JRA

JERSEY RETAIL ASSOCIATION

November 7th 2017

Deputy J A Le Fondre
Chairman, Corporate Services Scrutiny Panel
States of Jersey Scrutiny Office
Mourier House
St Helier
Jersey
JE1 1DD

Dear Deputy Le Fondre,

Review of Draft Budget Statement 2017. Budget proposal

Thank you for your letter of 27th October 2017 requesting a written submission on the budget proposals published on October 2nd. We are grateful for the opportunity to raise serious concerns over some of the proposals contained therein.

The key issue contained in the Budget is of course the proposal to **introduce a 20% tax on retail profits above £500,000.** We do not believe that the concerns set out below have been taken into consideration by the Treasury Minister when drawing up the new tax proposals. We believe that if implemented, the proposals are likely to damage the retail industry in Jersey and will commence a period of decline that will ultimately reduce GST revenues received by the States of Jersey.

The Jersey Retail Association (JRA) is a new organisation set up to promote the retail industry in Jersey, which is an important part of Island life and integral to our tourism industry. The JRA has received start-up funding from the Economic Development Department (EDTS&C) in the expectation that membership fees will provide sufficient resources to fund the future work of the Association. The comments contained in this letter concern the future of the industry as a whole and are not intended to promote the interests of any minority group. The membership of the JRA is content to pay fair and reasonable tax and our alternative proposals for raising funds are included at item 12.

Our concerns are as follows:

1. There has been no consultation whatsoever with the industry on the proposed new tax, either through the newly created JRA, its predecessor the Retail Development Group or the Chamber of Commerce. We respectfully suggest that any industry singled out for a special tax should have the courtesy of being consulted to enable all issues to be addressed. Furthermore, the EDTS&C have instructed an officer to develop a new retail strategy for the Island and this work is uncompleted, it is bizarre that the tax proposal has come forward in complete isolation to this strategy.

2. The JRA and its members are at a loss to understand why the Retail industry should be singled out for a 20% tax charge when the basic rate is Zero and the high-margin-creating Finance Industry is

taxed at only 10%. It has been argued that UK based retailers should pay tax to Jersey rather than the UK, however there are many businesses operating in Jersey across the entire economy that are owned by UK based companies, why single out retail? If other industry sectors are not taxed to the same extent as retail, then the tax is discriminatory and unfairly singles out the retail sector for more burdensome treatment than any other sector. It was the Sates of Jersey that decided to adopt a Zero-Ten tax regime to protect the finance industry in Jersey, if the States no longer like this regime then it should be amended in a non-discriminatory manner and the JRA calls for a complete review of the Zero-Ten system before embarking on piecemeal tax increases.

3. The very short time scale from announcing the detail of the measure (October 2nd) to implementation (January 1st 2018) promotes the Island as an unstable tax jurisdiction, where taxes are introduced without consultation and without observing basic fairness. This uncertainty over tax levels is justified by the fact that several changes have been made to corporate taxation arrangements since the introduction of the Zero-Ten regime being implemented in 2009. The JRA believe that the intention is to quickly reduce the £500,000 threshold proposed to capture a much larger part of the industry, in a similar way to GST, which quickly went from 3% to 5%.

4. The industry is concerned that the intention to levy tax from January 1st 2018 will make it retrospective. This is because most retail companies (especially larger retailers) will finish their financial year mid calendar year, meaning that profits earned up to December 31st will be taxed at 20% before the legislation comes into effect on January 1st 2018. The Budget proposition claims that this retrospective element can be avoided by retailers choosing to change their year-end to 31st December. Bearing in mind that the tax will initially target larger retailers, and the budget is not due to be debated until the end of November, it is totally impractical to expect businesses to change their accounting period and organise stock takes at such short notice and during the busiest time of the year. It is simply wrong to tax retrospectively and give businesses an impossible criterion to achieve to avoid the retrospective element of this tax.

5. The new tax must be seen as part of the bigger picture of general tax increases effecting the economy, long term healthcare tax, waste taxes on businesses, construction levies, charges on licenses to employ non-residentially qualified residents. These are all impacting upon the retail industry in Jersey together with concerns over Brexit, leading to the sector being in recession last year by 3% (see 'Measuring Jersey's Economy GVA and GDP – 2016' Table 3, issued by the States of Jersey Statistics Unit 29th September 2017).

6. The proposed tax rate of 20% is uncompetitive against UK corporation rates that are currently 19%, will reduce to 17% in 2020 and the current Government has committed to reducing UK corporation rates to 15%. Against this background, UK based companies with branches in Jersey will use legitimate transfer pricing to charge head office services, capital charges and brand royalty fees to reduce taxable profits in the island. The JRA do not believe that the level of tax that the Treasury hope to raise will be achieved.

7. The new tax will discourage investment in existing retail businesses for the following reasons:

    a. For UK based businesses the uncompetitive tax rate is likely to be an incentive to switch investment to other jurisdictions where either tax rates are lower or the cost of doing business is lower relative to the size of market that can be exploited. Many UK based retailers are maintaining their revenues during the UK retail slow-down by expanding into Europe and the Far East, where untapped markets are proving very lucrative. It must be remembered that Jersey is a difficult jurisdiction to do business in because of high costs, poor access to labour and a limited market.

    b. For local retailers the tax is largely unavoidable and therefore 20% of taxable profits will flow to the Treasury and simply be unavailable for investment by local retailers.

    c. For new businesses and entrepreneurs, the tax and the threshold are incentives to open a business in something other than retail. The threshold in particular is sending out the message that retail businesses should not grow to beyond producing a profit above the threshold or a penal marginal rate of between 40% to 60% will be payable on the additional profit.

8. The new tax proposals and in particular, the threshold proposals are likely to completely stop the expansion of local retailers in Jersey generating profits near the threshold. This is due to the aggressive manner in which the tax rate increases from 0% below £500,000 to 20% (payable on all profits) at £750,000, which actually makes businesses trying to expand worse off than if they remained below the threshold. For example, an existing retailer producing taxable profits of just below £500,000 sees an opportunity to open new premises to satisfy a demand or perhaps is presented with an opportunity to acquire another retail business, it is expected to significantly increase profits to £750,000 and will require a capital investment of £1.2m to achieve this (including stock investment). The business leader runs a forecast and finds that upon achieving profit of £750,000, tax of £150,000 will be due (20%) and capital repayments will be required of £120,000 per annum meaning that in cash terms, the company is actually £20,000 per annum worse off and no additional cash is available to return to shareholders to reward them for risk. The business leader decides that there is no point in applying his talents to this venture when, after the significant effort he puts into the expanded business and the risk taken by his shareholders, there is no financial reward from the investment until the capital sum is repaid in 10 years and the expansion does not proceed. It should be noted that at profits of £750,000, the tax due of £150,000 equates to 60% of the difference between the two thresholds (i.e. 150,000 / (750,000 – 500,000) x 100 = 60). This penal rate will discourage more businesses from expanding as threshold rates are reduced to capture more businesses to increase tax receipts.

9. The JRA has been informed that food retailers that are operating under extremely small margins may be forced to increase prices in order to make sufficient returns to justify their capital investment. There is a risk that prices may rise by 3%, which will hit all consumers but the poor and those on fixed incomes the most.

10. The footfall in St. Helier's shopping center has been falling for several years, last year footfall was -2.3% and this year it is currently -2.2%. If St. Helier is to attract people (islanders and visitors) to shop then the industry must constantly invest in both the offer presented to customers and the staff that are working there. There has recently been significant investment in the industry, with De Gruchy undertaking an extensive refurbishment and Next due to open a completely new store, this is an exciting time for St Helier. Why is this important for the States of Jersey? Because the Treasury collects significant amounts of GST on retail sales made in the Island. This GST is largely lost when shoppers spend on the Internet, it is therefore in the State's interests to encourage local retailers to continue to invest in their businesses.

11. The longer-term effects of the new tax will be to discourage entrepreneurial activity in retail, lose the industry disruptors that are so important to a vibrant retail offer and is likely to signal a slow decline in the island's retail industry and consumer choice. It will not be long before St. Helier has a retail offer that is similar to Guernsey, where customers are forced to shop on the Internet because of a lack of on-island choice. Once this decline starts to become apparent, it will be very difficult to turn around without significant States incentives. The retail offer in both the Isle of Man and Guernsey is not as vibrant as Jersey and in Guernsey it is in decline, possibly in part because of their own retail tax. Shoppers from Guernsey actually visit Jersey for the wide choice of shopping in the Island, this may will not last if the quality of choice diminishes.

12. The JRA believe there are other alternatives that should be considered to amend or replace the current proposals. These will produce greater tax returns than those currently proposed, will not discriminate against any one industry sector and will avoid the long-term negative effects of the current proposals. The alternatives to consider are:

    a. Instead of singling out the retail industry for tax, apply the 10% rate to all businesses that operate in Jersey.

    b. Apply a 10% rate on all business profits and remove the threshold that will discourage investment and expansion of smaller businesses.

    c. Make the tax effective from January 1st 2019 or another date to avoid retrospective taxation.

    d. Reduce the GST deminimus level on imported goods to zero, requiring UK based retailers to pay the GST due before parcels are shipped to the Island. This will also provide a level playing field for Jersey retailers, whether based in the Island or UK.

    e. The introduction of capital allowances which would be pre-tax and encourage investment.

We hope the above is sufficient for you to undertake a full and serious review of the current proposals. You and your panel should not underestimate the change that is running through the retail industry, with physical retailers battling for customers against pure play Internet retailers, this at a time when the Brexit vote has driven a collapse in consumer confidence. If physical retailers fail in Jersey then there will be a very large hole in the State's GST receipts and the best way to protect this is to encourage investment. The proposals on tax discourage this investment and risks the future of the retail industry in Jersey. We are happy to present these views in person and engage in meaningful dialogue with your panel.