teams of people who work together and, therefore, it is the team in HMRC. It is not an individual, it is a team who make the decisions and determine, on



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behalf of HMRC, not on behalf of an individual, the response to the French authorities.

Sir Tom Scholar: I am sorry but I can't answer questions as to how HMRC discharges its responsibilities because I don't have the information. That is its responsibility.

Q193 **John Mann:** No, but you would expect it to be consistent with what Mr Thompson and senior officials have told this Committee on how they operate.

Sir Tom Scholar: I am sure that Mr Thompson and his officials will always have been candid and accurate in the answers that they give to this Committee.

Q194 **John Mann:** Sir Tom needs to have a chance, Chancellor. Give him a chance. Would you expect, Sir Tom, HMRC to have taken legal advice in advance of sending this advice and information to one of our close allies in France?

Sir Tom Scholar: As the Chancellor said, the decision was taken on the basis of legal advice.

Q195 **John Mann:** The team would have taken legal advice and then submitted what they did to the French, as a team.

Mr Philip Hammond: I am sorry, I want to come in here because I think—

John Mann: I am asking Sir Tom. He is the civil servant. I appreciate you are a bit nervous about the issue. But, Sir Tom, at what stage—

Mr Philip Hammond: I am not nervous about the issue at all. I am just trying to help you because you are clearly misguided in your questioning.

Q196 **John Mann:** I am asking Sir Tom, if I may. You had a good go with two members of the Committee previously, Chancellor. Sir Tom, having seen that, in what way would HMRC know about political donations to a party, because they obviously did?

Sir Tom Scholar: I understand that HMRC is currently carrying out an internal inquiry to determine the exact sequence of events here.

Q197 **John Mann:** You are the Permanent Secretary in an organisation. How would they know that this organisation was donating to the Conservative Party? What is the process within which they would find that?

Sir Tom Scholar: First of all, as I have said, HMRC is doing an internal inquiry. Secondly, this is an HMRC matter; it is not a Treasury matter. I can't answer questions on how HMRC discharges its responsibilities and does its work.

Q198 **John Mann:** You can't give us any indication about whether this would be an investigation into money from the—



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Mr Philip Hammond: This is ridiculous.

John Mann: I will ask you, Chancellor.

Mr Philip Hammond: This is an individual who has written a letter and has included in the letter extraneous and irrelevant material. It is material that any one of us could have found out. Donations to the Conservative Party are recorded publicly, so you could have found that out, I could have found that out, an individual in HMRC could have known it simply by Googling. As to the question of teams—

Q199 **John Mann:** You are suggesting to the Committee that an individual—HMRC works on multinationals as a team, not as individuals.

Mr Philip Hammond: No, I want to correct that perception. Mr Thompson has told you in the past that HMRC deals with multinational taxpayers by organising in teams. That is how they deal with multinational taxpayer clients of HMRC. In this case we are dealing with a request from a foreign authority for information that HMRC holds. That is not the same as dealing with the tax affairs of a multinational company. It is a piece of process within HMRC for dealing with a request for information, just in the same way as HMRC will have a channel for dealing with requests under Freedom of Information legislation. It will not necessarily—

Q200 **John Mann:** What you are saying is that the other staff members responsible for dealing with Lycamobile were not consulted at all in this.

Mr Philip Hammond: I can't give you a definitive answer on that because, as Sir Tom said, there is an internal inquiry.

Q201 **John Mann:** Would you find it strange if they were not consulted in relation to this?

Mr Philip Hammond: Not necessarily. If a request is made for a document that a public body holds, there will be a proper process to be gone through in deciding whether that request can be met. The important thing is that that process will be followed and in this case it was.

Q202 **John Mann:** Why would it be relevant for an HMRC official to be Googling or finding out from newspapers—

Mr Philip Hammond: Clearly not relevant but HMRC officials are also human beings who have bits of general knowledge.

Q203 **John Mann:** This is going to the tax authority of a key ally of ours. This is not someone writing to his mate. This is on behalf of our country, our tax authority, to another sovereign state's tax authority.

Mr Philip Hammond: And I have said the letter is clearly inappropriate.

Q204 **John Mann:** You are implying that individuals have discretion to Google online and add things in of their choice at that discretion when our tax authority sends information to the tax authority of a major economy such



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as France. You are saying that.

Mr Philip Hammond: Or didn't send it. Not sending information in this case.

John Mann: I don't believe that is the case.

Mr Philip Hammond: What has happened is an individual has responded to the request substantively correctly, informing the other party that we cannot supply the information, but has included extraneous material that should not have been included.

Q205 **John Mann:** Sir Tom, with the EN+ Group flotation, was the Treasury's Office of Sanctions Implementation consulted?

Sir Tom Scholar: I think the Chancellor already replied to that earlier.

John Mann: I am just asking you.

Sir Tom Scholar: I don't know the answer to the question but I am happy to look into it and let the Committee know.

Q206 **John Mann:** You don't know whether they were. Would it be within the remit of Treasury, under the rules we have for sanctions, to block or suggest blocking a flotation on the stock exchange?

Sir Tom Scholar: Again, that is a very precise question relating to the law as it applies to sanctions. I don't want to guess the answer.

John Mann: That is what I am asking you.

Sir Tom Scholar: I would like to check the answer and I can write to the Committee.

Q207 **John Mann:** Russia is rather in the headlines at the moment, Chancellor, and I agree how serious a threat Russia is, I totally agree with the generality of that. But when you go into the detail, you are saying you don't know whether Treasury, under our rules on sanctions currently applying to Russia, could attempt to block a flotation of a company on the stock exchange. You don't know whether that is part of our sanctions regime in terms of the possible options. Do you know, Chancellor?

Mr Philip Hammond: This is not a question about sanctions applying to Russia. This is a question about the potential sanction status of any individual entity and what are the sanction restrictions imposed on that entity.

Q208 **John Mann:** I am asking whether Treasury has the ability under the sanctions regime that we are operating as the United Kingdom to suggest or to demand and require that a float on the stock exchange be blocked?

Mr Philip Hammond: My understanding of the sanctions regime is that it operates by imposing specific restrictions. It is not a regime about inviting Government Departments or agencies to make observations or suggestions. It imposes specific legal restrictions on certain entities.



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Chair: John, one more question and then we will move on.

John Mann: The reason I ask is because the FCA said they had consulted using the usual protocols. I am trying to find out what they were.

Chair: We asked that question earlier on.

Q209 **John Mann:** One final question for you, Chancellor. If hospital trusts make more than 50,000 a year through non-core business they are eligible for corporation tax. For example, if they allow space out for Starbucks cafés or other brands of cafés and make more than £50,000 they are eligible for corporation tax. How many have been charged corporation tax?

Mr Philip Hammond: Again, I can't answer that question. HMRC would be able to provide an answer to that question.

Q210 **John Mann:** If I were to suggest that none has been, would you think that that would be a suitable area for your attention?

Mr Philip Hammond: If you are suggesting that NHS trusts on any scale are not meeting their obligations in respect of corporation tax, I am certainly prepared to pass that on to HMRC and ask them to consider it.

John Mann: Very good. Thank you.

Q211 **Chair:** Just to finish off on the Lycamobile question, I think, Chancellor, you said earlier on that you had not had any conversations with HMRC about that particular issue.

Mr Philip Hammond: I haven't personally, no.

Q212 **Chair:** Sir Tom, have you had any conversations with HMRC about the Lycamobile story?

Sir Tom Scholar: No, not personally.

Q213 **Chair:** Have either of you asked any of your staff to have a conversation with HMRC about that story?

Mr Philip Hammond: I don't think so. I have asked for information about what was going on but I have not asked for any particular conversation to take place.

Chair: You just asked for a general briefing?

Mr Philip Hammond: My understanding was that an investigation is going on in HMRC.

Q214 **Chair:** Sir Tom, have you asked any members of staff to speak to HMRC about the story?

Sir Tom Scholar: No.

Q215 **Stephen Hammond:** Good afternoon. I am going to ask about three particular issues. The first one is the attractiveness of London as a place to be listed. If an investor buys an irredeemable, don't they have the



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right to consider that that should not be prone to cancellation?

Mr Philip Hammond: We are in Aviva, are we? We are in Aviva territory.

Stephen Hammond: We are in Aviva. Let me ask you the second question, which goes directly to that point as well. Don't you think that Aviva's actions in March have harmed London as a listing authority? They undermined the confidence of investors.

Mr Philip Hammond: There is an issue here that clearly has to be dealt with and we would very much be concerned about anything that undermines the confidence of investors. This is an issue that we want to see resolved as quickly and as effectively as possible.

Q216 **Stephen Hammond:** One way of resolving that issue would be to either amend or bring in a new Companies Act that would deal with that. Is that in Treasury's consideration at the moment?

Mr Philip Hammond: There are no current plans to amend the Companies Act. The reality of legislation is that one tends to gather a number of issues that need dealing with. Companies Acts get amended from time to time and it tends to be a question of gathering issues that need to be addressed and then dealing with them in a Bill.

Q217 **Stephen Hammond:** I take your point that it is an aggregate number of issues but this particular issue has been pretty controversial. Do you think it is beholden on Treasury to find a way outside of a Companies Act to make sure that investors feel reassured about the confidence they can have?

Mr Philip Hammond: It is certainly a matter of concern for the relevant authorities to ensure that investor confidence is maintained.

Q218 **Stephen Hammond:** Is the FCA looking into this? Has the Treasury had any conversations about looking into this and, if so, what was the upshot of those conversations?

Mr Philip Hammond: My understanding is that the FCA is looking at this issue but I don't think I can say anything further at this stage. This is an issue that touches on a specific company. The FCA is the relevant authority and fiercely jealous of its independence.

Q219 **Stephen Hammond:** This Committee is fiercely jealous of when we have Mr Bailey in front of us, which I think we do next week or the week after.

Mr Philip Hammond: You will have plenty of opportunity to ask him then.

Stephen Hammond: About that and many other failings. Can I bring back the B word? Is it correct that the UK's overseas persons' exemption allows non-UK-based financial institutions cross-border access to UK institutional investors and counterparties and that access is not conditional on the jurisdiction or indeed that that jurisdiction maintains a



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degree of regulatory alignment?

Mr Philip Hammond: I don't know. Do you?

Sir Tom Scholar: I think it is but I would have to check.

Q220 **Stephen Hammond:** If you could, because it then leads on to another question. If that is so, after Brexit you could see EU firms enjoying cross-border market access under that exemption.

Sir Tom Scholar: The whole question of, in both directions, the market access that EU firms will enjoy here or ours will enjoy there is all to be discussed.

Q221 **Stephen Hammond:** Of course, but if that exemption was used the key point would be that there would be differential access because there would be access into our market, not having to maintain any regulatory alignment with anywhere we choose to align, and yet we may not get the reciprocal. It is important to know whether the overseas persons' exemption exists or not.

Mr Philip Hammond: An announcement was made, as I think the Committee will know, on 20 December last year by the Bank of England, the Financial Conduct Authority and the Treasury reassuring foreign domiciled entities operating in London that they would be able to continue operating in London, giving them that reassurance in order to reinforce their presence in London and underpin London's financial markets. We judged that that was the right thing to do unilaterally to reinforce London's position as a financial services centre.

Q222 **Stephen Hammond:** You will probably remember, Chancellor, that we had the Governor in front of us on the day that he announced that. The question that follows on from that is I think there would be no one who would dispute that unilaterally making that offer was a sensible thing to do. What response have you had from other EU authorities to that offer?

Mr Philip Hammond: What we have not seen yet is the immediate leap to a reciprocal offer by the European Union authorities but we are, of course, discussing with the EU the question of financial services access. I made a speech in March in Canary Wharf that set out the Government's views as to how that could be achieved and delivered and attempted to rebut the often quoted EU mantra that it is impossible to include financial services in a free trade agreement.

Q223 **Stephen Hammond:** The negotiating position talked about financial services under host state rules and on a basis of potentially mutual recognition. Isn't the concern with mutual recognition that that would allow them at any stage in the future, if we do not get a signed deal, to withdraw market access because they would judge that we are not aligned or they do not choose to recognise any movement or deviation we choose and that leaves the UK financial services in a weak position?



Mr Philip Hammond: Yes, and I have made clear that for a structure and arrangement to be load bearing for the kind of volume of business that the UK and the EU-27 do together in financial services, it would have to have certain characteristics. It would have to have an objectivity around it, which the current regimes on offer don't have. It would have to have proper mechanisms for resolving any question as to whether equivalence or mutual recognition status had been lost. There would have to be proper notice periods so that businesses would be able to understand that even if they did lose their access they would do so in a way that allowed them properly to plan an alternative business strategy. Clearly something that is arbitrarily given and taken away on zero notice is not the basis on which to organise any largescale business.

Q224 **Stephen Hammond:** We can assume that that will not form part of the arrangement. A dispute resolution system will be required, as you have just said. That means that there has to be some substantial work done on materiality and deviation principles. Is that work being undertaken?

Mr Philip Hammond: As yet, we are not in substantive discussions with the European Union about future financial services relationships. We have only just got past the agreement on the implementation period. We have not yet begun the substantive discussions on the future partnership but we are in the preliminary foothills of exploring what might be possible in financial services.

Q225 **Stephen Hammond:** If we are in the foothills, will we have reached the summit of the mountain by October?

Mr Philip Hammond: We remain ambitious to make progress.

Q226 **Chair:** Have you facilitated any discussions between the UK's regulators, particularly the FCA and the Bank of England, with the EU's regulators? We have had evidence that the EU's regulators are proving either reluctant or not being enabled to discuss purely technical day one type matters for fear of getting caught up in the political negotiations. Is it something that has been raised in the political discussions with the EU?

Mr Philip Hammond: Yes. We have been in discussion with the European Union about a regulator-to-regulator dialogue to deal with some of the concerns that the industry has about day one issues. I met Vice President Dombrovskis yesterday to discuss these issues.

Q227 **Mr Alister Jack:** Chancellor, could we move to pay gap reporting? I would like to ask you, first of all, what your assessments are of the main trends emerging from the financial services sector's gender pay gap reporting? I will make the question longer. I can see you are looking at your notes.

Mr Philip Hammond: The Government are committed, as the Committee is well aware, to eliminating the gender pay gap. You are asking a question specifically about financial services. The Government launched the Women in Finance Charter to address the lack of



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representation of women in senior managerial roles in financial services and, as the Committee will know, I think, 205 firms across the financial services sector have signed up to the Women in Finance Charter, covering over 650,000 UK financial services employees. The UK was one of the first countries to introduce gender pay gap reporting and obviously the deadline for the first year of reporting was at the beginning of April. Not everybody has yet complied; 10,014 organisations in total across the economy had reported their figures by 4 April. We will look carefully at the data that has been reported and data that we still expect to receive. There is now a process going on of seeking to secure that data from the organisations that have not yet complied with their legal obligation.

Mr Alister Jack: You are rattling through answering a few of the questions but just coming back to the first one, it was really relating to the main trends emerging from the financial services sector reporting. Do you think the lack of women in senior positions is the main explanation for the gender gap?

Q228 **Chair:** Just before we get there, sorry, Alister, there has been a lot of newspaper reports. I am sure that you have press cuttings even if you don't read the newspapers. What is your thinking on the gap that financial services firms have reported? Are you happy with it?

Mr Alister Jack: That is one of my questions.

Chair: Sorry, it was a long answer read out from a file. It didn't really answer the question.

Mr Philip Hammond: Obviously we want to see the gap closing. I think the point about this reporting is to give us a baseline against which we will be able to measure clear progress. This is the first year of reporting. It creates the baseline. The question will be how that gap is closing next year and the year after.

Mr Alister Jack: I will give you the questions.

Q229 **Chair:** Thank you. What do you think of the numbers you have seen, Chancellor?

Mr Philip Hammond: Well, there is a gap and we would like the gap to close.

Q230 **Chair:** Could you get a little more emotional about it? Do you think it is acceptable?

Mr Philip Hammond: Clearly the Government believe that the gender pay gap is not justified and needs to be closed.

Q231 **Chair:** Doesn't it concern you that women at Barclays, for example, are being paid bonuses about three times less than men?

Mr Philip Hammond: Yes.

Chair: Right, good.



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Q232 **Mr Alister Jack:** Right, ladies, steady on. Clearly the roles that different people have within the organisations are creating a problem. We would agree with that.

Mr Philip Hammond: Yes. Well, that is probably one of the reasons. It may not be the whole reason.

Q233 **Mr Alister Jack:** Is the system flawed? Is that charter flawed in the way it reports? Should it take more recognition of different roles and then break it out and have comparators at different levels in organisational structures?

Mr Philip Hammond: It would certainly be informative to know more about the composition of the difference and to understand the different drivers of the pay gap. The different structures of careers, different representation of women in different parts of an institution will be relevant.

Q234 **Mr Alister Jack:** Would you consider reporting more along job grades and amending the charter?

Mr Philip Hammond: The Government Equalities Office will want to consider carefully the data that has been reported and to consider how and when and whether we need to change the requirements for reporting. But I think it would be extraordinary to do that within days of the deadline for the first set of reporting. Let's digest it, let's look carefully at it and consider what we can learn and what more we need to know and what information would best help us to know it.

Q235 **Mr Alister Jack:** Some professional services firms have omitted partners' pay from their reporting. This is the old thing where, as ever, the lawyers have managed to find a loophole and in this case it is for themselves. I don't think that is within the spirit of the requirements. Do you think the Government should require that the remuneration of partners is included within the figures?

Mr Philip Hammond: That will have to be a question for the Government Equalities Office to look at. The way the rules were structured was about pay and bonuses. I guess it does not include equity partnership shares. Maybe it should but I think that is something we need to look at across the spectrum, not just in financial services. It is particularly relevant to professional services but there will be other areas as well where limited partnership structures are used.

Q236 **Mr Alister Jack:** *The Financial Times* reported that numerous companies changed their pay gap data after the newspaper contacted them and that many firms have pay gap submissions that appear to be statistically unlikely, such as having both a zero median and a zero mean pay gap. What checks do you think the Government should be putting in place to make sure that submissions are more accurate?

Mr Philip Hammond: Companies have a legal obligation to report and to report accurately, but when we introduce new regulations, new



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measures, the typical approach is in the early stages to work with taxpayers, in this case with companies, to try to help them to be compliant, so using support rather than the stick to point out to them gently where they may have made mistakes, where they may have misunderstood what it is they are required to report. But obviously there will come a point where the authorities will need to become more robust if people are not reporting correctly the information that is required.

Q237 Mr Alister Jack: Would it help if the Government asked them to put it into their companies' annual reports and accounts?

Mr Philip Hammond: That would mean that it was subject to oversight by the auditors. That may be one way of securing better compliance with the reporting requirements, yes.

Q238 Chair: Sir Tom, can you just remind us? I can't remember what the Treasury's gender pay gap was?

Sir Tom Scholar: I wrote to you about it. If my memory is correct—I have got it here—it was something like the mean pay gap was 3.5% with a higher figure on the bonuses, which I think was 10%.

Q239 Charlie Elphicke: Chancellor, can I ask you about Government issued debt? Interest rates have been quite low for quite a long time, as has inflation. The Governor of the Bank of England goes up and down the land telling us that rates might get higher. Why would it make any sense to issue index-linked gilts now?

Mr Philip Hammond: That is a question for the Debt Management Office.

Q240 Charlie Elphicke: Isn't that a policy?

Mr Philip Hammond: If you are asking for my opinion, I think that we need our gilt issuance to be balanced. There needs to be an index-linked element in it. Obviously there are upsides and downsides to any type of gilt issuance and I think having a balanced portfolio is the best way to protect the taxpayer over the long run.

Q241 Charlie Elphicke: But we have been issuing gilts at 25%, 400 billion stock of index-linked gilts, which is more than twice the rate of the United States, Germany and France. Why?

Mr Philip Hammond: The UK has had a policy of increasing the percentage of index-linked gilts in the mix, but these policies are continuously under review.

Q242 Charlie Elphicke: That is your policy. Robert Chote said he is struck by the sensitivity of the public finances to interest rate and inflation shocks as a consequence of this. Why is this your policy?

Mr Philip Hammond: That has been the policy in the past. It is easy to look at the mix in the stock of gilts at a point in time and to suggest that perhaps it is not the most favourable mix for this point in time. But of



course these policies are around a stock of gilts that will be with us in some cases for many years, so a judgment has to be made. The judgment is made primarily by the Debt Management Office about the mix.

Sir Tom Scholar: If I may add something on the specific question of the proportion of gilts that are index-linked. We said in the Budget that that was something specifically that we would be looking at and the Debt Management Office has been following that, has been consulting on that and it is something that in due course will come back to the Chancellor to consider.

Q243 **Charlie Elphicke:** Sir Tom, it has been 25% since about 2010. Interest rates could not have been much lower since that point, nor could inflation. Why have you been issuing index-linked gilts when we could be issuing gilts at very low interest rates on very long terms, locking in very good rates for the public finances for the long term? Why don't we do that?

Sir Tom Scholar: As the Chancellor said earlier, the Debt Management Office provides us with its advice and the Chancellor makes the decisions, but in providing that advice and taking those decisions we seek to minimise the cost to the UK Government of issuing its debt. There is very good demand for index-linked Government debt because many people have long-term index-linked liabilities that they are looking to hedge or match, so there is good robust demand for that. The fact of being able to sell into a market where there is good demand means that we can get a good price.

Q244 **Charlie Elphicke:** That means you would be mortgaging the future, doesn't, Sir Tom?

Sir Tom Scholar: There is always a balance to be struck and there is a balance to be struck between cost effective issuance of gilt, of debt, as you say and the OBR has noted. The increase in that over time has increased the degree to which a future rise in inflation would hit the public finances. There is a balance to be struck there and in the Budget we said that was something that we had now decided we would look at.

Chair: We are going to finish off with local authority funding.

Q245 **Catherine McKinnell:** There have been serious concerns about the sustainability of local authority funding raised by the National Audit Office, DCLG and the Conservative Chair of the Local Government Association, among others. To put it into context, Newcastle City Council will have lost £283 million by 2020, which makes it a £268 a head cut compared to an England average of £131 a head or a £2 a head cut in Wokingham. While local taxpayers in Newcastle are facing cuts to local services, there is an increase in the council tax on top of increased social care precept on top of an increase in their police precept. They are wondering how does it add up to the Government that that is fair for the areas that are the most deprived, with council taxpayers with the least



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ability to pay these additional local taxes and the least able to raise alternative funding?

Mr Philip Hammond: There is a formula that the Government attempts to ensure it is fair.

Q246 **Catherine McKinnell:** Which removes deprivation weighting that has resulted in the most deprived parts of the country facing the biggest hikes in taxes and the lowest grant from the Government.

Mr Philip Hammond: There are a number of sources of pressure on local authority funding. Deprivation is a source of pressure. Sparsity, rurality, is equally a driver of cost for local authorities. Demography is also a source of pressure and the ageing process is no great respecter of economic status. Areas with higher than average proportions of elderly people, areas with higher than average proportions of people in economic deprivation and areas with sparsity of population distribution will all face cost drivers. My own area, Surrey, which people may think of as an affluent area, has an unusually high concentration of adults with learning disabilities, for historic reasons, and that is a huge driver of cost for the county council in that area. There are many different drivers of costs and the formula seeks to be as fair as possible. If I could add that councils in England will have access to over £200 billion to deliver local services from 2015 to 2020 and, of course, in looking at local authorities' ability to deliver services, it is not just the grant funding from central government. It is also access to council tax and business rates that need to be taken into account.

Q247 **Catherine McKinnell:** I was going to get on to that, because the local authorities currently face a long period of uncertainty about that future funding base, which has been highlighted in the DCLG Committee report this week. Responding to that, the Conservative Chair of the Local Government Association said, "The money local government has to maintain vital services is running out fast. Councils will see their core funding from the central government further cut in half over the next two years and almost completely phased out by the end of the decade. Delays to when business rate reforms will be implemented mean councils are facing a financial cliff edge in two years that the Government has to address". Is Lord Porter wrong?

Mr Philip Hammond: The Government are aware of, and I have acknowledged at the despatch box many times, the pressures that local authorities are facing. Local authorities have done some amazing work in delivering services efficiently and effectively, but they do hold substantial reserves. Local authorities' reserves currently stand at £23 billion, which is an increase of £8 billion since 2010.

Q248 **Catherine McKinnell:** Sorry, could we talk more specifically? You acknowledge that Lord Porter is not wrong about the financial cliff edge that local authorities face.



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Mr Philip Hammond: No, I acknowledge that local authorities are under pressure.

Q249 **Catherine McKinnell:** The Chancellor must know that reserves are exactly that, they are reserves. They do not make up for the shortfall in annual spending that local authorities face. What analysis has the Treasury undertaken to find out whether local tax bases and local economies can sustainably fund local services going forward? Have any other local authorities been identified in addition to Northamptonshire that may be in financial trouble?

Mr Philip Hammond: This is a lead responsibility for the Ministry of Housing, Communities and Local Government and it will—

Q250 **Catherine McKinnell:** But you control the purse strings. This is a financial sustainability question about our local authorities and whether they can sustainably provide local services and that is a matter for the Treasury.

Mr Philip Hammond: The settlement to local government is made in aggregate. The Ministry of Housing, Communities and Local Government is responsible for the distribution formula that is used.

Q251 **Catherine McKinnell:** Has it undertaken an assessment of the financial sustainability of local authorities up and down the country?

Mr Philip Hammond: Of course it will have a model that analyses the yield of the council tax base in different local authority areas.

Q252 **Catherine McKinnell:** The Treasury has not undertaken an assessment of the financial sustainability of local authorities under the reforms that it has implemented that have put local authorities in the situation that they are in?

Mr Philip Hammond: CLG will do that analysis. We don't duplicate things across Government. That will be done in CLG.

Q253 **Catherine McKinnell:** But CLG has to deliver and respond to the decisions of the Treasury.

Mr Philip Hammond: Of course we work very closely together.

Q254 **Catherine McKinnell:** Has there been an assessment undertaken as to whether local authorities are financially sustainable over the next two years, the next five years, on the basis of the current settlement that they are looking at and also the delay in the implementation of the business rate reform?

Mr Philip Hammond: Of course we work very closely with CLG and it shares its analysis with our experts in Treasury.

Q255 **Catherine McKinnell:** Have you identified any other local authorities that are in financial difficulty potentially?



Mr Philip Hammond: I am not aware of any other authorities that are at risk. Many authorities face pressures, of course, but I am not aware of any other authorities that are at imminent risk. I would remind the Committee that it is the Government's intention to carry out a spending review in 2019, which will be an opportunity to look at priorities across the whole arena of public spending.

Q256 **Catherine McKinnell:** Could I say to the Chancellor that local service provision is one of the biggest issues now in my constituency mailbox? Local people are concerned about litter, graffiti, antisocial behaviour, vandalism, grass cutting, dog fouling, cuts for youth services. You name it about local services, they are concerned about it. The Government's cuts are clearly having a real impact. They might appear like low-level issues but they are having a real impact on the quality of life of local people and their ability to enjoy their environment. Can the Chancellor give my constituents some hope that there is going to be some respite to the continuous cuts to local services that are having such a detrimental impact?

Mr Philip Hammond: You gave a long list of concerns and issues. I could add, from my constituency postbag, potholes, which are probably the number one issue, but what you did not mention was the two biggest items in local authority budget pressure, which is long term care of the elderly—

Catherine McKinnell: I was coming to that.

Mr Philip Hammond: —and social care of working age adults.

Q257 **Catherine McKinnell:** That is the issue. Local authorities are spending all their money trying to meet their statutory obligations for social care and for children in care, which I know that other colleagues want to ask about.

Mr Philip Hammond: That is the challenge that we face.

Q258 **Catherine McKinnell:** But by answering that, Chancellor, you are suggesting that you have no regard for these issues that may appear low level that are having a really serious impact on the day-to-day happiness and wellbeing of people up and down the country.

Mr Philip Hammond: No, I am agreeing with you. I am simply pointing out the cause, which you obviously are aware of but you did not mention in your previous list. The main driver of pressure on these services is the dramatic growth in the cost to local authorities of funding long-term care of the elderly, driven by demography, and working age adult social care, which is also largely driven by demography and the advance of medical technology. Those are very significant issues, which the Government have acknowledged. We are committed to a Green Paper on social care before the summer recess, which looks at the social care funding system and the overall sustainability of it, the challenges and how we are going to meet them. We have to look at this problem in the round.



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Q259 Catherine McKinnell: Yes, I agree and there is a massive shortfall in the funding. The LGA has made clear that adult social care still faces a £2.2 billion funding gap by 2020 and that does not even include the back pay sleep-in payments that need to be made to carers. These are unfunded cost pressures just adding to the cost pressures on local authorities and the impact on ordinary council taxpayers. You mentioned a Green Paper, but surely this issue is urgent and continuing to put off dealing with a crisis by announcing a Green Paper that is not yet published quite frankly just is not good enough. When will the recommendations in this Green Paper be implemented? We need to see urgent action on this issue.

Mr Philip Hammond: We are aware of the pressures. Over the three years 2017-18 to 2019-20 we have announced £9.4 billion of additional funding capacity for local authorities through the Better Care fund, the adult social care council tax precept, the adult social care support grant—together £9.4 billion—but we are aware that to make the system sustainable in the long term we have to look at some of the fundamentals of it and that is what we are doing ahead of the Green Paper that will be published before the summer recess. We will then need to take measures forward as a consequence of that Green Paper, but there are some pretty big and important decisions that need to be made. Sir Simon Stevens made a contribution to this debate this morning that some people will find controversial, but I think we have to be prepared to ask the big difficult questions about how we fund an ageing population that will continue to be a source of pressure on local authority budgets for the foreseeable future. As a society we have to decide how best to respond to that.

Q260 Mr Simon Clarke: Chancellor, you identified three factors that drive pressure on local authorities: deprivation, sparsity and demography. All three of those are present in my own local authority of Redcar and Cleveland that has the perfect storm of poverty, sparsity and ageing population. Business rates retention concerns me insofar as I think I am right in saying we are forecast to have the very lowest level of business rates in the whole of the country. What mitigation will be put in place for those authorities such as my own that, if we do not mitigate, stand to have a very low revenue stream?

Mr Philip Hammond: The overall formula for supporting local authorities will take account of the likely yield from other sources of revenue that authorities have: business rates retention and council tax.

Q261 Mr Simon Clarke: There will be a balancing, a dampening fact to prevent them from losing out?

Mr Philip Hammond: Yes, of course.

Q262 Mr Simon Clarke: Specifically the authority has raised with me the pressure that it faces with children in need. Our briefing today sets out that there has been a 10.9% increase in the number of children classified as being in need—sorry, looked-after children—from 2010-11 to 2016-17.



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I think Redcar and Cleveland's figures are rather higher than that. They identify this as a particularly problematic factor in the pressure on children's services. Is that something that could be looked at as part of the spending review next year?

Mr Philip Hammond: Everything will be looked at as part of the spending review. That is the point of the spending review. It is a comprehensive reappraisal of what Government do and what Government's priorities are. But of course the spending review will take place within the context of the real world fiscal constraints that we face.

Mr Simon Clarke: Yes, and which I appreciate.

Chair: I think we will count that as your first submission to the spending review for next year from Mr Clarke.

Mr Simon Clarke: Getting in early.

Q263 **Chair:** I want to finish on one matter, which is fixed-odds betting terminals, which you will know are a source of huge concern in terms of the stakes to Members across the House from all different constituencies. I appreciate you might not be able to say anything definitive, given where we are in local elections, but I just want confirmation that you are aware of the issue, it is something you are looking at, or the Treasury is looking at, and particularly you are aware of the moral consequences of high stakes.

Mr Philip Hammond: Yes. I have had discussions with the Culture, Media and Sport Secretary and we are mapping a way forward. As you have indicated, this is something that is subject to the local government purdah rules, so I don't think I can say anything more at this stage.

Chair: Thank you both very much indeed for being here this afternoon. I am sure that next time, whenever it is, there will be another long list of things to raise with you. Chancellor and Sir Tom, thank you for your time this afternoon.