STATES OF JERSEY

DRAFT BUDGET 2016 (S.R.10/2015): RESPONSE OF THE MINISTER FOR TREASURY AND RESOURCES

Presented to the States on 2nd March 2016
by the Minister for Treasury and Resources

STATES GREFFE

DRAFT BUDGET 2016 (S.R.10/2015): RESPONSE OF THE MINISTER FOR TREASURY AND RESOURCES

Ministerial Response to:	S.R.10/2015
Ministerial Response required by:	23rd February 2016
Review title:	Draft Budget 2016
Scrutiny Panel:	Corporate Services

MINISTER'S INTRODUCTION

The Minister issued an initial response to all States Members on 11th December 2015 in order that his views could be considered prior to the debate of the Budget 2016. In accordance with the Code of Practice for Scrutiny Panels and the Public Accounts Committee, the Minister is now presenting his full response.

The States Assembly approved P.127/2015, the Draft Budget 2016, on 15th December 2015. The Minister was pleased to receive the Panel's report prior to that debate and is now formally presenting his detailed comments on the findings and recommendations. Whilst welcoming the Panel's work, the Minister was disappointed to find that the Panel have chosen not to base their findings on the conclusions reached by their own advisers, CIPFA. In light of the conclusions contained in the Panel's own expert report, and the work that has already been done by the Treasury and Resources Department, the Minister is unable to agree with all of the Panel's findings, or to accept their 3 recommendations.

FINDINGS

	Findings	Comments
1	No background studies have been carried out as to the consequence on the housing market should these changes be implemented.	PwC provided independent, expert advice to the States of Jersey to inform the property tax review Green Paper. Part of their advice looked specifically at the issue of mortgage interest tax relief ("MITR"); PwC identified the following arguments against providing MITR – • It supports artificially high prices for housing that benefits current owners and create unnecessarily high barriers to entry for new buyers. • It encourages the use of debt, with potentially negative consequences for financial stability and household finances. • It drives a wedge between the cost of owner-occupation and the rental market that primarily disadvantages those on lower incomes and with less capital available to them. • It provides the largest benefit to those with the highest debt and the highest incomes.

	Findings	Comments
		• It appears to be positively correlated to greater volatility in the housing market. There is no reason to suggest that these arguments are not valid in the context of the Jersey housing market.
2	The Panel is also concerned that those already struggling to pay a mortgage may face great financial difficulty when this benefit is removed as it is not something they had planned for in the long term.	The Minister has proposed that MITR is phased out, starting in 2017 and taking a decade to complete. This phased approach has been adopted so as to allow existing and potential future claimants to adjust to the change in tax relief available. Based on the Taxes Office data available for the YOA 2013 it is estimated that the majority of taxpayers currently receiving MITR will not be impacted by the phase-out of the relief until 2021. Also, a significant number of taxpayers currently receiving MITR will not be impacted at all, as they will have repaid their mortgages during the phase-out period (paying less interest in each year than the applicable interest cap).
3	The eventual withdrawal of age enhanced exemption thresholds will adversely impact on pensioners, when one in three pensioners are already living in relative low income – twice the proportion of that in the UK.	This measure will not affect those pensioners who are living in relative low income. The relative low income figures recently published by the Statistics Unit are: £11,700 (single person) and £17,600 (couple). These compare to the standard income tax exemption thresholds for 2016 of £14,350 (single) and £23,000 (couple). Therefore no-one (be they pensioner or of working age) who is in relative low income will pay income tax in Jersey.
4	The forecasts for overall States income have increased by approximately £9 million since the presentation of the MTFP 2016 – 2019 in July 2015.	The States' income forecasts increased by £8.7 million in 2015, and are forecast to increase by £1.98 million in 2019 before the agreed 2016 Budget measures. The movements in income forecasts are explained in Section 12 of the Budget Report 2016, together with an explanation of the changes in economic assumptions. Appendices 1 to 6 provide further detail as to the movement in income forecasts for each area of income.
5	The personal tax forecasts in the 2016 Budget compared to the MTFP 2016 – 2019 show a deterioration of £26 million.	The Panel has focussed exclusively on the personal income tax forecasts which show a small deterioration against the MTFP of less than 2%, but have not recognised the forecast increase in company income tax of £26 million, which results in a broadly unchanged overall income tax forecast vis-à-vis the MTFP.

	Findings	Comments
6	The trend over the last decade of downgrading personal income tax forecasts continues in this Budget, which raises questions about the accuracy of forecasting models.	There is always significant uncertainty regarding income tax forecasting in terms of assessing future trends in the key economic variables such as economic growth, inflation, employment and average earnings; how they might translate into trends in taxable income, and what the yield will be from that taxable income. The IFG highlighted that, at the time of their last forecast, there was even higher uncertainty in general terms, and advised that the Council of Ministers must continue to maintain appropriate flexibility in the preparation of the MTFP Addition for 2017 – 2019, to recognise the potential range of outcomes and the risks for States income forecasts around the downside of the central scenario. There was a further slight reduction in personal income tax forecasts in Budget 2016 from 2016 onwards, which reflected the latest trends from ITIS in-year data for the first half of 2015 in respect of employment income. It is not yet clear that this trend did actually materialise in the full year data, and this will be considered in detail by the IFG as part of their next forecast.

RECOMMENDATIONS

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
1	An up-to-date impact study is carried out on the impact on the housing market to include the rental sector, as a result of these changes to MITR. This is to be presented prior to the lodging of the MTFP Addition – currently due on 30th June 2016.	T&R	Reject	The Minister can see no value in commissioning further advice on the impact of the withdrawal of MITR on the Jersey housing market. The States has already received expert advice on MITR from PwC, which is wholly consistent with the economic advice relating to MITR by respected bodies such as the OECD, EU and Institute of Fiscal Studies. Consistent with advice from PwC that the phasing-out of MITR is best achieved over a relatively long period of time, the Minister has proposed that MITR is phased out steadily over a decade.	N/A

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
2	The implementation of these changes are reviewed following the results of the impact study.	T&R	Reject	N/A	N/A
3	The age enhanced income tax exemption thresholds for taxpayers aged over 65 should not be removed from the year of assessment 2018 from taxpayers reaching the age of 65 after 1st January 2017 and that the age exemption thresholds should not be held at 2016 levels and instead should continue to rise in line with standard exemption thresholds.	T&R	Reject	Consistent with the strategic priority, the Minister is committed to delivering sustainable public finances. Currently, the enhanced exemption given to taxpayers aged 65+ costs about £4 million per annum. With the ageing demographic, the cohort of taxpayers eligible to claim the enhancement is growing each year. Based on the data available, it is estimated that the cost of the enhancement will increase by approximately £300,000 each year as the cohort of eligible claimants grows. This is unsustainable in the longer term, hence the Minister maintains that it is appropriate to limit the cohort of eligible claimants from the 2018 YOA.	N/A

MINISTER'S CONCLUSION

The basis behind all of the (now agreed) proposals in the Budget 2016 reflect the Medium Term Financial Plan, which has been constructed to allow a degree of flexibility, in line with previous recommendations of this Panel. The budget-raising measures here are part of that flexibility and, in the Minister's view, represent a prudent and sensible approach aimed to assist in the delivery of the States' primary strategic objective of sustainable public finances in a way which avoids taxpayers experiencing a major change in their tax position.

The focus of the MTFP 2016 – 2019 is on growing States' income and supporting productivity, whilst reducing departmental expenditure and maintaining other flexibilities within the Plan, including annual budget measures.