

June 2016

## **Distributional analysis of the MTFP proposals**

*compiled by the Chief Economic Adviser*

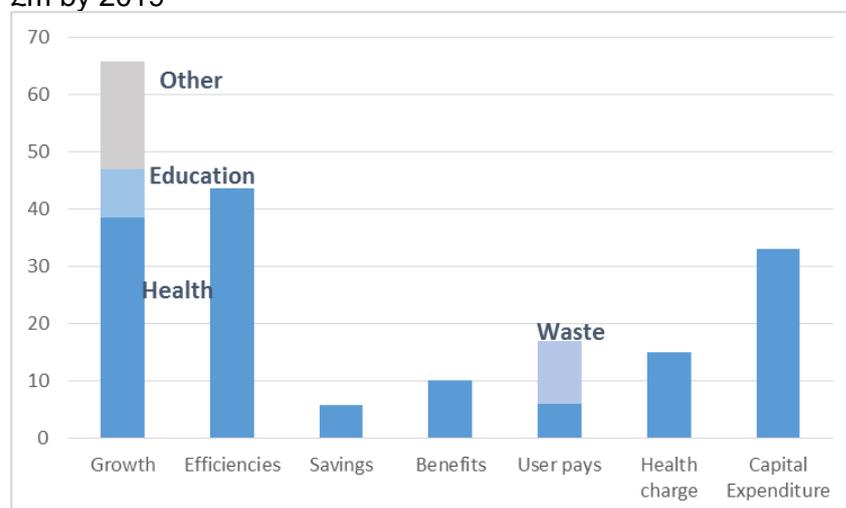
### **Summary**

#### *Introduction*

As set out in the terms of reference agreed with the Council of Ministers (see Appendix 1) this paper considers the distributional impact of the key proposals being considered by Council of Ministers as part of the MTFP Addition. It focuses on measures being considered in early June 2016 and not necessarily the final MTFP proposals. The analysis looks at how the impact of the proposed measures may vary across households in the income distribution. It is intended to be informative for Ministers and the States in understanding where the burden of the fiscal adjustment may lie by drawing on evidence and research from elsewhere and information provided by the Treasury and Resources Department about the nature of the measures that are proposed in Jersey.

Figure 1 below shows that the measures break down into 6 key categories covering changes in expenditure – growth, efficiencies and savings (including benefit changes), user charges, a new health charge and capital expenditure.

**Figure 1: Key components of MTFP addition**  
£m by 2019



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The paper covers the changes in four key sections:

- Section 1: Expenditure proposals
- Section 2: Benefit changes
- Section 3: User pay charges
- Section 4: A new health charge

The key findings from each section are summarised below:

### **Section 1: Expenditure**

The distributional impact of spending changes are generally much harder to analyse than tax/benefits changes. One of the biggest obstacles is that the monetary cost/saving that might occur from a change in expenditure do not equate to the benefits/costs to individuals of that change. The critical question is how each individual/household values the service and in particular how much they might be prepared to pay for that service. Different people will value a service differently, particularly if they have different options in terms of alternatives.

The efficiency savings presented in the MTFP Addition fall into the category of cash-releasing efficiency savings. These efficiency savings are designed by departments such that they will not impact on the level of quality of services provided by government and for the purposes of this analysis have been assumed to have no distributional impact.

With these caveats in mind, section 1 looks at what evidence elsewhere can tell us about the distributional impact of key components of the MTFP. Health expenditure is generally considered to be progressive. Assessing the distributional impacts of an increase in health expenditure is complex but the Institute for Fiscal Studies<sup>1</sup> conclude:

*“.....there is nothing that can gainsay the fact that the largest item of public spending in kind, health, also benefits most strongly lower income groups in which ill health is most strongly concentrated.”*

How education spending impacts different households at different points in the income distribution is less clear. However, a large proportion of the increase in education expenditure in the MTFP is a result of the Jersey Pupil Premium and a further increase is in secondary education which suggests that the increase in education spending will be broadly progressive in Jersey. However, the freezing of

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<sup>1</sup> The distributional impact of public spending in the UK, June 2010

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maintenance grants will be somewhat regressive for those affected but this is a relatively smaller measure.

Overall, the evidence from elsewhere is mixed on the impact of public spending outside health, education, social housing and welfare. Likewise the beneficiaries of capital spending are not always clear. The distributional impact of these aspects of spending in the MTFP is therefore difficult to determine.

## **Section 2: Benefit changes**

The benefit changes included in the MTFP were chosen with emphasis on ensuring that the benefit system is fair, encourages financial independence, is well targeted and changes are spread across large groups to minimise individual impact.

The benefit changes make up £9.5m of the overall measures, which is made up of £8.3m of Income Support changes by 2019 and £1.2m from targeting the Christmas bonus from 2016 onwards.

The Income Support changes affects about 6,500 households who are mainly towards the lower end of the income distribution. Overall, the changes are likely to be regressive.

The Income Support changes do not affect about 36,500 households who do not claim Income Support. These households range from the low end to the top end of the income distribution.

The previous Christmas bonus was a relatively small benefit paid to about 19,000 households (mainly pensioners) irrespective of income or wealth. Given the high proportion of pensioners in the bottom two quintiles this would appear to be a regressive change. However, replacing the previous Christmas bonus with a means-tested Christmas bonus, some of the potentially regressive impact will be offset, and vulnerable households at the lower end of the income distribution will not be affected. Likewise, some of the savings from making the Christmas bonus more targeted will be invested in the 65+ health scheme, which helps eligible pensioners towards the lower end of the income distribution with the cost of dental, optical and chiropody costs.

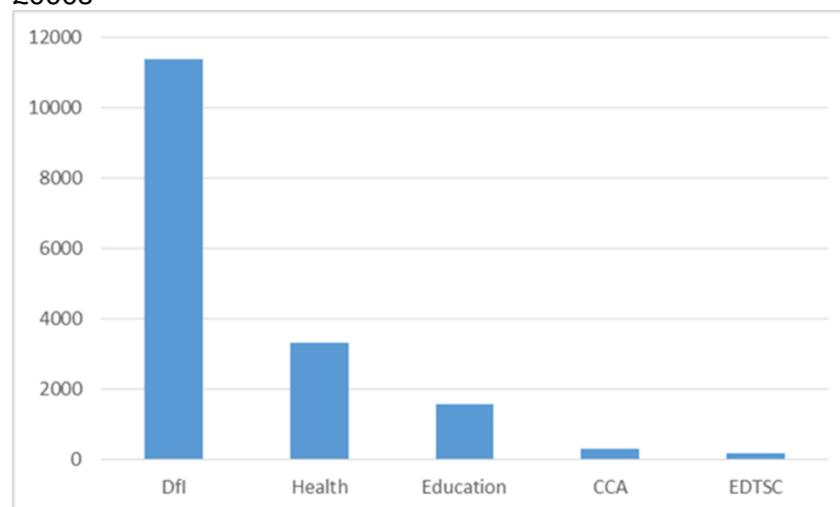
It is also important to consider what the impacts of the changes would be on different groups within those receiving income support and at the same points in the income distribution:

- Couples with children / existing pensioners will be less affected
- Single parents will be more affected
- The impact on other household types that receive income support will depend on their individual circumstances
- Most households do not receive Income Support and will not be affected at all by these changes.

### Section 3: User charges

There are a range of user charges proposals across a number of departments as set out in the chart below. The majority of them are in the Department for Infrastructure with other significant charges being those put forward by the Health and Education departments.

**Figure 2: User charges in MTFP by department**  
£000s



Section 3 looks at the distributional impacts of the key proposals and points out that when looking at commercial charges it is important to bear in mind what the actual incidence of the charge is - businesses do not pay tax, people do. This means that commercial charges (assuming they cannot be completely offset by efficiency gains) could impact on islanders through a number of routes:

- increased prices
- reductions in other costs such as employment costs (salaries and/or jobs)
- reduced dividends for shareholders (less likely)

How they feed through the economy does depend on the nature of the markets for the final product/service and whether they are domestic or export, the degree of competition from imports and the responsiveness of demand to price changes.

In summary section 3 concludes that while user charges may generally be regressive if a fixed charge per household, the following may be the case for charges covered in the MTFP Addition:

- Waste charges that feed through into higher prices will tend to be regressive
- A Green Waste charge could feed through in a more progressive way
- Reduced subsidies/grants to fee paying schools may be progressive
- Means-testing the Nursery Education Foundation may be also be progressive
- Increased fees for Jersey Music Service is likely to be regressive
- Reduced maintenance grants for on-island degrees is also likely to be regressive
- Medical user pays generally tend to be regressive but the impact of individual measures is complicated.

#### **Section 4: Health charge**

MTFP 2016-2019 originally included a target amount of additional revenue from the health charge of £15m in 2018 and £35m in 2019. The MTFP Addition 2017-2019 now includes a target amount of additional revenue from the health charge of £8 million by 2018, increasing to £15 million in 2019.

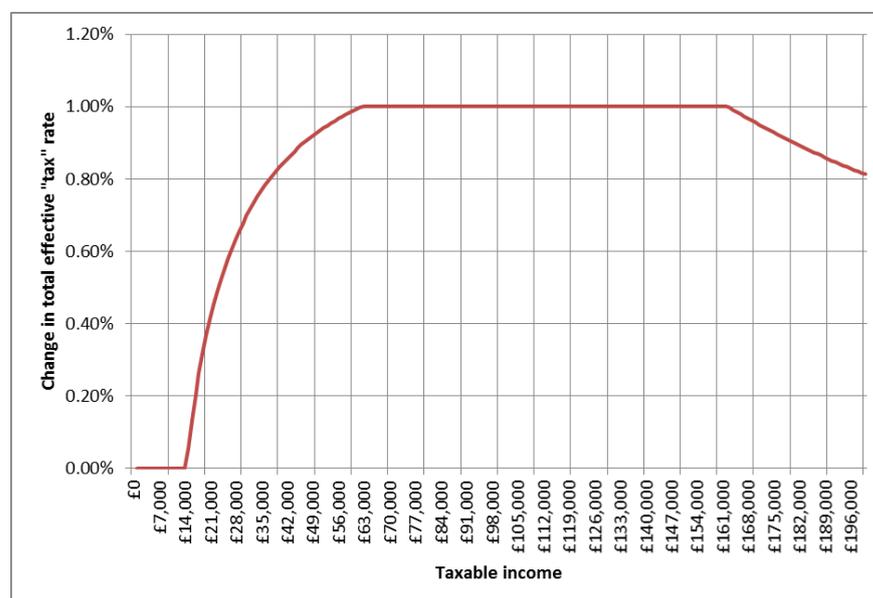
This section of the document outlines the distributional analysis associated with each of the potential revenue raising options considered by Ministers for the health charge. Having considered all these options there now appears to be two options which are receiving more detailed consideration: a new income based health charge which mirrors the Long Term Care contribution and an increase in GST.

The analysis in section 4 and summarised below for a single person shows that a 1% income based charge mirroring the LTC would be broadly progressive across the whole income distribution but would have the following distributional impacts between different parts of the distribution:

- there would be no impact on those people with incomes below the exemption limits
- for those on the marginal tax rate the effective rate would gradually rise to 1% as income rises (progressive for these income levels)
- for those on the standard rate of 20% the effective rate would be 1% for all incomes (subject to the next caveat) (proportional for these income levels)
- for those on the standard rate and above the £162k cap utilised for the LTC contribution the effective rate would gradually fall as a proportion of income as income rises (regressive for these income levels).

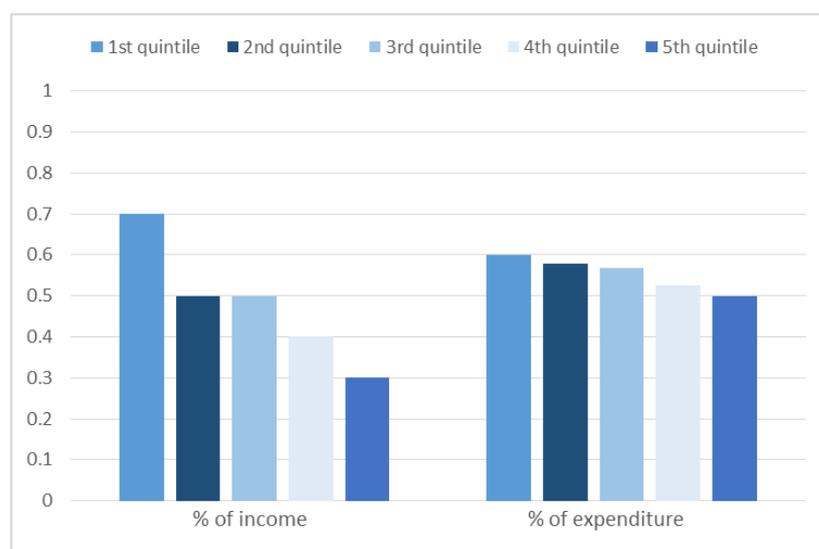
**Figure 3: Change in effective tax rate after introduction of a 1% LTC type health charge**

Single person, change in effective rate, % of income



The distributional impact of GST is summarised in the chart below. Section 4 highlights that it is important to look at the impact as a proportion income and expenditure and that while the degree varies slightly by the measure chosen, GST is mildly regressive. This is mainly due to the effect on those households on the lowest incomes, which spend a larger proportion of their income on essential items such as food and domestic energy. Those on higher incomes tend to save more and GST therefore represents a lower proportion of income/expenditure because they do not spend all their income in any one year.

**Figure 4: Increase of 1% in GST as a share of income and expenditure across the income distribution**  
%



Source: States of Jersey Statistics Unit/Economics Unit calculations

It is important to recognise that looking at the impact of the MTFP measure across the household income distribution is only indicative of the distributional impact. The distribution of household income is not the same as the distribution of wealth and changes in income are not necessarily reflective of overall changes in a household's welfare which could be impacted by monetary and non-monetary factors.

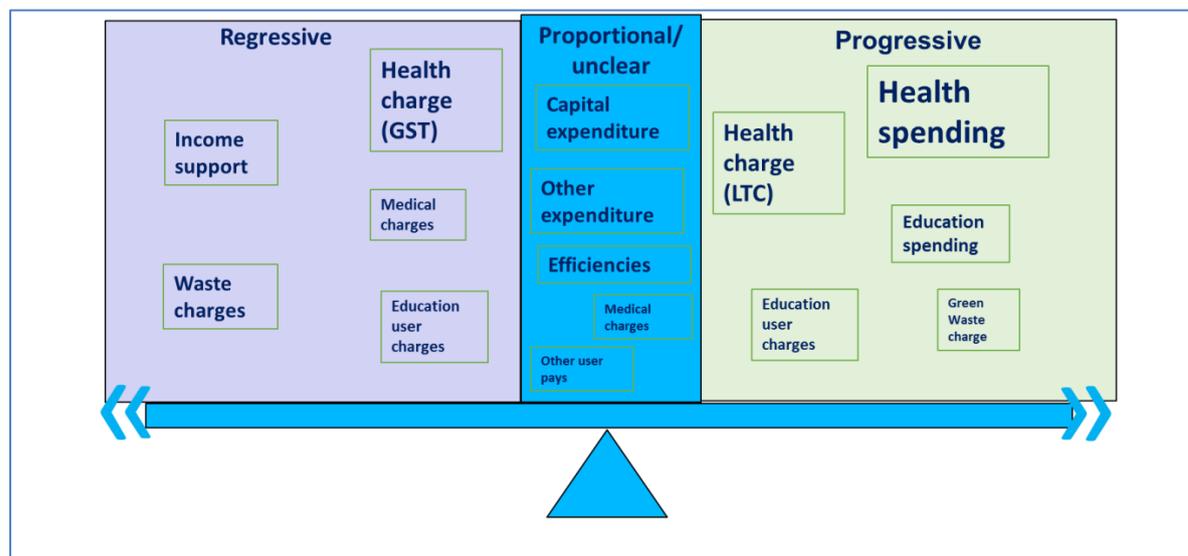
Such analysis does not take into account that households' circumstances may change over time and those in one part of the income distribution may only be there temporarily and that at different stages in their lifetime an individual's income may vary. For example, as people get older and more experienced their income may rise meaning that those in the lower part of the income distribution also spend time in higher parts of the distribution during their lifetime. Conversely there may be households which remain in one part of the distribution for their whole life time – for example some less well-off households may never leave the bottom part of the income distribution. This means that two households at the same income level at one point in time could be impacted by a fiscal change in significantly different ways over their lifetime.

## Summary

The table below summarises the key findings and where possible an indication is given as to whether measures are progressive or regressive or indeed where it may be difficult to say. How to achieve the correct balance is a political question but it is

important to recognise that comparing measures that are progressive and regressive is difficult to do. For example, a £1m measure that impacts on a certain group of high income households is not equally balanced by a £1m measure that impacts on a different group of particular low income households.

**Figure 5: Summary – is the balance right?**



### Policy issues

The distributional impacts of fiscal policy changes are complex and not always clear cut, especially where changes in expenditure are included. Even where it is possible to consider the impact of measures on households of different income this may only be looking at part of the picture and it is important to consider wider impacts in terms of wealth, welfare and impacts over people's lifetime.

Distributional impacts need to be balanced against other objectives such as the efficiency of public services, the competitiveness of the economy and ultimately the requirement to put finances on a sustainable footing to help secure economic growth.

When looking at the impacts of changes to fiscal policy it is also important to put it in the context of the impact of government policy as a whole, not just the changes at the margin. For example, if it was deemed that the combination of existing policies was unfair because it impacted too much on the better-off, regressive changes might be more appropriate. Similarly if the combined impacts of existing policy were considered to impact too much on the less well-off then a more progressive package could be justified.

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It is also important to consider what options there are to offset any distributional impacts that are thought to be unfair. It does not necessarily have to be the case that individual policies should not be pursued (particularly if they are achieving other objectives). However, they may require adjustment or compensating measures to protect those people of concern or future policy could be changed in a way to address aspects of concern e.g. in future budgets.

## Introduction

### Household Income Distribution Survey

The following sections of this paper draw on the Income Distribution Survey published by the States of Jersey Statistics Unit. The survey presents robust and representative information on the incomes of Jersey households, from a large survey of Jersey households carried out between April 2014 and May 2015.

Over 1,200 randomly selected households took part and the report looks at four stages of household income as summarised below. Between each stage components of income are included and deductions are made as set out below.

**Figure 6: The four main stages of household income**

<b>Pre-benefit income</b>	Sum all gross earned and unearned income, pensions, regular gifts and maintenance payments
<b>Gross cash income</b>	Above plus add benefits (household and individual)
<b>Net income before housing costs (BHC)</b>	Above less income tax, parish rates, social security contributions, pension contributions and transfers
<b>Net income after housing costs (AHC)</b>	Subtract mortgage interest payments, gross rent, service charge and buildings insurance
Source: Statistics Unit	

#### *Composition of income*

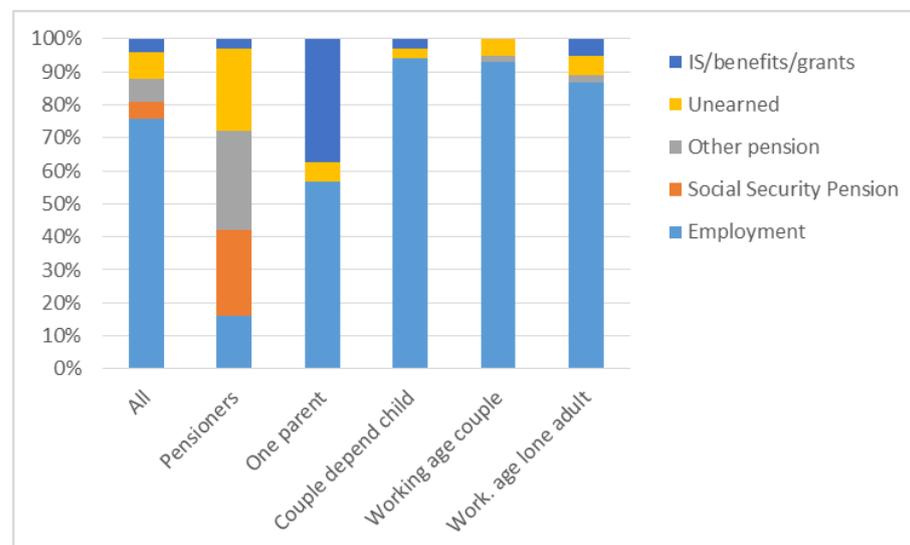
Analysing gross cash household income by source (see Figure 7) shows that three-quarters of total household income in Jersey originated from employment (including self-employed), nearly a tenth from unearned income sources such as shares or dividends and savings and an eighth of total household income was from a pension (public or private).

Looking at differences across the household types it is clear that pensioner households are more dependent on public and private pension (over 50% of income) and a quarter of their income comes from income support and other benefits. Single parent families are much more dependent on income support (37% of total), while

couples with/without children and working age adults living alone get about 90% of their income from employment.

**Figure 7: Composition of household income by source**

% of total for different household types



Source: Statistics Unit Income Distribution Survey

### *Equivalisation*

Average (mean) household income will generally be affected by household size - single adult households will generally have lower incomes than two or more adult households. Furthermore, housing costs will have differing impacts according to the size of the household. To remove the variation caused by differences in household size and make-up a process of equivalisation is used to standardise every household to the same household size and type. The standard used is that of an adult couple with no children. This process of equivalisation, allows fairer comparisons to be made across different sized households.

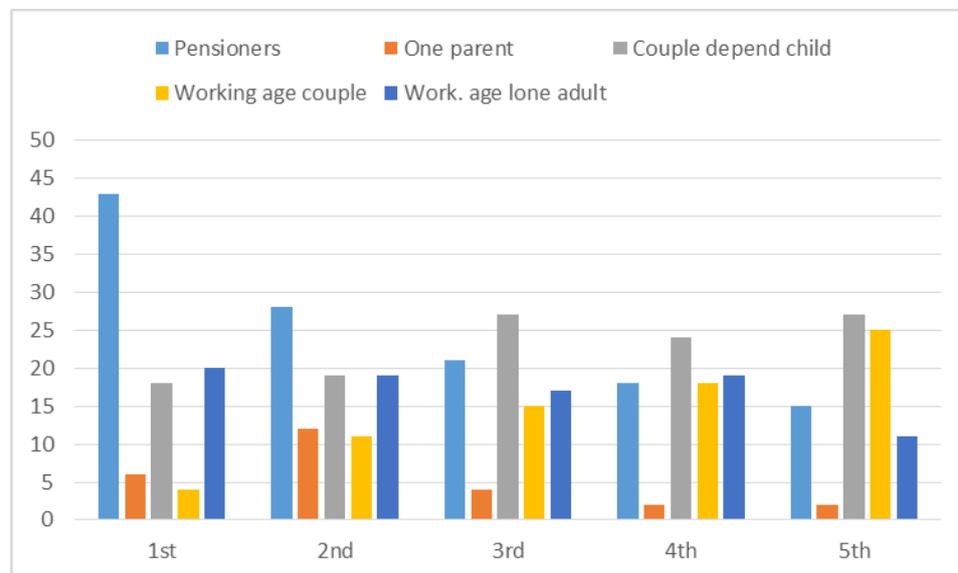
A useful approach for exploring the distribution of household income is to divide households in Jersey into five equal sized groups ('quintiles') according to their income level – the first quintile being the 20% of households with the lowest incomes, the second quintile being the next 20% of households and so on, up to the fifth, or top, quintile being the 20% of households with the highest incomes.

Figure 8 below shows the make-up of each quintile by household type. Pensioner households are more concentrated in the lower quintiles while couples with

dependent children and working age couples are more concentrated in the higher income quintiles. Single parent households are more prevalent in the lower income groups, while working adults are fairly evenly split across the lower 4 quintiles.

**Figure 8: Make-up of quintiles by household type**

% of each quintile



Source: Statistics Unit Income Distribution Survey

It is also possible to look at the actual mean and upper boundary for each income quintile which is set out in the table below.

**Figure 9: Income means and upper bounds by quintile**

Net income before housing costs, £

	Quintile 1	Quintile 2	Quintile 3	Quintile 4	Quintile 5
<b>Mean</b>	16,950	27,000	35,650	48,200	91,650
<b>Upper bound</b>	23,000	30,900	41,000	57,700	n/a

Source: Statistics Unit Income Distribution Survey

To get an understanding of how various fiscal measures impact on different parts of the income distribution it is possible to look at whether measures are:

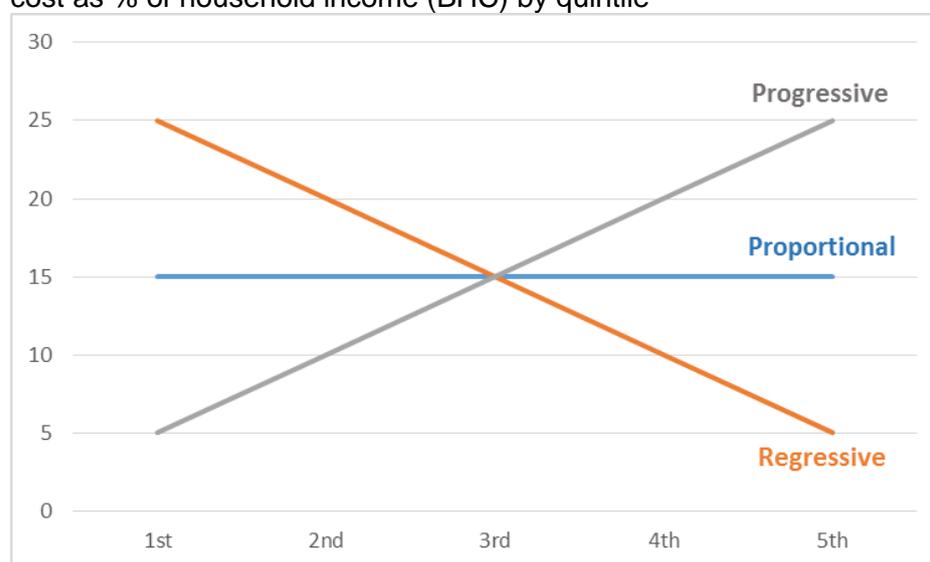
**Regressive:** The average cost to the household falls a share of income as income rises. This means that those with the lowest incomes pay more relative to their incomes (even though they may pay less in monetary terms).

**Proportional:** The average cost to the household is constant as a share of income as income rises. This could still mean that the lowest incomes pay less, just that it is the same proportion of their income.

**Progressive:** The average cost to the household increases as a share of income as income rises. This will mean that the better off pay more in monetary terms and as a share of income.

This is summarised in the chart below.

**Figure 10: Different distributional impacts**  
cost as % of household income (BHC) by quintile



Looking at the impact of the MTFP measures across the household income distribution and assessing whether they are progressive or regressive is only indicative of the distributional impact. The distribution of household income is not the same as the distribution of wealth and changes in income are not necessarily reflective of overall changes in a household's welfare which could be impacted by monetary and non-monetary factors.

Similarly, it does not factor in how people at different points in the income spectrum change their behaviour in response to the impact on their income. For example, where a measure appears progressive in terms of its impact relative to income it could have more regressive tendencies if the less well-off respond in such a way that

they are ultimately made worse off by consuming less of essential services or cutting back on other important expenditure.

Such analysis also does not take into account that households' circumstances may change over time and those in one part of the income distribution may only be there temporarily and that at different stages in their lifetime an individual's income may vary. For example, as people get older and more experienced their income may rise meaning that those in the lower part of the income distribution also spend time in higher parts of the distribution during their lifetime.

Conversely there may be households which remain in one part of the distribution for their whole life time – for example some less well-off households may never leave the bottom part of the income distribution. This means that two households at the same income level at one point in time could be impacted by a fiscal change in significantly different ways over their lifetime.

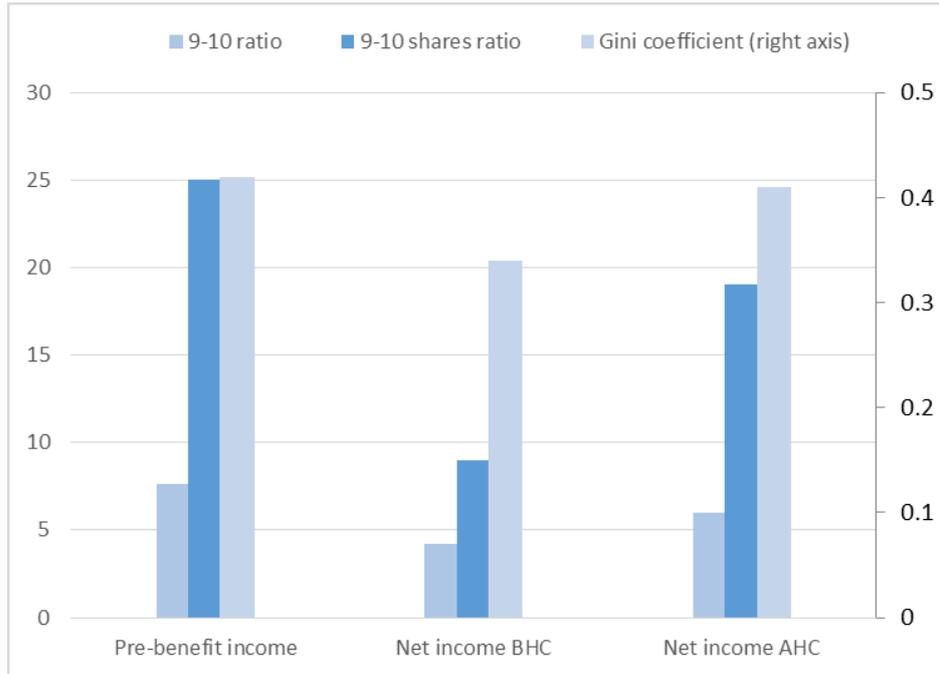
### *Income inequality in Jersey*

In all societies there tends to be some income inequality – that is incomes are generally distributed unevenly across households and some households have a higher income than others. There are a number of different ways of measuring the extent of income inequality with three of the measures covered in the Statistics Unit Income Distribution Survey covered below.

1. **90-10 ratio:** divides the income of the 90th percentile household by that of the 10th percentile.
2. **90-10 shares ratio:** divides the mean average income of those households in the top 10% by the mean average income of those households in the bottom 10%.
3. **Gini coefficient:** an indicator taking values between 0 and 1, where 0 represents complete equality (all households have equal income) and 1 represents complete inequality (one household has all the income).

The chart below shows each indicator for Jersey and a similar pattern where net income after benefits and taxes/contributions is more equally distributed than pre-benefits income. However, when housing costs are taken into account inequality widens again.

**Figure 11: Different measures of income inequality**



Source: Statistics Unit Income Distribution Survey

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## **Section 1: Distributional impact of MTFP expenditure proposals**

### **Summary**

The measures considered in this section fall into four broad categories:

- a. Revenue expenditure growth
- b. Revenue expenditure savings
- c. Routine capital expenditure
- d. Major capital schemes

It is much more difficult to measure the distributional impact of changes to benefit-in-kind government expenditure, when compared to cash benefits or revenue-raising.

There are a number of issues at work:

- a. Willingness to pay – The benefit to users of public services is not the same as the cost of providing the service.
- b. Public goods – It is particularly difficult to assign the benefit of a service which is used by society as a whole.
- c. Efficiencies – It has been assumed that efficiency savings do not impact on service delivery and therefore have no distributional impact.
- d. Administrative costs – It is difficult to measure the distributional impact of administrative costs which is an essential cost for provision of government services as a whole.

In revenue terms, the MTFP addition represents a significant increase in spending in health and education – after allowing for efficiencies. While other revenue spending falls, the service impact of this is expected to be positive, assuming that efficiencies do not negatively affect service delivery.

Evidence from elsewhere suggest that public spending on health is likely to be broadly progressive, i.e. it benefits those on lower incomes proportionally more than those on higher incomes. There is no clear evidence that the proposed increase in health expenditure in the MTFP addition would have any different impact to that observed elsewhere.

The picture is less clear in relation to public spending on education. However, the majority of the growth in spending on education is due to spending in secondary schools, which shows some evidence of being progressive elsewhere, and the proposed pupil premium – which is directly targeted at pupils from low income families.

The net increase in spending elsewhere is a combination of growth in some areas and service cuts in other areas. It is difficult to conclude on the distributional impact of many of the individual measures and harder still to conclude on the distributional impact of the package overall.

Measuring the distributional impact of capital expenditure presents potentially even greater challenges, as it is difficult to judge who benefits from spending which is mostly in support of service delivery rather than a service in itself. The MTFP includes significant capital expenditure on IT systems and for infrastructure and education. While there is evidence that the education spend (mostly on secondary provision) could be progressive, it is difficult to make any conclusions about the impact of the remaining expenditure.

## 1.1 Introduction

### 1.1.1 Expenditure changes considered

The measures considered in this section fall into four broad categories<sup>2</sup>:

*a. Revenue expenditure growth*

This includes £39m of proposed growth in health expenditure, £9m for education and £17m for other departments<sup>3</sup>, including contingencies.

*b. Revenue expenditure savings*

This includes over 180 reductions in expenditure, including 163 efficiency savings worth approximately £44m and 25 service reductions worth approximately £6m.

*c. Routine capital expenditure*

The capital programme for 2016-19 was set out in the MTFP adopted in October 2015, including approximately £60m for the Department for Infrastructure, £21m

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<sup>2</sup> This information was correct as at 1 June 2016.

<sup>3</sup> This excludes £0.8m of growth for the Social Security Department, which has been covered separately in section 2.

for the Chief Ministers Department (primarily IT expenditure), £20m for Education (including sport and culture) and £16m for Health.

*d. Major capital schemes*

This includes the sewage treatment works, Les Quennevais School, the new hospital, the office modernisation project and phase 6 of the prison improvement works. Expenditure has so far only been set out for Les Quennevais (£40m) and the prison improvement works (£8m).

The remainder of Section 1.1 looks at the principals involved in distributional analysis of public expenditure, plus some research from elsewhere. Section 1.2 considers the net impact on revenue expenditure – i.e. the revenue expenditure growth minus the revenue expenditure savings. Section 1.3 considers the net impact on capital expenditure – i.e. the routine capital programme plus the major projects.

### 1.1.2 Principles considered

The majority of government expenditure results in delivery of services which is provision of a benefit-in-kind rather than a direct cash payment. As a result, it is generally much harder to determine the distributional impact of any changes to the level of government expenditure than it might be to consider the impact of changes in taxation or cash benefits.

This leads to a number of issues/principles which need to be considered in attempting to undertake an analysis of distributional impacts:

*Willingness to pay*

The cost of providing goods and services to consumers will not necessarily be the same as the benefit which consumers get from the goods or services. This is a particular issue where goods are free at point of use – if no direct payment is required to use the service it is difficult to know what value users place on the service. To give an example, the cost of one year of schooling in the UK was estimated by the IFS at approximately £6k per pupil per year in 2010<sup>4</sup>, whereas the benefit to individuals from receiving school education is likely to be significantly greater - with one year of schooling estimated by UNESCO to increase lifetime earnings potential by up to 10%, among a number of other significant benefits<sup>5</sup>.

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<sup>4</sup> Institute for Fiscal Studies (2011) 'Trends in education and schools spending'.  
[www.ifs.org.uk/bns/bn121.pdf](http://www.ifs.org.uk/bns/bn121.pdf)

<sup>5</sup> United Nations Educational, Scientific and Cultural Organisation (2011) 'Education counts: towards the millennium development goals'.  
<http://unesdoc.unesco.org/images/0019/001902/190214e.pdf>

It is also possible that the cost of providing certain services might be greater than the benefit derived from users. This might be the case for example for some free prescriptions, where a number of individual users might receive medication which they would not have been prepared to pay the cost price for and which they may not use.

One possible solution to this discrepancy between cost price and benefit to the consumer is to measure users' willingness to pay for the goods and services, if they were chargeable, as this represents the value they place on the good or service. So, for example, a household may be willing to pay a certain amount per year to use public schools or medical care which is in practice free at the point of use. Willingness to pay for government services is particularly difficult to measure, however, as even a survey of users may not give accurate results if users have an incentive to overestimate the benefits – i.e. they know they will never need to pay the price they place on it but yet do value the service and therefore do not want to lose it.

Therefore, in the absence of reliable data on willingness to pay, this analysis has primarily been based on the cost of providing government goods and services, rather than the benefit of the goods and services to the user.

### Public goods

Public goods are defined as 'non-excludable' and 'non-rival', which means that they are available to use by anyone and one person's use does not prevent others from using the good. Due to these features, public goods are most often provided by government – as it would be difficult for commercial operators to be able to sell these goods. Public defence or protection of the environment are examples of public goods, as the entire population benefits from them, so it would not generally be possible to restrict consumption only to those who pay for the service.

Measuring the distributional impact of provision of public goods is particularly problematic. As they are available to the whole population, it is difficult to identify what value each individual household is deriving from it. As a result of this, the impact of public goods are often excluded from distributional analysis, for example the analysis which the UK Treasury undertake.

Jersey's government expenditure plans have not been separated into public goods and non-public goods. Therefore, all expenditure has generally been included in the assessment of distributional impacts. However, where any significant items of

expenditure are identified as potentially offering public goods, this will be considered as a potential caveat to the analysis.

### Impact of efficiency savings

The 2004 Gershon review of public sector efficiency in the UK<sup>6</sup> defined efficiency savings as processes and resource utilisation that achieve:

- Reduced numbers of inputs (e.g. people or assets), whilst maintaining the same level of service provision; or
- Lower prices for the resources needed to provide public services; or
- Additional outputs, such as enhanced quality or quantity of service, for the same level of inputs; or
- Improved ratios of output per unit cost of input; or
- Changing the balance between different outputs aimed at delivering a similar overall objective in a way which achieves a greater overall output for the same inputs (“allocative efficiency”).

The efficiency savings presented in the MTFP Addition fall into the first two categories – i.e. they are cash-releasing efficiency savings. These efficiency savings are designed by departments such that they will not impact on the level of quality of services provided by government and have been assumed to have no distributional impact. They have therefore been excluded from the analysis, though it is worth noting that there would be distributional impacts of any alternative measures to cut expenditure or increase revenues, so making the efficiency savings will have an impact – i.e. that of avoiding the distributional effects of alternative measures.

Similarly, outsourcing of services has also been assumed to have no impact on services.

### Administrative spending

While delivery of government services requires front-line staff, there is also an element of administrative spending which supports this. It is very difficult to make a judgment as to who benefits from this administrative spending. Administrative spending takes place both within service delivery departments and within central departments. For example, the finance function within the Department for Infrastructure will contribute towards and support the delivery of services, but so will the central human resources function within the Chief Minister’s Department.

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<sup>6</sup> Gershon (2004). Releasing resources to the front line, independent review of public sector efficiency. [http://www.hm-treasury.gov.uk/d/efficiency\\_review120704.pdf](http://www.hm-treasury.gov.uk/d/efficiency_review120704.pdf)

For the purpose of this report, administrative spending is assumed to have the same distributional impact as the majority of activity by the department within which the administrative spending takes place. For example, administrative spending in the Education Department is assumed to support the delivery of education in general and will have similar distributional impacts.

### 1.1.3 Research from elsewhere

Research from elsewhere suggests that the distributional impacts of government spending varies considerably depending on what area the funding is spent in:

**Spending on out-of-work and in-work benefits** are generally very progressive, i.e. those on low incomes benefit more (as a proportion of household income) than those on higher incomes. This is because the decisions around allocating such benefits generally mean that they are more easily available to those on low incomes. Jersey has similar methods for allocating these benefits, and the distributional impact of changes to welfare spending is covered separately.

Similarly, **expenditure on social and affordable housing** is generally considered to be highly progressive. This is again because social and affordable housing is most often allocated in a way which makes it easier for those on low incomes to access it as those on higher incomes are expected to be able to access housing through the private housing market. Jersey's Housing Gateway generally restricts affordable housing in Jersey to households with under £40k annual income. As a result, Jersey's Income Distribution Survey Report indicates that 84 per cent of households in the social-rented sector have income below the median level, compared to 54 per cent of those in the private rented sector, 49 per cent of owners without mortgages and 18 per cent of owners with mortgages. Expenditure on social housing is not included in the MTFP, as this investment is undertaken by social housing providers using funding awarded from the Housing Development Fund.

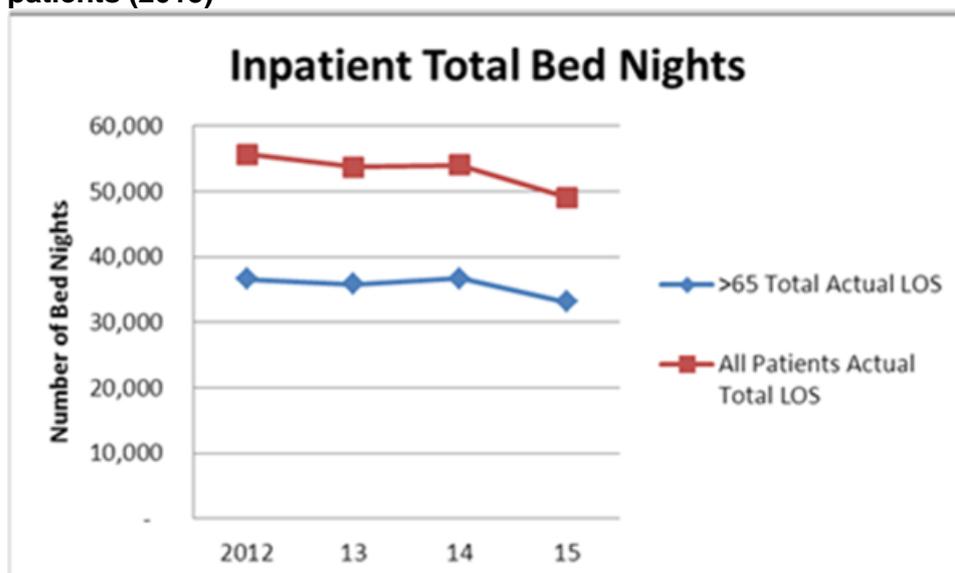
Research from other jurisdictions suggests the distributional impact of other areas of expenditure is much less clear. Two in particular are discussed in the remainder of this section: health and education.

There is a significant amount of literature on the distributional impacts of **spending on health**, including debate about the appropriateness of measuring health expenditure rather than health outcomes – those with lower incomes tend to have lower health levels and therefore a greater need for health spending but do not necessarily have greater health outcomes as a result.

However, the evidence does appear to suggest that those with greatest need for health expenditure tend to be in lower income groups, as there is a greater predominance of chronic diseases, acute illness and general poor health. On this basis, health expenditure is generally considered to be progressive.

Evidence from Jersey suggests that over 65s use a large proportion of hospital services, as defined by the number of bed nights. Of the total number of bed nights in 2015, 68% were for patients over 65 years of age.

**Figure 12: Number of inpatient bed nights / total length of stay for >65s and all patients (2015)**



Source: Health and Social Services Department

In turn, households with over 65s are much more likely to be in the lower income quintiles. 43% of pensioner households are in the lowest quintile group, with a further 28% in the second lowest quintile. This suggests that any service which primarily serves over 65s is likely to be used heavily by low income households. Almost one third of the lowest income quintile is made up of pensioner households. Therefore there is a strong likelihood that health care spending in Jersey is likely to be progressive.

The distributional impact of **education spending** tends to depend on what is being funded, with examples of education spending being progressive, proportional or regressive – depending on what is being funded.

In an education system with both 'free at point of use' and fee-paying schools (whether private or publically-owned), increasing expenditure in free at point of use education will generally tend to be progressive – because households with higher incomes will be more likely to use the fee-paying option. Evidence from the UK

suggested that investment in public education is likely to have quite significant distributional impacts – with a cut in spending from 6% of GDP to 5% thought to as much as double the dispersion of earnings<sup>7</sup>. This is because the quality of publically funded education will be reduced relative to privately funded education; which will increase the earnings differential between privately educated individuals (who tend to be from higher income households) and publically-educated individuals (who tend to be from lower income households).

The Jersey situation is somewhat different as some public education expenditure will go on fee-paying schools - more likely to benefit higher income households. As demonstrated in section 3 of the paper on user pays charges private education spending is a higher proportion of income for households in the top two quintiles. These households will benefit from increases in public expenditure on education which affect the fee-paying schools.

Education spending can sometimes be regressive, as some services will be primarily used by students from higher income households, for example due to lower university enrolment rates for lower income households.

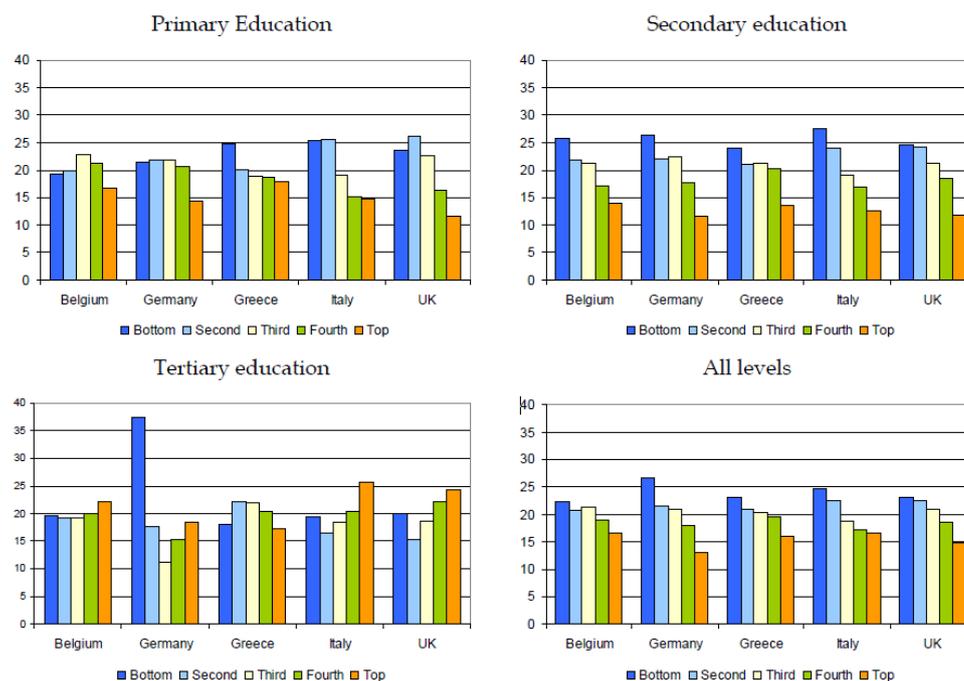
Research by the Institute for the Study of Labour (IZA) looked at the distributional impact of education spending in five European countries and found that it was largely progressive in all the countries considered<sup>8</sup>. However, while this was the case for secondary education in all countries, primary education was somewhat more proportional in some countries and progressive in others; while tertiary education was regressive in some countries. The IZA note that the tertiary figures are skewed for some countries due to students living away from their parental home during education – with generally a low household income at the time of study – this may make the actual picture more regressive or less progressive than would otherwise be the case.

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<sup>7</sup> National Institute of Economic and Social Research (1999). The distributional effects of education expenditures. <http://ner.sagepub.com/content/169/1/68>

<sup>8</sup> IZA (2009) The Distributional Impact of In Kind Public Benefits in European Countries. <ftp.iza.org/dp4581.pdf>

**Figure 13: Distribution of public education beneficiaries by quintile of household disposable income**



Source: EUROMOD

Notes: Quintile points are defined on the basis of equivalised household disposable income, allocated to individuals, using the modified OECD equivalence scale. Beneficiaries are individuals participating in the relevant level of education.

Source: Reproduced from IZA (2009)

The Institute of Fiscal Studies (IFS) have come to similar conclusions, finding research that suggests state school education in the UK is largely pro-poor, due to the tendency for higher income households to use more private schools, while tertiary education is more pro-rich<sup>9</sup>. However, the IFS go on to indicate that a purely private education system (with no public expenditure) would constrain social mobility, as lower income families will have access to less resources and may struggle to borrow privately against uncertain future returns, therefore missing out on the opportunities created by investment in education.

Overall, evidence from elsewhere suggests the distributional impact of any increase or decrease in education spending will depend on what area of spending is affected – e.g. if it is an increase in funding only to non fee-paying schools then it may be progressive; whereas if it is an increase in funding for university education then it may be regressive.

<sup>9</sup> Institute for Fiscal Studies (2010). The distributional impact of public spending in the UK. [www.ifs.org.uk/wps/wp1206.pdf](http://www.ifs.org.uk/wps/wp1206.pdf)

## 1.2 Revenue expenditure

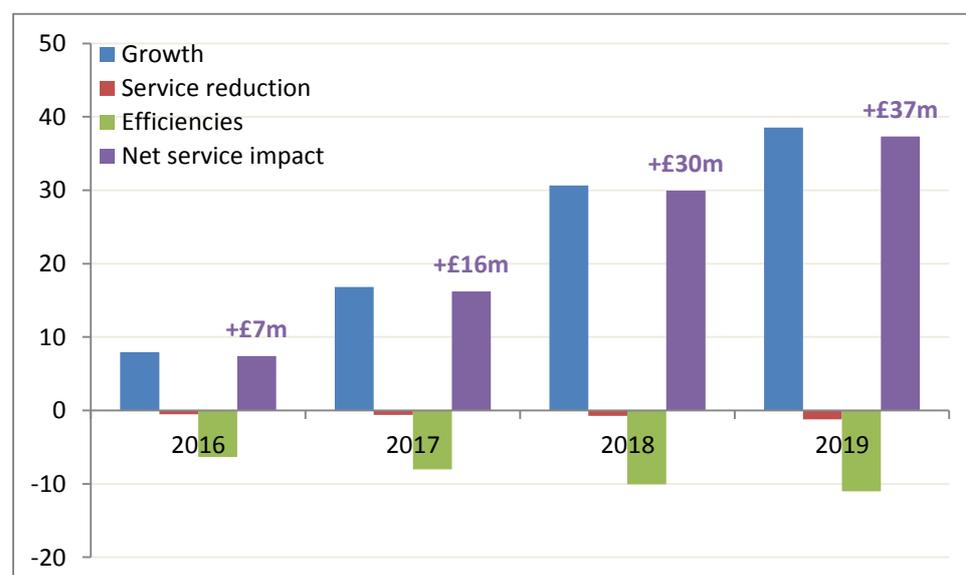
The distributional impact of government revenue expenditure is difficult to measure but based on the findings in section 1.1.3, the potential impacts have been looked at in three areas: net impact on health expenditure, net impact on education expenditure and net impact on other expenditure.

### 1.2.1 Health

The savings and expenditure proposals in the MTFP Addition are expected to result in a net increase in revenue expenditure by the Health and Social Services Department (HSSD) of £26m by 2019. This is the net result of growth bids totalling £39m, compared to £12m of budget cuts (numbers may not sum due to rounding).

However, as 8 shows, the cuts to the HSSD budget are primarily related to efficiency savings, with only £1m of the £12m coming from reductions to service provision. Therefore, on the basis of the assumption set out in section 1.1.2 that efficiencies have no impact on services, the net impact on service provision could be said to be a £37m increase.

**Figure 14: Net impact of changes to HSSD budget (£m)**



However, the impact of the £37m net increase in spending will not necessarily result in an additional £37m of benefit to be shared among users of the services affected. The benefit to users of individual components, and therefore the spending increase as a whole, may be greater or less than the cost of providing it. In the absence of evidence of the willingness to pay for these services, it is not possible to measure the benefit of the extra £37m. As per section 1.1.2, the distributional analysis therefore focuses on the cost of provision, rather than on the value of the service to the user.

Further, also as per section 1.1.2, this analysis looks at total spending by the Health and Social Services Department and may therefore include administrative spending, as well as spending on service delivery.

Subject to the three caveats above, the changes in health expenditure under the MTFP appear to have a net positive impact – i.e. the HSSD budget will increase significantly by 2019.

Section 1.1.3 demonstrates that health expenditure elsewhere is generally considered to be progressive; so in general terms a case could be made that the £37m increase in health expenditure is likely to be progressive, though this will depend somewhat on what the expenditure involves.

It is also possible to look in more detail at individual expenditure cuts and additional investment, in order to make a judgement about whether the distributional impact of specific measures might be different to the assumption for health expenditure overall. The main impact on net spending is from an additional £19m of expenditure due to the “2% investment in service standards and healthcare inflation” by 2019. There is no evidence to suggest the distributional impact of this would be any different to the distributional impact of health spending as a whole. Similarly, there is no clear evidence that the growth in expenditure for the Acute Service Strategy (£9m), out of hospital (£6m), services for children (£3m) and mental health (£1m) will have any different distributional impact.

None of the individual service cuts is expected to be worth more than £500k, so there is unlikely to be a significant distributional impact across the income distribution from any one individual cut.

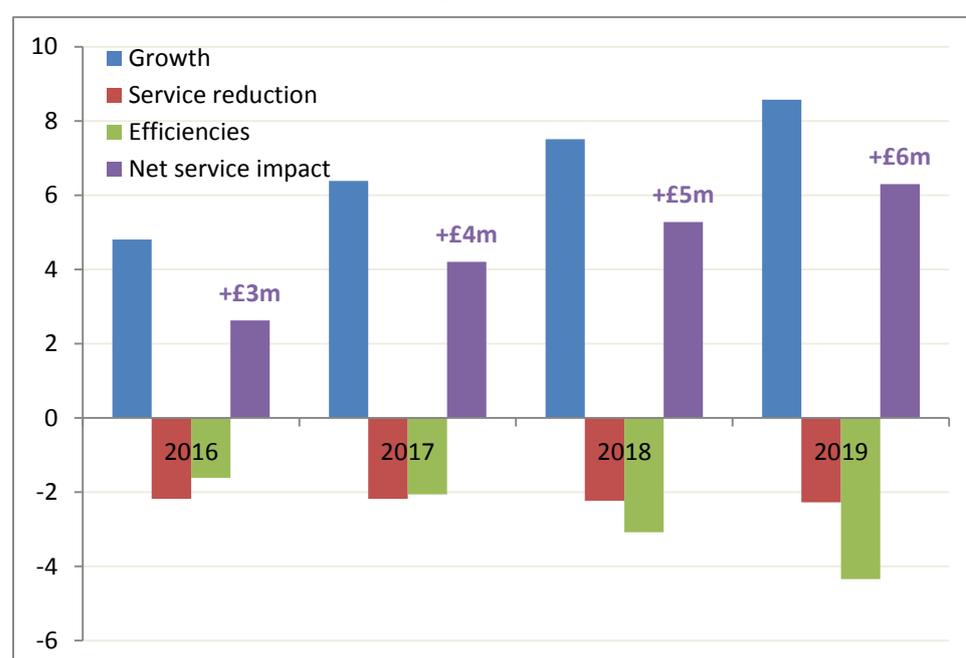
In summary, then, the net increase in expenditure on health is likely to have a progressive distributional impact overall – i.e. it will have a greater positive impact on households in the lower income quintiles, as a proportion of their income. This is because spending on health is generally considered to be progressive in other jurisdictions; and there is no evidence that any of the significant specific proposals in Jersey would have a different impact across the income distribution.

## 1.2.2 Education

The savings and expenditure proposals in the MTFP Addition are expected to result in a net increase in revenue expenditure by the Education Department of £2m by 2019. This is the net result of growth bids total £9m, compared to £7m of budget cuts.

However, as 9 shows, more than half of the projected cuts to the Education Department budget are efficiency savings. Therefore, on the basis of the assumption set out in section 1.1.2 that efficiencies have no impact on services, the net impact on service provision could be said to be a £6m increase.

**Figure 15: Net impact of changes to Education Department budget (£m)**



This £6m increase in investment in services will not necessarily result in £6m of additional benefit to service users. The benefit to users of individual components, and therefore the spending increase as a whole, may be greater or less than the cost of providing it. In the absence of evidence of the willingness to pay for these services, it is not possible to measure the benefit of the extra £6m; this issue is covered in more detail in section 1.1.2. Further, as set out in section 1.1.2, this analysis looks at total spending by the Education Department and may therefore include administrative spending, as well as spending on service delivery.

Evidence from elsewhere suggests that the distributional impact of education spending varies significantly, depending on what the funding is being spent on – with some types of spending tending to be progressive, some proportional and some regressive.

Section 1.1.3 indicates that secondary education elsewhere tends to be broadly progressive. Therefore a case could be made that the £1.6m expenditure on secondary school demographics is likely to be progressive, as is a proportion of the revenue consequences of capital programmes for both the ICT Skills Strategy (£0.8m) and for new schools (£0.5m). The distributional impact of spending to fund primary school demographics (additional £2.4m by 2019) may be more likely to be proportional.

The only significant new expenditure likely to have a significantly different distributional impact is the additional money for raising achievement through the Jersey Premium, which represents £2.5m by 2019. While a detailed distributional analysis of this has not been carried out for Jersey, the funding is intended to be available to schools based on the number of pupils they have who are from households with low income<sup>10</sup>, or who are looked after children. The expenditure is therefore likely to be progressive, though the distributional impact will depend on the extent to which it is effective in improving the educational outcomes for these pupils.

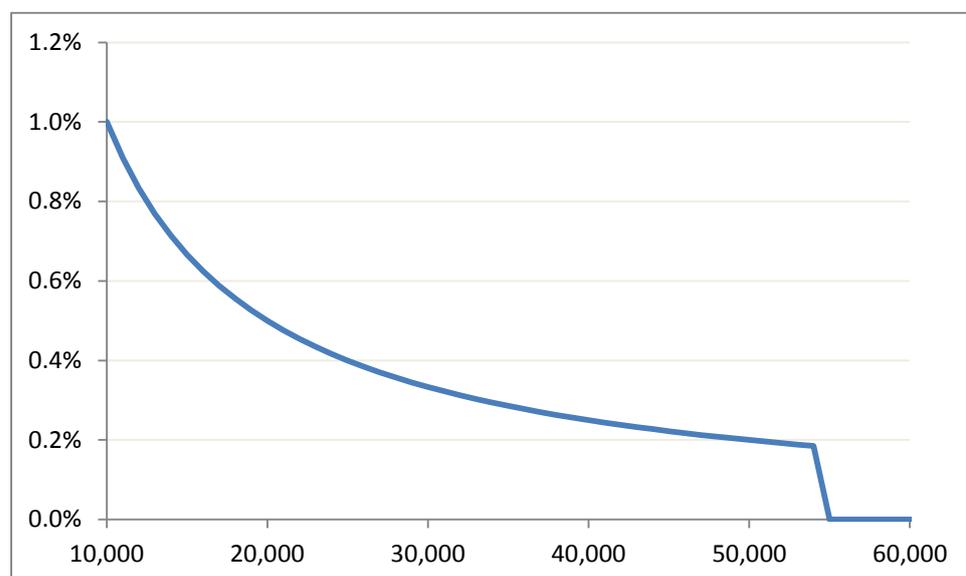
In terms of the budget cuts for Education, the majority of these are efficiencies which are assumed to have no distributional impact, as per the assumption set out in section 1.1.2. Of the cuts which will impact on services, the most significant is the £2m savings in higher education and skills as a result of reduced student numbers; a delay in increasing UK fees and a freeze on maintenance grants. The reduced student numbers and delay in increasing UK fees will not have any impact on the incomes of Jersey residents, but the freeze on maintenance grants will be regressive, as shown in Figure 16.

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<sup>10</sup> This is defined as pupils who live in a household that either receives income support or would be eligible for income support if they had lived in Jersey for five years or more.

### Figure 16: Impact of freezing student maintenance grants

Cost as % of household income, household with one university student studying off-island



The proposed change will cost approximately £100 per year extra for households with gross income below £54,000 and one university student studying off island. Freezing the maintenance grant will therefore be regressive, but is not likely to have a very significant impact on any households.

In summary, then, the net increase in expenditure on educational is likely to have a progressive distributional impact overall – i.e. it will have a greater positive impact on households in the lower income quintiles, as a proportion of their income. This is because the impact of the net increase of £2m (or £6m net increase in services) is likely to be very much swayed by the £2.5m for the proposed Jersey Premium, which will be targeted at those on lower incomes. While the freezing of maintenance grants will be somewhat regressive for those affected, this will have a much smaller impact.

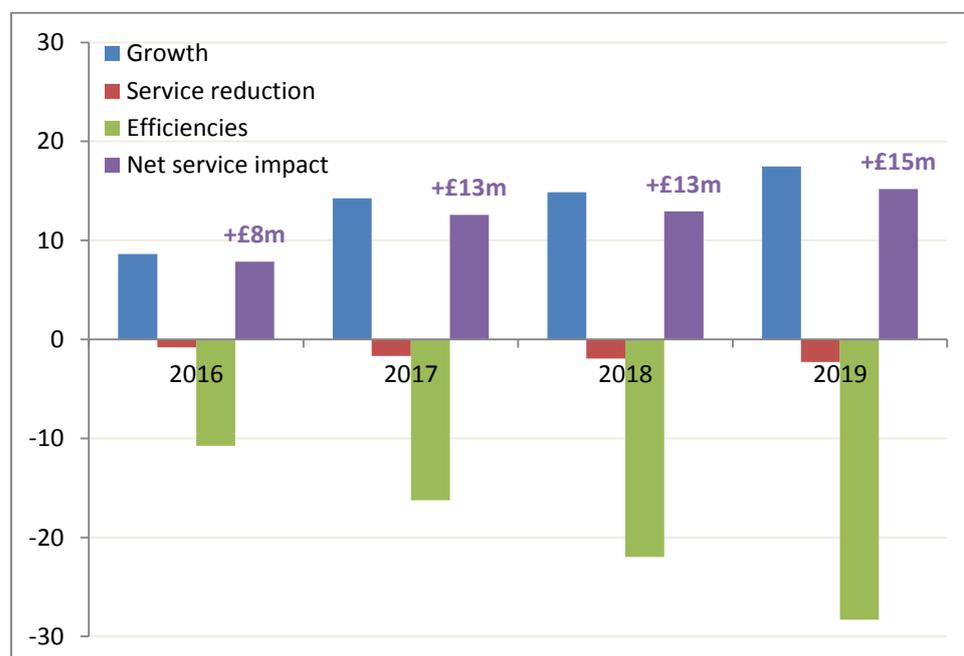
#### 1.2.3 Other revenue expenditure

The savings and expenditure proposals in the MTFP Addition are expected to result in a net decrease in revenue expenditure by all other departments of £12m by 2019 (excluding changes to the Social Security welfare budget, which are covered elsewhere in the paper, but including efficiency savings in the Social Security Department). This is the net result of growth bids totalling £17m, compared to £31m of budget cuts.

However, as Figure 17 shows, the vast majority of the expenditure cuts are efficiency savings. Therefore, on the basis of the assumption set out in section 1.1.2 that

efficiencies have no impact on services, the net impact on service provision could be said to be a £15m increase by 2019.

**Figure 17: Net impact of changes to other departments' budgets (£m)**



This £15m increase in investment in services will not necessarily result in £15m of additional benefit to service users. The benefit to users of individual components, and therefore the spending increase as a whole, may be greater or less than the cost of providing it. In the absence of evidence of the willingness to pay for these services, it is not possible to measure the benefit of the extra £16m; this issue is covered in more detail in section 1.1.2. Further, as per section 1.1.2, this analysis looks at total spending by all departments other than Health and Social Services and Education and may therefore include administrative spending, as well as spending on service delivery.

Overall, the evidence from elsewhere is mixed on the impact of public spending outside health, education, social housing and welfare. This requires looking at some of the significant individual components of the net growth in public spending.

The most significant growth in spending is £4m for additional property maintenance of Health and Social Services Department properties. While this is not direct service provision, it is likely that not maintaining these properties would have a detrimental effect on provision of health services and therefore a case could be made that this expenditure is progressive.

There is a further £3m of growth to fund a shortfall in Energy from Waste income, £0.8m to fund a shortfall in tipping fees, £0.5m from increased cost of insurance,

£0.3m to fund a shortfall in funding for the bus contract. There is no direct distributional impact of funding these shortfalls – if they were not funded through a growth bid it would require a reduction in expenditure elsewhere or an alternative income stream. The distributional impact of this would therefore depend on what the alternative mechanism might be to compensate for lower than expected revenues.

Almost £2m of growth has been proposed to fund the revenue consequences of capital investment in sewage treatment works. The impact of public provision of sanitation could be thought of in a number of ways:

1. Benefit of sanitation – in circumstances where no sanitation is provided there is often a greater impact on those on low incomes who tend to live in higher density housing and will therefore be more susceptible to disease due to living conditions.
2. Avoided cost of public provision - if no publically funded sanitation were provided, those in more remote locations might see a greater cost (as a proportion of their income) to put in place alternative measures. This will include many higher income families (25% of households outside St Helier are in the top income quintile, both before and after housing costs, compared to only 12% of the households in St Helier).

Contingencies are the only other lines of growth worth more than £1m, and the distributional impact of these will depend on how they are allocated. Other areas of growth include £0.9m for payment of rates on States properties (covered in more detail in the section on user pays charges), £0.5m for the implementation of the financial services policy framework, £0.5m for IT – none of which appear likely to have significant distributional impacts, plus £0.5m for the sports strategy. Given that spending on equipment for sports, camping and open air recreation increases as a proportion of household spending (until falling sharply in the top quintile), there could be some justification for saying that this spending is regressive – but this depends on whether the distribution of spending on sports equipment is in any way correlated with the distribution of the benefits from government spending on sport.

The majority of cuts in other departments are efficiencies, and the service impacting cuts are primarily small in value (less than £0.5m). However, some of the cuts may have significant impacts on individuals – particularly the £385k cut to Village Enhancement (Back to Work) schemes, the £340k cut to the energy plan delivery budget and grants budget, the £220k cut to the Community Policing Team and the restriction of concessionary fares to non-peak travel only. The distributional impacts of these will depend on how the cuts are targeted and managed.

### 1.3 Capital expenditure

The distributional impact of capital expenditure is more difficult to judge than revenue expenditure. Firstly, few capital projects are direct transfers – i.e. they are not assigned to a single household to consume. They are generally benefit-in-kind transfers and often public goods. Further, it is difficult to assess who benefits from capital expenditure as it is generally spent in support of a service (e.g. a hospital supports health care) rather than representing a service in itself.

While many analyses of distributional impacts leave capital expenditure out, for example the UK, an alternative approach would be to consider the impact of capital expenditure being a supporting role, allowing services to continue to be delivered.

Much of the public sector capital programme set out in the MTFP is based on maintaining or upgrading the existing asset base, for example repairing vehicles or replacing a school. The timing of capital expenditure is therefore not entirely at the discretion of decision makers – it may be led by the time at which repairs are needed, or the time when an asset is approaching the end of its useful life and therefore needs to be replaced to maintain service levels.

The capital programme set out in the MTFP includes approximately £60m for the Department for Infrastructure, £21m for the Chief Ministers Department (primarily IT expenditure), £20m for Education (including sport and culture which was in the Education Sport and Culture Department at the time of the MTFP) and £16m for Health<sup>11</sup>. In addition, there is some expenditure on the major capital programmes which includes the sewage treatment works, Les Quennevais School, the new hospital, the office modernisation project and phase 6 of the prison improvement works. Les Quennevais School and the prison improvement works are the only major capital programmes to which the MTFP allocated expenditure<sup>12</sup>.

#### 1.3.1 Chief Minister's Department

The capital spending by the Chief Minister's Department is primarily on IT systems. This could be considered to be 'administrative spend' and the assumption stated in section 1.1.2 is that the distributional impact of administrative spending is in line with the distributional impact of the Department's spending as a whole.

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<sup>11</sup> Capital expenditure is allocated in the annual budget, so the totals in the MTFP were indicative only.

<sup>12</sup> The MTFP stated that *"future amendments... will be brought forward for approval to facilitate the funding for the office consolidation project and a future hospital provision."*

In the case of the Chief Minister's Department IT spending, however, this is likely to support service delivery across the public sector as a whole. Therefore it could be assumed that the distributional impact of this is similar to the distributional impact of government spending as a whole. No analysis has been done of the distributional impact of existing expenditure so the impact of the proposed capital expenditure for IT is therefore unclear.

### 1.3.2 Department for Infrastructure

The £59m capital spending by the Department for Infrastructure is for replacement assets, infrastructure rolling vote, La Collette Cell Construction and infrastructure works backlog. Calculating the distributional impact of this spending is complex. There is some evidence that extra spending on infrastructure can improve equality (summarised by the IMF<sup>13</sup>). It will depend on the type of infrastructure being funded. The £59m Dfl capital spending is expected to be split as follows:

1. £12.5m for replacement assets;
2. £43.4m for the infrastructure rolling vote;
3. £1.7m for La Collette cell construction;
4. £1.8m for backlog infrastructure works.

Looking at transport infrastructure as an example, research from the United States<sup>14</sup> found that the bottom 90% of households spent a much greater proportion of their budgets on transport costs and concludes that "*infrastructure investments that can reduce the cost of transportation significantly - say, by providing public transit options or by repairing highways so that automobiles do not require as frequent repairs—will provide benefits that are progressively distributed*". However, research from the UK<sup>15</sup> suggests that cuts to transport expenditure will have a greater impact at the top end of the distribution (mainly because rail and road users tend to be particularly well off). The Institute of Fiscal Studies suggest that the impact is much more complex – as richer households tend to travel further by all modes except bus and foot or bike so subsidies to bus transport will benefit low income households whereas subsidies to rail benefit the rich<sup>16</sup>.

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<sup>13</sup> International Monetary Fund (2014). Redistribution, inequality, and growth. <https://www.imf.org/external/pubs/ft/sdn/2014/sdn1402.pdf>

<sup>14</sup> Economic Policy Institute (2014). Briefing Paper 374: The short- and long-term impact of infrastructure investments on employment and economic activity in the U.S. Economy <http://www.epi.org/files/2014/impact-of-infrastructure-investments.pdf>

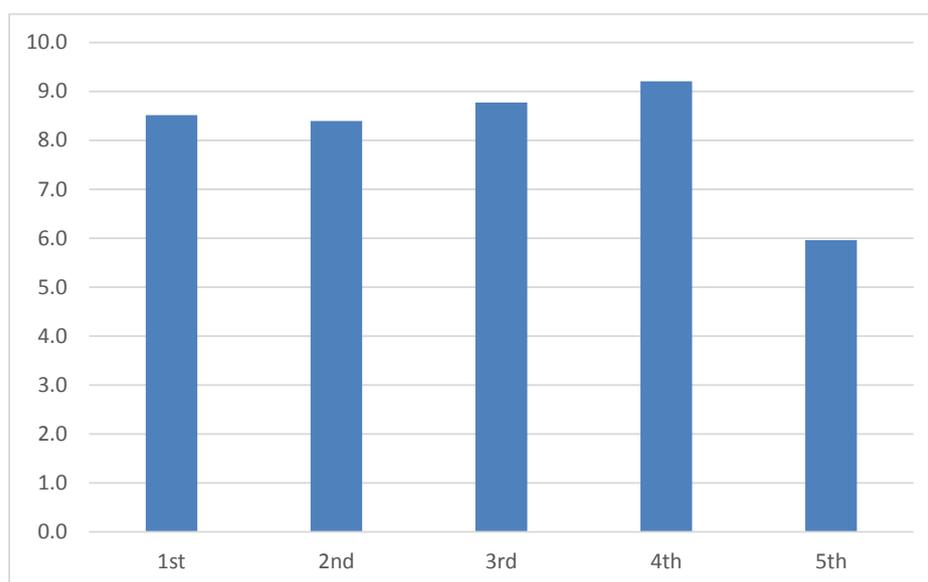
<sup>15</sup> Landman Economics (2016). The impact of planned cuts to public spending over the 2015-20 Parliament. <https://www.tuc.org.uk/sites/default/files/Spending-cuts-Report.pdf>

<sup>16</sup> Institute for Fiscal Studies (2010). The distributional impact of public spending in the UK. [www.ifs.org.uk/wps/wp1206.pdf](http://www.ifs.org.uk/wps/wp1206.pdf)

Spending patterns in Jersey suggest that each of the bottom four quintiles spend approximately 9% of their before housing income on local transport costs – i.e. purchase of vehicles, spares and accessories, petrol and diesel, repairs and servicing, parking, other motoring costs, bus and coach fares, taxi fares – but that there is a gradual increase between the bottom two quintiles and the next two. The top income quintile spends significantly less as a proportion of their income – 6%. If the benefit of public expenditure on roads is proportional to private expenditure on road-based transport, then the capital expenditure on roads could be considered to be mildly regressive for lower quintiles but progressive at the higher end of the income distribution. However, public expenditure on roads is much less likely to be a substitute for private expenditure than it may be in the case of health expenditure or education expenditure.

As explained in section 1.2.3, the distributional impact of spending on sanitation can be even more difficult to measure. This will depend on whether the distributional impact is based on the benefits from public provision (where those in higher density housing might see greater health benefits) or the avoided private costs resulting from public provision (where those in higher density housing may find it less expensive to provide sanitation privately).

**Figure 18: Spending on local transport (motoring and public transport)**  
% income before housing costs, by income quintile



### 1.3.3 Education

Capital expenditure on education is significant over the period, with £40m for Les Quennevais School, £10m for Grainville Phase 5, £5.5m for St Mary's School refurbishment, £3.5m for Jersey Heritage, and a further £1m for replacement assets

and minor capital. The bulk of this expenditure is on replacement/refurbishment of schools.

While the distributional impacts of spending on specific schools may vary according to the income of those enrolled and those in the catchment area, this level of detail is not required if this capital is assumed to be part of an ongoing programme of school refurbishment and renewal. Therefore, capital spend on secondary schools (which is over 80% of the proposed expenditure) is likely to be progressive, in line with spending on secondary education overall while spending on primary education (just under 10%) could be closer to proportional (see section 1.2.2).

A proportion of the expenditure on Granville Phase 5 relates to provision for Jersey Music Service. Section 4 of the paper on user pays charges shows that the Jersey Music Service is used by pupils attending a variety of schools, with a small underrepresentation from fee-paying schools (which tend to be used by higher income households). However, the proportion of the Grainville cost which relates to Jersey Music Service is likely to be a small part of the £60m Education capital programme overall.

#### 1.3.4 Other capital expenditure

The only other significant capital expenditure is on health and Community and Constitutional Affairs, related to replacing and upgrading existing assets. The £16m capital spend by the Health and Social Services Department could be assumed to have similar distributional impacts to spending on health overall – i.e. broadly progressive.

Spending on CCA projects includes £8m for prison improvement works as part of the major capital projects spend, £1.3m for minor capital and £500k for relocation of fire and rescue with the ambulance HQ. The bulk of this is the prison improvement works which falls under public order spending (i.e. including expenditure on the prison), for which the benefits to the population are twofold - benefits from avoided crime and benefits from a greater feeling of safety.

The Institute of Fiscal Studies show that while vandalism and vehicle-related theft in the UK are concentrated on higher income households, lower income households are more likely to be victims of burglary and violent crime. When looking at fear of crime, this seems to be more concentrated for less prosperous groups<sup>17</sup>. However, the interpretation of this data and what it means about the distributional impact of public

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<sup>17</sup> Institute for Fiscal Studies (2010). The distributional impact of public spending in the UK. [www.ifs.org.uk/wps/wp1206.pdf](http://www.ifs.org.uk/wps/wp1206.pdf)

expenditure depends on whether you assume that the benefits of expenditure fall to those with low risk or fear of being a victim of crime (as public order expenditure is most effective for them) or to those with a higher degree of risk or fear (as they are those most likely to be affected and benefit more from greater protection reducing that risk).

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## **Section 2: Distributional impact of the benefit changes**

### **Summary**

The benefit changes included in the MTFP were chosen with emphasis on ensuring that the benefit system is fair, encourages financial independence, is well targeted and changes are spread across large groups to minimise individual impact.

The benefit changes make up £9.5m of the overall measures, which is made up of £8.3m of Income Support changes by 2019 and £1.2m from targeting the Christmas bonus from 2016 onwards.

The Income Support changes affects about 6,500 households who are mainly towards the lower end of the income distribution. Overall, the changes are likely to be regressive.

The Income Support changes do not affect about 36,500 households who do not claim Income Support. These households range from the low end to the top end of the income distribution.

The previous Christmas bonus was a relatively small benefit paid to about 19,000 households (mainly pensioners) irrespective of income or wealth. Given the high proportion of pensioners in the bottom two quintiles this would appear to be a regressive change. However, replacing the previous Christmas bonus with a means-tested Christmas bonus, some of the potentially regressive impact will be offset, and vulnerable households at the lower end of the income distribution will not be affected. Likewise, some of the savings from making the Christmas bonus more targeted will be invested in the 65+ health scheme, which helps eligible pensioners towards the lower end of the income distribution with the cost of dental, optical and chiropody costs.

It is also important to consider what the impacts of the changes would be on different groups within those receiving income support and at the same points in the income distribution:

- Couples with children / existing pensioners will be less affected
- Single parents will be more affected

- The impact on other household types that receive income support will depend on their individual circumstances

Most households do not receive Income Support and will not be affected at all by these changes.

## **2.1. Introduction**

### **2.1.1 MTFP 2016-2019 benefit measures**

This section looks at the £10 million benefit measures included in the MTFP 2016-2019, as agreed by the States in 2015, including the proposed growth bids in the MTFP 2016-2019 Addendum. The benefit changes make up a relatively small part of the overall plan and overall, holds benefit spending broadly at its 2015 level by 2019. The net impact of all the benefit changes, including the proposed growth bids, is a reduction of £9.5 million by 2019.

### **2.1.2 Principles**

The benefit changes put forward by the Social Security Minister were carefully chosen to meet the following objectives:

- **Promote financial independence** – use changes in benefit to promote activities that will support the financial independence of claimants, and protect benefits which are supporting the financial independence of claimants;
- **Improve targeting of benefits** – change benefits in areas where public money is not specifically targeted to vulnerable groups. Consider the question “If this benefit did not exist, would we introduce it now?”;
- **Minimise impact on individuals** – spread changes over large groups of people, rather than a few individuals.

## **2.2 Summary of the benefits protected**

The Social Security Department provides a range of benefits not just from its tax funded cash limit (as provided by the Treasury) but also from three-ring fenced funds:

- The Social Security Fund (SSF) receives both Social Security contributions from working age people, their employers, and a tax-funded States grant. The SSF is used to pay the cost of old-age pensions and a variety of working age benefits.
- The Health Insurance Fund (HIF) receives Social Security contributions from working age people and their employers. It does not receive any funding from

tax-funded budgets. The HIF is used to pay a subsidy towards GP visits and meet the costs of dispensing community-prescribed drugs.

- The Long-term Care Fund (LTCF) receives both contributions from adults who pay income tax and a tax-funded States grant. The LTCF is used to provide financial support to adults who have long-term care needs.

The Department examined all areas of expenditure, regardless of the source of funding, before deciding which proposals to put before the States Assembly. No savings were proposed in respect of any of the benefits provided through these ring fenced funds. In particular:

**The old age pension has been protected.** The old age pension is a key element of the local benefit system. At the end of 2014, 17,500 pensioners living in Jersey received an old age pension, based on the number of years of contributions that they have made. In 2014, the States paid pensioners living in Jersey £131 million – an average of £146 per week per pensioner. The current full rate pension is £199.99 per week.

Old age pension rates are increased automatically each October. Since 2013, the uprating process has taken account of both the growth in earnings and the cost of living for pensioners.

**Support for primary care services will not be affected** – Health Insurance Fund benefits provide financial support for some primary care services such as GP consultations and prescriptions. In 2014, these benefits cost a total of £28 million.

**The long-term care scheme will not be affected.** This benefit, introduced in July 2014, supports individuals with the cost of long-term care, for example domestic care fees and care home fees. It is predominantly claimed by older people, with 82% of the claimants being aged 65 or above.

A number of tax funded budgets have also been protected. These include:

**Income Support – rental costs will be uprated:** Weekly Income Support payments help about 4,700 working age households and 1,800 pensioner households to maintain an acceptable standard of living. This costs £74 million a year. The Income Support benefit changes do not affect the support for rental costs, which make up nearly 40% of the weekly Income Support budget.

Implementation of the Housing Transformation Programme was a key strategic aim for the previous States Assembly. The agreed changes included rental increases for Andium and other social housing providers at 0.75% above RPI each year. These

increases will be fully reflected in the rental components available through Income Support.

**Cold weather payments and cold weather bonus have been protected:** These additional payments were introduced in 2008 and 2012 and help lower income households. The payments are well targeted as they cover income support households and pensioners with incomes too low to pay tax who may struggle with heating costs. The value of the payments is adjusted each year in line with the severity of the winter weather and the local cost of fuel.

**65+ health scheme has been protected:** This scheme supports lower income pensioners with the cost of dental, optical and chiropody costs, and covers both check-ups and treatment. It is available to locally resident pensioners with incomes too low to pay income tax. The scheme is well targeted to help pensioners maintain their independence by helping with vital areas of personal health spending. Both the cold weather scheme and the 65+ health scheme provide funding to meet specific needs, which may be difficult to plan for.

**Increase funding for the 65+ health scheme:** The benefit proposals put forward by the Social Security Department include an extension of the 65+ health scheme, with an allocation of an additional £200,000 from 2016 onwards. This will give more help to pensioners to maintain their independence.

The use of the additional funding has been reviewed and discussed with stakeholders, including pensioner and healthcare groups. Draft Regulations have been lodged that will change the claim process – removing the need for customers to pay upfront by ensuring payments can be made to practitioners on behalf of customers. The same range of healthcare services will be covered and the scheme will essentially be targeted at the same cohort of lower-income pensioners. The level of payments made via the scheme will be reviewed later in 2016.

**Housing adaptation grants will not be affected:** These help homeowners, private tenants and housing trust tenants with the cost of adaptations to their home to help them to continue to live independently where they have particular physical needs. A similar scheme is provided separately by Andium for their tenants.

## **2.3 Distributional impact of the agreed benefit changes**

### **2.3.1 Introduction**

This section describes the estimated impact of the benefit changes on different households, and how this varies by income level, considering the income distribution of Jersey's population.

In order to do this, two scenarios are compared to each other. The first scenario includes all the MTFP 2 benefit changes, whilst the second scenario includes a benefit system without the MTFP 2 benefit changes, and instead continues with unchanged benefit policy. Unchanged benefit policy means, for example, providing an annual uprate for Income Support in each year 2016-2019.

The findings in this section should be put in the context of the whole MTFP 2 and its expected impact on households, including those that claim Income Support, while they claim it.

### 2.3.2 Summary of the benefit changes

The proposals for benefits changes and their contributions to the £10 million target by 2019 are summarised in the following table:

**Figure 19: Summary of the benefit changes**

Benefit changes	2016 £m	2017 £m	2018 £m	2019 £m
Maintain most income support component rates at 2015 levels for two years (increase rental and childcare cost components)	2.0	3.9	4.0	4.1
One off changes:				
Close the Christmas Bonus after it has been paid in 2015 and improve the 65+ Health Scheme*	1.3	1.4	1.5	1.6
Remove LTIA / Invalidity / Survivors Benefit disregards	0.6	0.6	0.6	0.6
Limit eligibility for jobseekers under 25	0.2	0.2	0.2	0.2
Change more emergency grants to loans (and close RADS)	0.1	0.2	0.2	0.2
Limit growth of the TV licence benefit **	0.1	0.1	0.1	0.1
Phased changes to Income Support, including removal of single parent component, introduction of percentage pension disregard and net improvements in incentives	0.8	1.7	2.8	3.2
<b>TOTAL</b>	<b>5.1</b>	<b>8.1</b>	<b>9.4</b>	<b>10.0</b>

\* The MTFP 2016-2019 Addition includes additional funding for the targeted Christmas Bonus scheme, reducing the annual savings in this area by £0.5m

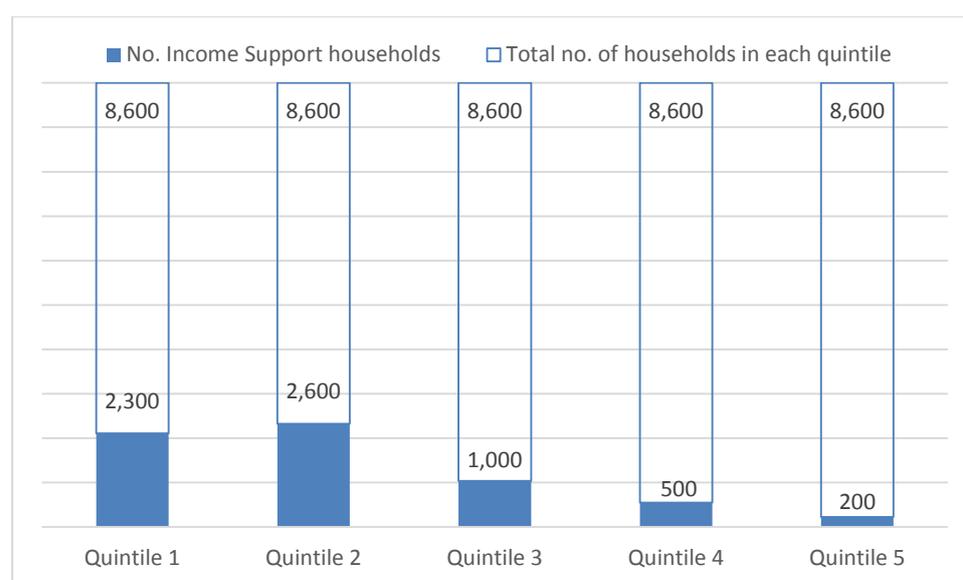
\*\* Note that the States Assembly did not approve limiting the growth of the TV licence benefit, and so this is not examined any further.

### 2.3.3 Households affected by the Income Support benefit changes – by income

The Income Distribution Survey 2014/2015 includes information about the amount of Income Support benefit the households in the sample claimed, as well as their total household income. The majority of households surveyed that claim Income Support have household incomes, after adjusting for their household size, that are in the lowest two income quintiles, both before and after housing costs (76% before housing costs, 83% after housing costs).

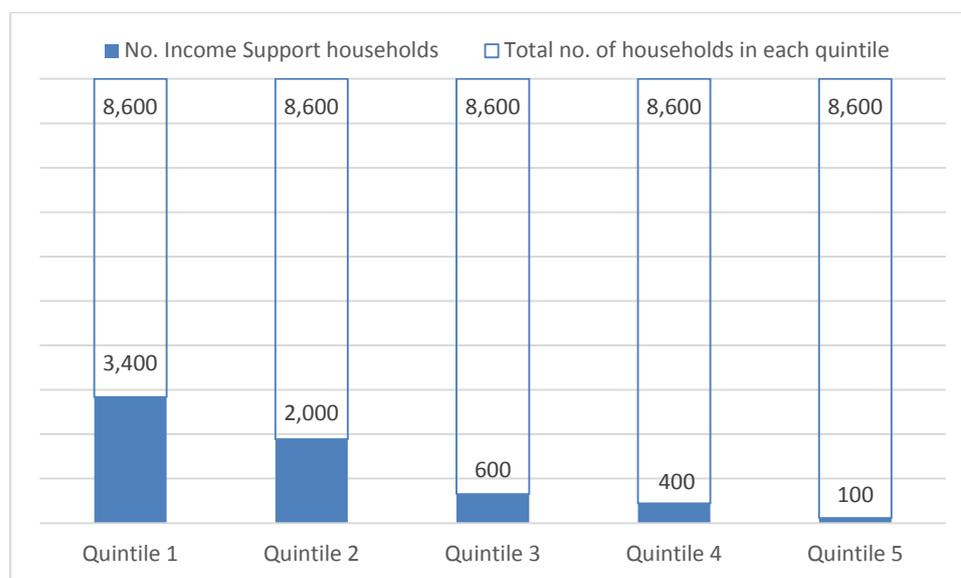
The charts below provide a rough guide to the total numbers of households claiming Income Support in each income quintile, by scaling up the results of the Survey. It is useful to understand the overall distribution, but it should be noted that this analysis is based on a sample of households, and there are differences in the way that Income Support and the Survey defines a household. As such it should be treated with some caution.

**Figure 20: Estimated number of households claiming Income Support in each quintile - before housing costs**



Source: 2014/15 Income Distribution Survey.

**Figure 21: Estimated number of households claiming Income Support in each quintile - after housing costs**



Source: 2014/15 Income Distribution Survey.

A small proportion of the households that had an Income Support payment were recorded as being in the top income quintile in the Income Distribution Survey.

These households will include:

1. Some households that receive the Child Personal Care benefit, which is categorised as Income Support, although it is not means-tested. This benefit helps households that have a child with a high level of long term illness or disability, regardless of the level of household income.
2. Households that include a young adult with a disability claiming Income Support, whilst still living in the family home. The income distribution survey has a broader definition of a household than that used for income support. The young adult is treated as a separate household for income support purposes, but the young adult is included with his/her parents for the Income distribution purposes. Depending on the income level of the parents the household could be in the upper income quintiles.
3. Some households are only in receipt of Income Support for a short period due to a significant and sudden change in circumstances. The income survey looks at annual income whereas income support provides for immediate needs.

There are also households in the higher income quintiles receiving Income Support benefit to help with the personal care costs of an adult, or the costs of child care, for example. These benefit payments increase the total household income of these

households, moving them up the income distribution, although the extra Income Support benefit will go towards meeting these extra costs.

**The Income Support benefit changes will affect households that claim Income Support benefit, while they claim it, and they will generally have low household incomes. The majority will have household incomes putting them in the lowest two income quintiles.**

**The Income Support benefit changes will not affect an estimated 36,500 households that do not claim Income Support. This includes about 12,000 households that are in the lowest two income quintiles who do not receive Income Support.**

#### **2.3.4 Households affected by the Income Support benefit changes – by type**

Income Support is provided to households in a variety of different circumstances, and is focused on households who have low incomes and low capital assets. Income Support is available to households in which at least one adult meets the residence test of at least five years, and every adult under 65 must meet a work test either by being in full-time work or being included in an exempt category.

The following table compares data on Income Support households in 2014 with the estimated population for 2014 by household type. The proportion of Income Support households in the total population is an estimate, given that two different sources of data are being compared and that there are slightly different definitions of households being used in each source.

The most common household types that tend to claim Income Support are single working age adults (including many who have a long term illness or disability) (2,300) and single pensioners (1,400), followed by single parents (1,100) and couple parents (890).

The majority (79%) of single parent households in Jersey claim Income Support compared to 28% of single adults and 27% of single pensioners.

Some of these households will include people with a long term illness or disability.

**Figure 22: Breakdown of households claiming Income Support and all Jersey households at the end of 2014**

<b>Household type</b>	<b>Income Support</b>	<b>Estimated total</b>	<b>Estimated % of total</b>
Pensioner single	1,400	5,200	27%
Pensioner couple	360	9,650	4%
Single adult	2,300	8,130	28%
Two adults	320	4,750	7%
One adult and one or more children	1,100	1,400	79%
Two adults and one or more children	890	6,770	13%
Three or more adults	120	7,210	2%
	<u>6,500</u>	<u>43,100</u>	15%

Note does not sum due to rounding

As noted above, there are significant differences between the definitions of household under Income support compared to that used in other surveys. In particular, Income support allows for separate claims to be made from adults who remain living in a family setting – for example if the adult is under 25 and has a disability, or is aged 25 or above. This will overstate the number of single adult households receiving income support.

**The Income Support benefit changes will affect all these households claiming Income Support to some extent. The impacts will be different for each household because some of the changes affect certain household types and not others.**

The following table summarises the different households affected by each benefit changes. The rest of this section provides more detail on the impacts outlined in the next table.

**Figure 23: Summary of how the changes impact different households**

Changes	Households affected
<b>Income Support</b>	
Maintain most component rates at current levels until October 2017 (increase rental and childcare cost components)	All IS households (About 11,700 people in 6,500 households).
Phase out the single parent component (£40 a week by 2019)	Single parent IS households (1,100).
Simplify the treatment of income	Existing OAPs receive higher of fixed value disregard or % disregard. Future OAP claims will receive % disregard.  Single parents with maintenance income will see an improved maintenance income disregard (about 650 households).  Approximately 1,100 individuals also claim another benefit alongside Income Support and will no longer receive an extra disregard.
Jobseekers under 25 change	75 young jobseekers will no longer qualify for Income Support.
One-off payments as loans rather than grants	Approximately 40 claims a month.
<b>Other benefits</b>	
Replace the Christmas Bonus scheme after it has been paid at the end of 2015 with a targeted scheme.	Approximately 15,000 individuals will no longer receive a payment of £85. Income support claimants who are over 65, disabled or providing unpaid care will continue to receive the payment, as will other pensioners who do not pay tax and have limited assets.
Improve the 65+ Health scheme for low income pensioners	2,400 low income pensioners currently registered, uptake planned to increase.
Close RADS to new entrants	Less than 5 new claims per year.

### 2.3.5 Maintain most Income Support components for two years

*Maintain most Income Support component rates at 2015 levels until October 2017.*

*Rental components and childcare components will be increased each year.*

Key theme: Minimise the impact on individuals – spread changes over large groups of people rather than a few individuals.

The household, adult, child, impairment and carer's components will be maintained at their 2015 values until October 2017. Maintaining these component values will save £4.1 million a year by 2019 compared to the cost of uprating them in line with

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inflation. By holding these components steady, a substantial saving in the overall budget is achieved, whilst reducing the impact on individual households.

Even though the maximum amount of Income Support a household can claim will now increase much more slowly, households that claim Income Support will have the opportunity to increase their total income by increasing their own household income, for example through earnings.

The accommodation and childcare components of Income Support will be increased each year.

The increase in the accommodation component each year will ensure that households' benefits adjust to take full account of any social rent increase. The increase in the child care component each year will make sure that parents can afford the cost of child care when they return to work. This helps families move towards financial independence.

There are about 6,500 households that claim Income Support, and over the next four years many households will stop claiming Income Support as their circumstances change, whilst others start a new claim. The impact of this change will be shared across all these households.

As most types of household income (earnings, pension and maintenance payments) are subject to a percentage disregard in the Income Support calculation, an increase in any of these types of income will result in a higher overall household income even whilst components remain at a fixed level.

The impact on households will depend on their circumstances and the Income Support components they are eligible to receive. Generally speaking, the less income the household has and the more Income Support they claim, the more this change will have an impact on them as a proportion of their total household income. This suggests this change is regressive across households that claim Income Support. However, this option should be considered in context of alternative measures to achieve the same level of savings. These are likely to have led to a more serious detrimental impact on other specific household types.

### 2.3.6 Phase out the single parent component by 2019 and improve the maintenance income disregard

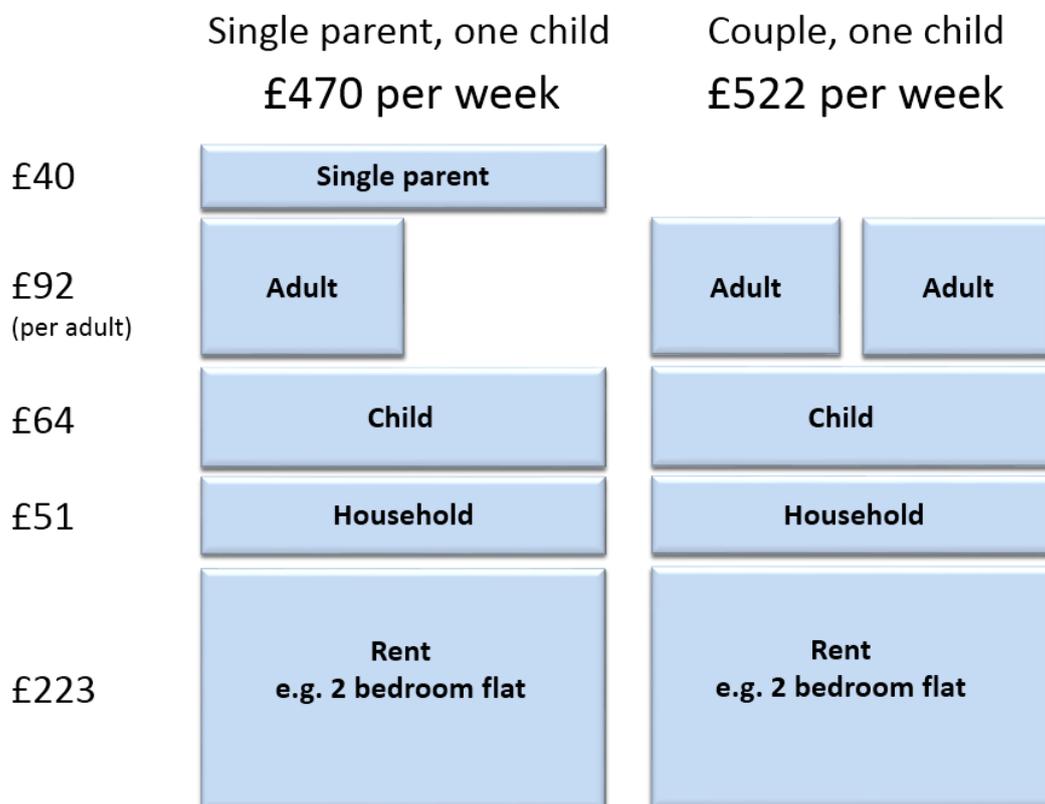
Key theme: Improve the targeting of benefits

Phasing out the single parent component (£40.39 a week) by 2019 will equalise the treatment of a single parent with other adults in the Income Support system, to create a fairer overall system. The single parent component can also act as a barrier to another adult joining the household as a partner.

The extra component for single parents was not available to new Income Support claimants from November 2015.

The diagram below compares the weekly components that are included in a typical Income Support claim, for a single parent with one child and a couple with one child. The single parent receives an additional component of £40.39 per week but, given that a separate component is available for each child, the extra payment made to the single parent is not linked to any specific, additional household cost that a single parent would face. For simplicity, this diagram does not show the effect of household income and is rounded to the nearest pound.

**Figure 24: How an Income Support claim was made up before the changes. The single parent component is now being phased out over the next three years.**



Separately, providing fair and simple rules for the treatment of income will provide a greater incentive for single parents to enter into maintenance agreements and collect maintenance income. Income Support already requires that single parents pursue maintenance, and so this policy is further supported by an increase in the disregard of maintenance income from 10% to 23%, in line with the treatment of earned income.

- *Impact of the change on households*

The maximum amount of Income Support benefit a single parent can claim will be £40 per week lower than it would otherwise have been by 2019.

There are about 1,100 single parent households claiming Income Support at any one time that will be affected by this change. Most of these households will not experience the full transition – over this period many parents will no longer need Income Support, for example, when a parent returns to full-time work as their child gets older. In other cases, the household composition will change as the single parent moves into a new long-term relationship. Analysis of Income Support claims shows that half of all single parent Income Support claims last less than 20 months.

Just under half of the single parents who claim Income Support receive maintenance income, typically ranging from £10 a week to £100 a week. Increasing the maintenance income disregard from 10% to 23% will mean that the single parent will keep a higher proportion of the maintenance payment that they receive. For example, if a single parent has £45 per week maintenance income (the average), the higher 23% disregard will mean that their total income will increase by almost £6 per week compared to the current rules.

### **2.3.7 Simplify the treatment of income under Income Support rules**

Key theme: Promote financial independence
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Prior to January 2016, the Income Support system included a variety of different income treatments. These added complexity to the operation of the scheme and did not give a consistent message to claimants to help them to move towards financial independence. This table shows the six main treatments of weekly income (figures rounded to the nearest pound).

Type of income	Current disregard	For £100 of income the household will keep an extra:	For £200 of income the household will keep an extra:
Earnings	23%	£23	£46
Pension	Fixed amount	£55	£55
Maintenance	10%	£10	£20
Short term incapacity allowance (STIA - sickness benefit), maternity allowance	None	£0	£0
Long term incapacity allowance (LTIA), invalidity benefit and pension income received by working age people	6%	£6	£12
Investment income (interest, dividends etc) (See point 3 below)	100%	£100	£200

Note: There are also extra rules for the earned income of single parents.

The Income Support benefit changes have simplified the treatment of income as follows:

1. **Income that helps the household towards financial independence is subject to a 23% disregard.** This includes: earnings; pension income for those over pension age; and maintenance income. This means that for every extra £100 of income received, a household claiming Income Support will be £23 better off. This provides an incentive to earn and tapers the reduction in benefit that occurs when earnings gradually increase. These households have a strong incentive to move towards financial independence whilst claiming Income Support, and in the case of working adults to work to provide a larger pension.
2. **Other income is subject to a pound for pound reduction in the amount of Income Support received.** This mainly comprises income from other benefits that the claimant is receiving. **The receipt of these other benefits does not encourage the claimant to move towards financial independence and there is no justification to award an additional disregard.**
3. **Income received from capital assets (e.g. interest received from a savings account) - there is no change.** This income is not included in the Income Support claim, i.e. it has a 100% disregard. Instead, the value of the assets themselves are taken into account and a generous level of assets is allowed before there is any impact on the benefit payable. For example, a pensioner couple can hold savings of over £22,000 before they see any reduction in their weekly Income Support benefit. Holding a reasonable

amount of capital assets provides a household with a level of financial stability, which allows them to meet unexpected costs and helps to maintain financial independence.

These changes are an important part of the whole package of measures that will treat claimants fairly, improve the operation of Income Support and incentivise desirable working and savings behaviour in the future.

The changes lead to the following simple structure:

<b>Type of income</b>	<b>Proposed disregard</b>	<b>For £100 of income the household will keep an extra:</b>	<b>For £200 of income the household will keep an extra:</b>
Earned income, pension income, maintenance income	23%	£23	£46
All other income including short term incapacity allowance (sickness benefit), maternity allowance, long term incapacity allowance, invalidity benefit and pension income received by working age people	None	£0	£0
Investment income (interest, dividends etc)	100%	£100	£200

The details of these changes are explained below.

### **2.3.8 Changing the pension income disregards for new pensioners**

*Treatment of pension income - gradually replace the fixed value pension allowance with a percentage allowance*

The fixed pension income disregard of £55.23 for a single person (£91.00 for a couple) has been replaced by a 23% income disregard for new claims.

This means that a working age person who has made more provision for pension income in old age (for example, by paying into a pension scheme) will have a higher total household income if they should reach pension age and need to claim Income Support.

This change has not affected current pensioners who claimed Income Support before 1 January 2016 as they will not have had the opportunity to increase their pension income. The existing flat rate disregards will be maintained at the current level for this group, to protect their existing household income. However, this group does benefit from the 23% percentage disregard if this results in a higher total benefit amount - in other words from January 2016 they are eligible to receive whichever is the higher of the fixed amount or the percentage amount.

Pensioners who claim Income Support for the first time from 1 January 2016 will receive the new 23% income disregard. Based on recent trends, roughly 200 people will start to receive the new pension disregard in 2016.

In the absence of any change in behaviour to increase income, new pensioner households with less than £240 a week pension income for a single person (£395 a week for a couple) will have a lower household income than they would have done without the benefit changes. New pensioner households with pension income above these amounts will have a higher household income than they would have done without the benefit changes.

### **2.3.9 Remove the income disregard for contributory benefits and pension income received by people below pension age**

The disregards that are applied to some types of contributory benefit and pension income received by working age people have been removed from 1 January 2016.

Previously, a disregard of 6p in the pound was applied to income received from Long-Term Incapacity Allowance, Invalidity Benefit and Survivor's Pension. However, claimants receiving other benefits such as Short Term Incapacity Allowance or Maternity Allowance were not entitled to this disregard.

The maximum standard rate of benefit for a single working age person was £196.42 per week in 2015 and the 6% disregard, for those who qualified, was worth up to £11.79 per week.

This change brings the treatment of all contributory benefits in line. The full value of the contributory benefit received will be included as a form of income in the Income Support calculation. This makes good sense because there is no reason to include a disregard, in effect paying people twice, if they receive one of these benefits whilst claiming Income Support.

People in low-income households with a disability or a long-term medical condition are already able to receive additional support through the separate impairment component of Income Support. This component offers extra financial assistance to people who have personal care needs, mobility needs and/or costs incurred by the need for additional visits to their doctor.

For people with a lower level of incapacity, where working part-time or full-time is a realistic expectation, the full range of 'Back to Work' services are available, supporting people to move towards and into employment to improve their financial independence.

Back to Work services are available to entitled claimants up to the age of 65. Claimants are encouraged to look for appropriate work, even if they are already in receipt of some pension income before they reach the state pension age.

Every Income Support claimant of any age who has a part-time or full-time job will benefit from the 23% disregard of earned income, and will be better off by 23p for every extra £1 earned, after their benefit has been adjusted.

### 2.3.10 Jobseekers under 25 change

Key theme: Improve the targeting of benefits

*Include most jobseekers aged under 25 still living at home in their parents' household for Income Support purposes*

This small change includes 19-24 year old jobseekers in the family Income Support claim, if they have one.

This has resulted in a reduction of benefit of £92.12 a week for about 75 19-24 year old jobseekers whose families already have sufficient income that they would not qualify for Income Support when considered as a household. These households are more likely to be in the top three income quintiles.

55 jobseekers aged 19-24 moved to their parents' Income Support claim and altogether they were not made better or worse off.

Jobseekers in this age bracket still continue to receive full, tailored support through Back to Work, regardless of whether or not they qualify for Income Support. A young person with a disability<sup>18</sup> or who is living independently, for example, a care leaver, will continue to have their own claim and will not be affected by this change.

The position at the end of December 2015 of those claimants aged under-25 who were Actively Seeking Work (ASW) and had their own Income Support claim in July 2015 was as follows:

Category	% of total
Employed	40%
Actively Seeking Work	39%
Turned down support from Back to Work	9%
JET	5%
Full time education	3%
Other	3%

(Table does not equal 100% due to rounding.)

<sup>18</sup> Claiming personal care level 2 or 3 of the Income Support impairment component.

### **2.3.11 Provide some Income Support special payments through loans rather than grants**

Key theme: Promote financial independence

*One – off payments - provide loans for white goods, furniture and fittings rather than grants*

In the past, Income Support households have been able to apply for help to cover one-off payments for buying and replacing white goods (like fridges and cookers), essential furniture and other fittings (like carpets). This help has usually been in the form of a grant.

Now, Income Support households will apply for an interest-free loan from the Social Security Department to help cover these costs. These loans are repaid by making a small reduction in the household's ongoing weekly Income Support benefit.

This facility is very useful for households with low incomes who might not have the savings to deal with the cost of a move or something breaking unexpectedly.

Offering a loan, rather than a grant, is a more cost effective way of providing this service. It is vital that loans should be available so that households, often including children, have appropriate living conditions. At the same time, the household gains an appreciation of the cost of the item and the need to budget for this type of expense.

### **2.3.12 Estimated impact of the Christmas Bonus and 65+ health scheme change**

Key theme: Improve the targeting of benefits

One of the major financial pressures facing the States is the level of extra public spending associated with the growth in the number of people aged 65 and above, which is set to rise steeply – by about 75% - between 2015 and 2035.

For pensioners with lower incomes, targeting government help to meet specific needs is more effective than a benefit that helps with regular expenditure that can be more easily budgeted for. Furthermore, it is difficult to justify paying a benefit such as Christmas Bonus to large numbers of wealthier households when it is clear that the needs of low income pensioners will increase significantly in the future.

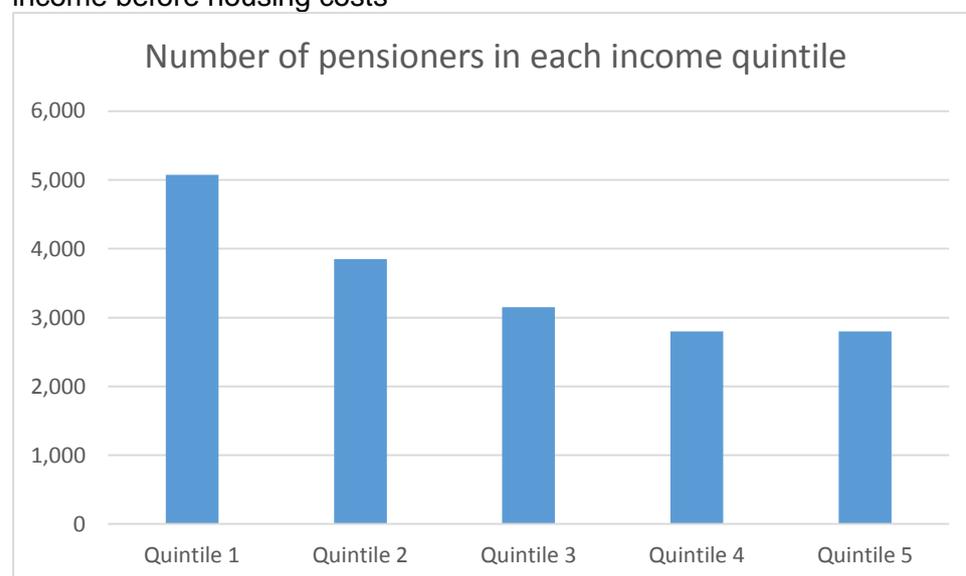
The previous Christmas Bonus was paid to 17,500 pensioners (of which about 2,000 qualify for Income Support) and 1,700 working age individuals. The Christmas Bonus was not means tested, or targeted, and cost over £1.5 million in 2014. Of the

£1.5 million total cost, £1.3 million was paid to 15,500 pensioners each year who have a regular income and savings that can support more than just basic living costs.

This is one of the smallest benefit changes on a per person basis, equivalent to a loss of £1.60 per week. The replacement targeted scheme protects vulnerable low income households from this loss. As such this is a small progressive change to the benefit system.

The following chart shows that around half of pensioners are in households that are in the lowest two income quintiles (before housing costs) with the other half being in households that are in the top three income quintiles. Replacing the Christmas bonus with a more targeted bonus for vulnerable low income households will impact mainly on the top three income quintiles.

**Figure 25: Estimated number of pensioners in each income quintile income before housing costs**



The extension of the 65+ health scheme with an extra £200,000 funding each year will give more help to pensioners with low incomes to maintain their independence by helping to pay for dental, optical and chiropody costs. This will primarily help pensioner households that are in the lowest income quintiles.

### 2.3.13 Childcare costs for recently arrived parents

*Close the Recently Arrived Discount Scheme to new entrants at the end of 2015*

Key theme: Improve the targeting of benefits

The Recent Arrivals Discount Scheme (RADS) was a childcare benefit designed to help recently arrived parents who do not qualify for Income Support to support their childcare costs whilst they are at work. It was specifically aimed at parents who did

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not satisfy the residency condition for Income Support as they have lived in Jersey for less than five years.

The scheme has had very limited take-up and existing claimants will continue to be supported until they have lived in Jersey for five years and can claim Income Support, if they still need it. This benefit was closed to new entrants from the end of 2015.

### **2.3.14 Growth bid to fund the Child Personal Care Benefit**

In September 2014 the States Assembly agreed to introduce a new benefit whereby parents of children who meet the requirements for the highest levels of the impairment award can receive a payment in respect of the child, independent of parental income. The MTFP Addendum includes a growth bid to fund this benefit until 2019.

Funding this benefit provides help to a relatively small number of households that would not otherwise qualify for Income Support. These households are more likely to be in the top half of the income distribution, because they do not qualify for Income Support.

### **Section 3: Distributional impact of user pays charges**

This section looks at the distributional impact of the user pays charges proposed in the MTFP. User pays charges covers a range of potential charges where the user of the public services is charged at the point of use (rather than for example paying for the service through general tax revenues).

They can cover a wide range of charges covering such varied public services as health, roads, air traffic control, fire services, statistics and legal services. The OECD<sup>19</sup> point out that the objective of user charging policies generally includes some or all of the following:

- “reducing budget deficits;
- making the cost and benefits of services more visible to their users and government organisations providing services;
- relieving the general taxpayer of costs properly borne by the users who benefit directly from a service;
- imposing discipline on user demand for services;
- fostering more business-like, customer-oriented management and generally improving the financial and service performance of the supplier; and
- encouraging the development of markets and competition.”

The main economic rationale for such charges falls into making more efficient use of government resources and in particular that the consumers of the service have regard to the cost. Where a public service is provided for free there is a risk that it will encourage overconsumption, imposing unnecessary costs on society and making government less efficient.

However, taking this general economic concept and applying in practice is fraught with difficulties not least as the wide range of public services generally provided by government means that some services may be more suitable for such an approach than others although there will be many services which it is hard to place a value on. Pricing is critical as getting prices too low or too high can encourage over or under consumption neither of which is efficient and without costs to society.

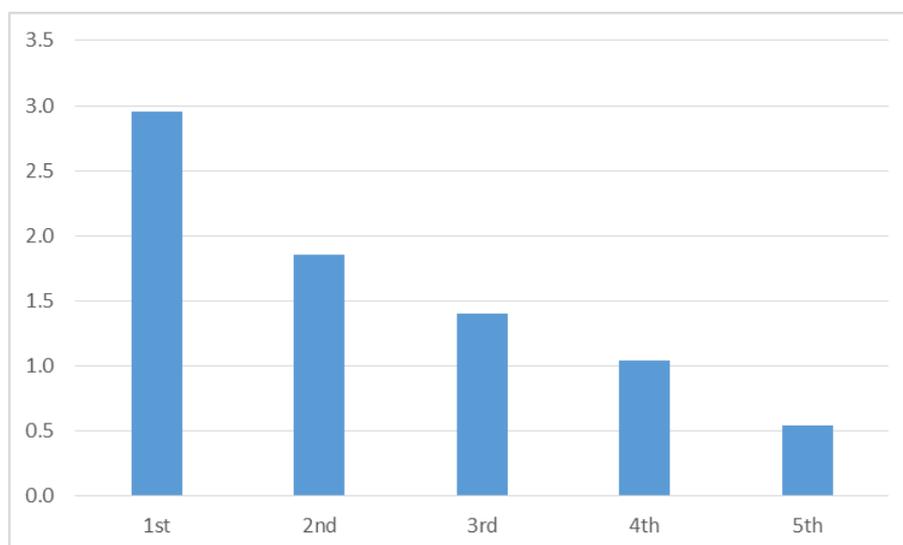
An often cited concern with user pays charges is that they are regressive in nature impact on the less well-off disproportionately. This comes from the fact that if there is

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<sup>19</sup> User charging for government services: best practice guidelines and case studies, Occasional Paper 22 1998

a fixed charge (or even a per unit charge where consumption/use does not vary with income) the cost is likely to be a higher proportion of lower incomes. The chart below shows that situation where a £500 charge is applied that each household pays and therefore the cost of this charge falls as a proportion as income rises.

**Figure 26: Distributional impact of user pays charge**  
£500 annual charge as % of income by income quintile



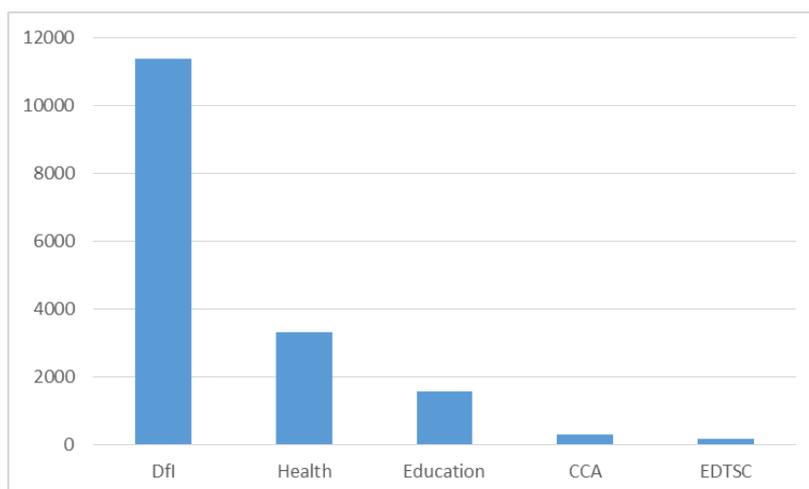
Source: Statistics Unit Income Distribution Survey/Economics Unit calculations

Such a high level analysis does not always apply in practice or to particular user pay charges. To give full consideration of the distributional impacts of user pays charges it is necessary to consider who benefited from the previous system where the services were provided free to users. It is possible that higher income households benefit more from the provision of certain services such as harbour berths or airport landing fees. Provision of free services may not be an effective way for society to achieve its equity and redistributive goals. In addition, even if there are adverse distributional impacts from such charges they could be designed in a way to offset the impacts on those on lower incomes through transfer payments or voucher/smart card style schemes where everyone gets a certain amount free or at low cost.

### 3.1 User charges in the MTFP

There are nearly £17m of user pays charges proposed in the MTFP. This amounts to about £400 per household although as discussed above how this impacts on households in practice and across the income distribution needs further consideration and examination of the detail. The chart below breaks the charges down by key department and the amount of revenue that it is proposed they will raise.

**Figure 27: Revenue raised by user pays charges by department by 2019**  
total revenue by 2019, £000s



Source: Treasury and Resources Department

It can be seen that the sets of charges by the Department for Infrastructure, health and education make up nearly 90% of the revenue raised. Each of these groups of charges is considered in turn below.

#### *Department for Infrastructure*

The proposed charges by Dfl make up nearly £11.5m which consist of £5.5m each for a new Liquid and Solid Waste charge and £0.35m for a green waste charge. The indicative Liquid and Solid waste charges are commercial charges of £3.12 per cubic metre (average commercial charge in 2018 of £1,728 per annum) and £150 per tonne.

Such charges should encourage businesses to manage their waste more efficiently but are still likely to feed through into higher costs to some degree. Where such charges that fall on commercial enterprises cannot be offset by efficiency improvements they are likely to impact on islanders through one of three ways:

- increased prices
- reductions in other costs such as employment costs
- reduced dividends for shareholders.

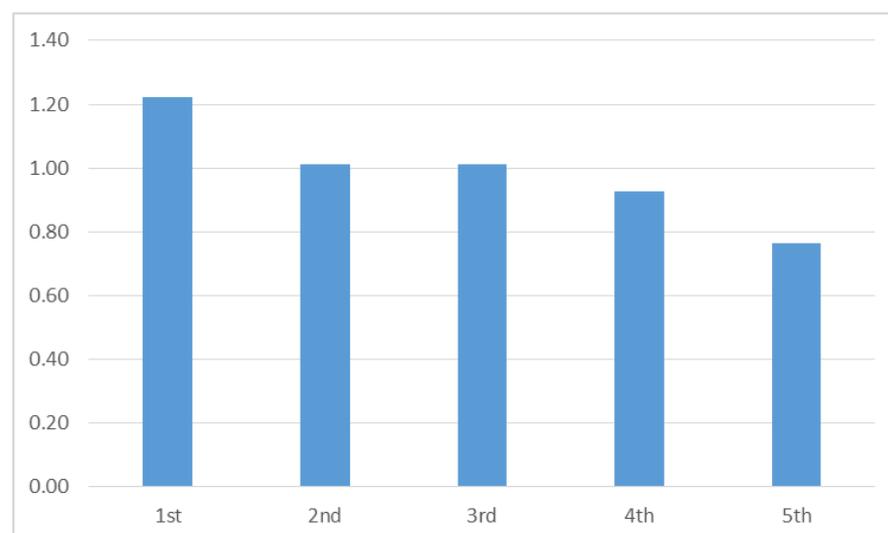
The degree to which it feeds through any of these routes will depend on the nature of the markets for the final product/service. Businesses exporting large shares of their output may not be able to pass the costs on through increased prices as their competitors may not be subject to the same change in their costs. Shareholders may not be prepared to take lower returns and the degree to which it reduces returns

relative to other investments could impact (marginally) on the level of investment in the island.

Where the businesses affected are competing in local markets and impacted to the same degree the cost is more likely to be passed straight through into prices. This is because there would be little impact on their competitive position and would mean that islanders (and to some degree visitors) are likely to bear the costs.

There is insufficient data available to calculate the relative impact but, in general, activities producing more waste per unit of output would see their prices rise more in absolute terms than other activities. As a first approximation, these increases in the costs of production will hit residents in proportion to their expenditure. The chart below shows that if expenditure rises by 1% across each income quintile then this would be mildly regressive across the bottom four quintiles although the top quintile would pay a significantly lower proportion of their income than the other four (this reflects the fact that expenditure is a much lower proportion of income).

**Figure 28: Distributional impact of a 1% increase in expenditure**  
% of income by income quintile



Source: Statistics Unit Household Expenditure Survey/Income Distribution Survey

Initial indications from the Department for Infrastructure are that although the charges will apply to all commercial sectors, some sectors may naturally produce more waste than others. For solid waste the sectors likely to be responsible for the largest solid waste charges are:

- Construction / Demolition / Property Development
- Large Hotels

- 
- Health Services (Municipal & Clinical Waste)
  - Large Supermarkets

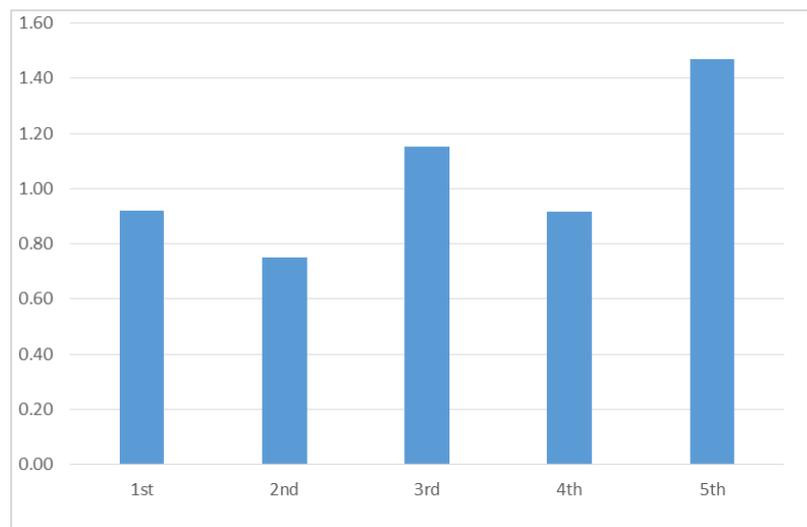
As liquid waste charges are likely to be based on water usage businesses using a large volume of water will face the greatest bills and are likely to be in the following sectors:

- Hotels
- States housing
- Dairy
- Hospital
- Schools
- Fitness Centres (particularly with swimming pools)
- Cleaning businesses that rely on water volumes

The combined distributional impacts of charges impacting in these sectors will be complex. For example, how the States meets the costs in areas such as health or education could depend on whether they are funded from general income taxation (raised in a broadly progressive way), GST (mildly regressive) or user charges (likely to be regressive). However, given that the sectoral impact is still somewhat uncertain it is not clear that there is sufficient information at this stage to contradict the general finding that if such charges feed through into higher prices they are likely to be regressive. As the detail around charging structures and impacts on sectors emerges as work on the charges progresses this is something that can be reviewed in due course.

It is also proposed that a Commercial Green Waste Charge will raise £357k by 2019. This is a charge for the disposal of garden waste by business and could therefore feed through into higher professional gardening costs. It might be expected that the better off would be impacted more by such a charge and although there is not sufficient detail in the household expenditure survey to look at this type of expenditure alone, spending on domestic services does tend to rise as a proportion of income as shown in the chart below. This suggests that if gardening services show similar distributional traits such a charge could have progressive distributional impacts although it is not uniform across the quintiles.

**Figure 29: Domestic services spending as a share of income % of income by income quintile**

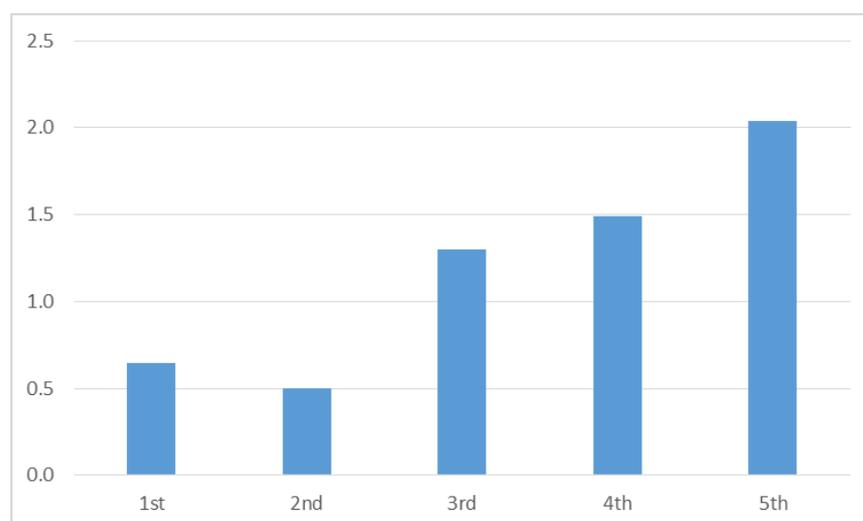


Source: Statistics Unit Household Expenditure Survey/Income Distribution Survey

*Education*

The proposed reduction in grants to fee paying States schools raises the most revenue from the measures proposed by the Education Department and about £600k per annum by 2019. It is assumed that this will lead to an increase in fees for those paying these school fees. The household expenditure survey provides information on expenditure on school fees across the income distribution. Although this will also include expenditure on fees from schools outside the island it should be a fairly good proxy for indicating the likely distributional consequences of raising school fees in Jersey.

**Figure 30: Expenditure on schools fees across the income distribution school fees % of income by income quintile**



Source: Statistics Unit Household Expenditure Survey/Income Distribution Survey

It is anticipated that the reduction in grants will lead to an increase in fees and the analysis above suggests that if this is a uniform increase in fees then the impact will be progressive. That is every 1% increase in fees will be a higher proportion of the average income of the higher earners. This may simply reflect the fact that a larger proportion of higher earners are able to send their children to fee paying schools. It may not change the distributional impact of the overall policy which may be that the grants to fee paying schools are regressive in nature because they disproportionately benefit those on higher incomes.

### *Maintenance grants*

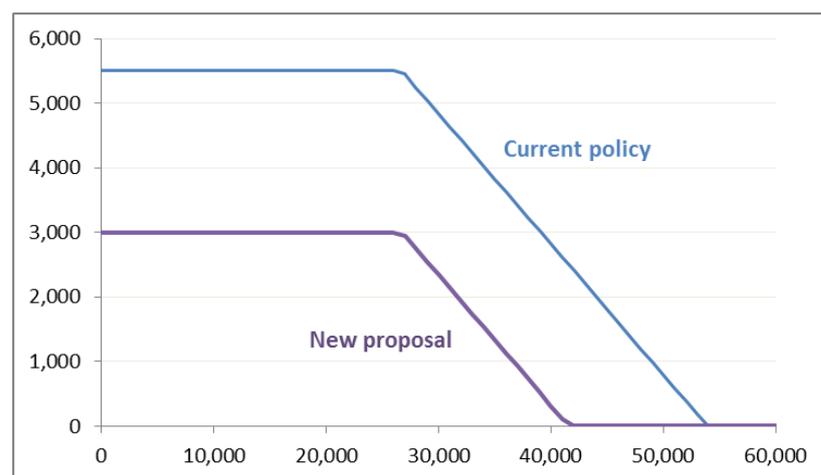
It is proposed that maintenance grants for on-island degrees will be cut from £5,500 to £3,000 from 2018. These grants are means tested and capped at £5,500 for a standard course for the 2016/17 academic year and is to help towards living expenses.

If a household earns below £26,750 it will receive the maximum grant available and if a household earns over £54,000 it won't receive a maintenance grant. The parental contribution is calculated as below:

$$\text{Parental contribution} = (\text{gross household income} - £26,750) \times 20.25\%$$

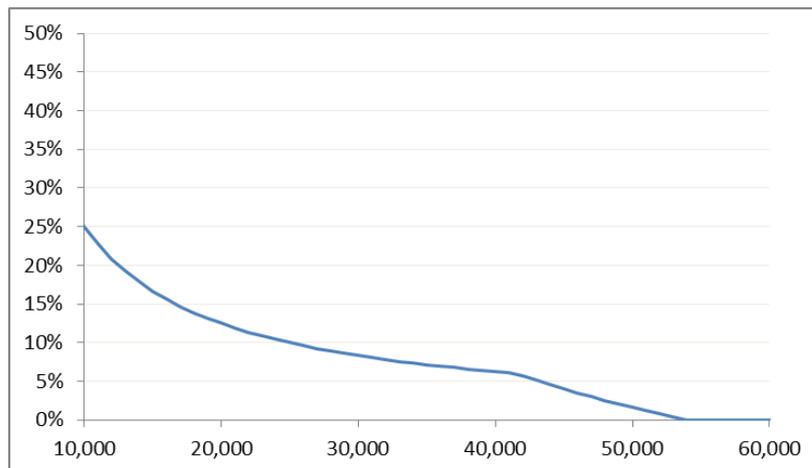
The chart below shows how the States grant varies by income under the current scheme and when it is capped at £3,000.

**Figure 31: States maintenance grant by income before and after policy change**  
£ per household



**Figure 32: Change in States contribution as a proportion of income after policy change**

% of income



### *Nursery Education Foundation*

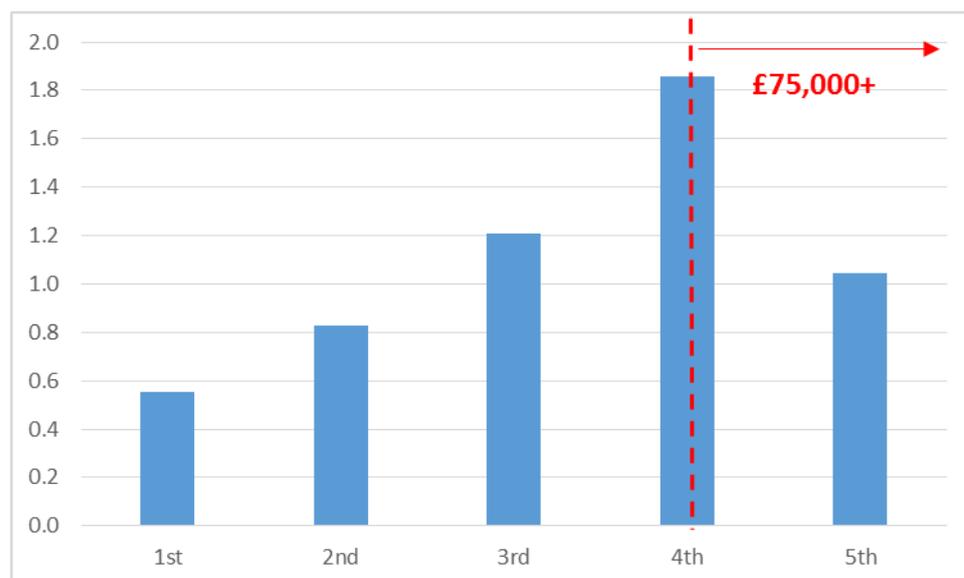
The Nursery Education Fund, which provides free nursery places for three-to four year olds, is being changed to focus funding on the families that most need assistance.

Currently, almost every child in Jersey has their nursery education subsidised by the States when they are aged 3 to 4 and in the year before they start Reception at primary school. Irrespective of their income, all families can receive 20 hours of free nursery education for their child for 38 weeks in term time at a private commercial nursery. This accounts for £1.9 million of the Education Department's budget annually.

It is proposed that from September 2017 the Nursery Education Fund will be targeted for the first time so that children families with a household income of less than £75,000 will receive the free places. The States spends £3,914 per child per year on the nursery places.

### Figure 33: Expenditure on nursery, crèche and childcare across the income distribution

% of income by income quintile



Source: Statistics Unit Household Expenditure Survey/Income Distribution Survey

Over the 2017-2019 period there will be about 1,000 children per year of nursery age. About 60% of those children will go to States funded nurseries, about 7% will go to private nurseries with about 30% in NEF nurseries.

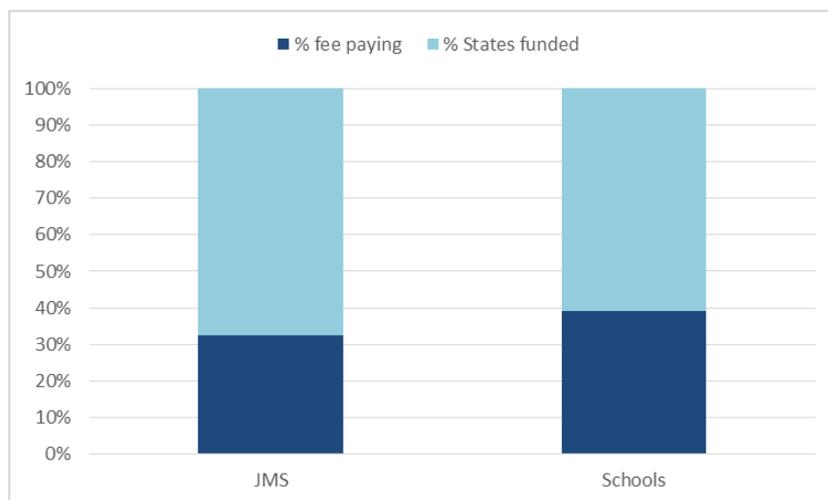
From information provided by the Statistics Unit, it is predicted that means testing at a household income level of £75,000 will impact on 30% of households with at least one child under five. Calculations by the Education Department suggest that once the number of children attending States nurseries and private nurseries is taken into account this measure might impact on between 60-120 families per year between 2017/18 and 2019/20.

#### *Jersey Music Service*

792 students received lessons from the Jersey Music Service in the summer-term of 2016. About 33% of those children were at fee paying schools. This compares to 39% of the school children (year 5 plus) attending the fee paying schools and suggest that if the JMS moves to cost recovery then the impact will be spread across families in all areas of the income distribution. Assuming that children have a similar number of lessons then the impact may be regressive i.e. that the less well-off households have to contribute a larger share of their income in fees for music lessons. However, there may be families in each quintile that have private lessons

and are unaffected and there may be a different response between households at different points in the income distribution e.g. in choosing whether to continue and how many lessons to have.

**Figure 34: Proportion of children at fee paying schools**  
those receiving lessons from Jersey Music Service, year 5+ school population



Source: Education Department

### 3.2 Health user pays

As Smith and Oxley (2008)<sup>20</sup> point out in their OECD conference paper, user charges in health care tend to have two broad roles:

- to raise finance for health expenditure
- send market signals to patients who would otherwise pay nothing for services.

The latter point relates to concerns about ‘moral hazard’ – that is when patients face no costs for using the service they may use it when it is not required. They do not bear the cost of using the services so they are not prevented or discouraged from using the services in an inefficient way.

They conclude that there is a shortage of reliable evidence in developed countries on the impact of health user charges on the take up of health care services and the health of patients. The one major exception is from the US where the RAND experiment, which covered 2,000 patients over an extended period who were allocated different charging regimes – ranging from complete freedom from charges to near full cost charges. The results showed consistent reductions in all types of health care as the charges became more significant. However, with one important

<sup>20</sup> The impact of user charges in health care, Smith and Oxley, OECD/EU Conference paper 2008

exception, the results also did not detect any material variations in health outcomes for those exposed to the charging structures. They highlight that the conclusions are that for most of the population “charges succeeded in encouraging less profligate use of health care without serious health consequences”.

The one important exception was that charging appeared to have serious impacts on those who were both poor and suffering from poor health. Smith and Oxley conclude that:

*“unless carefully designed, user charges designed to curb excessive demand amongst the bulk of the population could have ruinous financial or health consequences for a relatively small number of poor people with health problems. It is therefore important to view the design of user charges within the broader objectives and institutions of the health system as a whole.”*

Concerns about the impact of such charges on the less well-off could at least partially be alleviated by excluding them from charging systems through some form of means testing or indirectly through the benefit system. In addition, voucher type schemes could be used to mean that people only get a certain number of visits/treatment for free or at lower cost and have to pay more when they exceed this level of use.

Understanding the distributional impacts of any type of medical user pays charges is also complicated by the fact that different groups may have different price elasticities of demand and therefore respond differently. For example, if the less well-off have higher price elasticities they could reduce the use of a service more than the better off. How this impacts on their health and health outcomes depends on the degree to which the service was being used by them in the first place, the benefits they obtained as a result and their health circumstances.

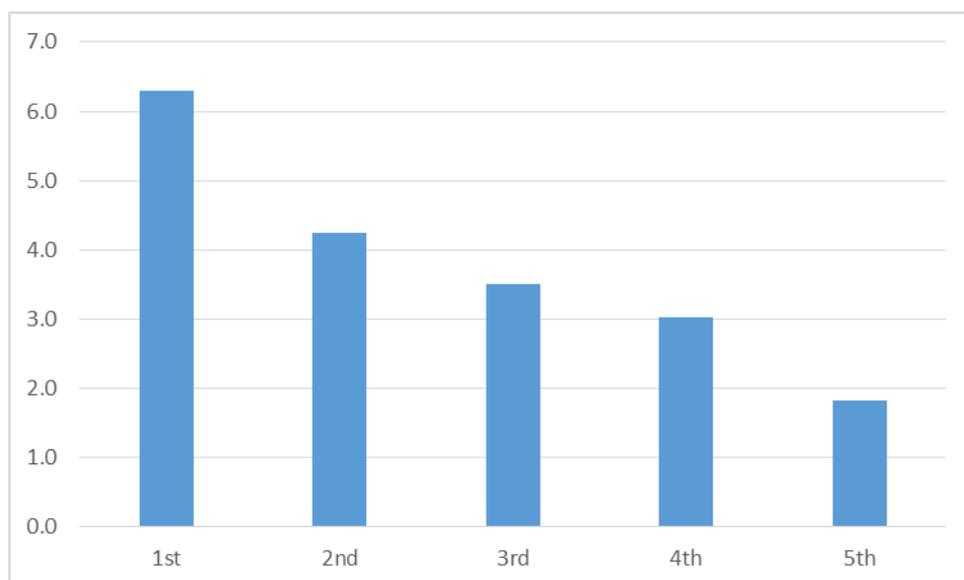
It is possible that user pays leads to better use of health resources. This can mean that the use of services is more cost effective and allow service improvements for any given level of health budget. In addition, by allocating resources to those who most need them they can prevent over utilisation of resources and reduce waste. It is important to consider if either of these are achieved – at least partially - who benefits and to what degree. However, as section 1 points out if health expenditure is generally seen as progressive then making better use of existing health expenditure could benefit people in a progressive way.

#### *Health expenditure in Jersey*

Jersey households already spend on average £25 a week on health related expenditure. This is made up of spending on pharmacy/other products, doctor and

dentist fees, opticians and other expenditure (such as existing hospital charges). The largest proportion of this expenditure is dentist fees followed by pharmacy and doctor fees. The chart below shows that expenditure in these areas falls as a proportion of income as income rises. This would suggest that an increase in the relevant charges covered in this area of expenditure would tend to impact in a regressive way.

**Figure 35: Household expenditure on health across the income distribution**  
% of income by income quintile

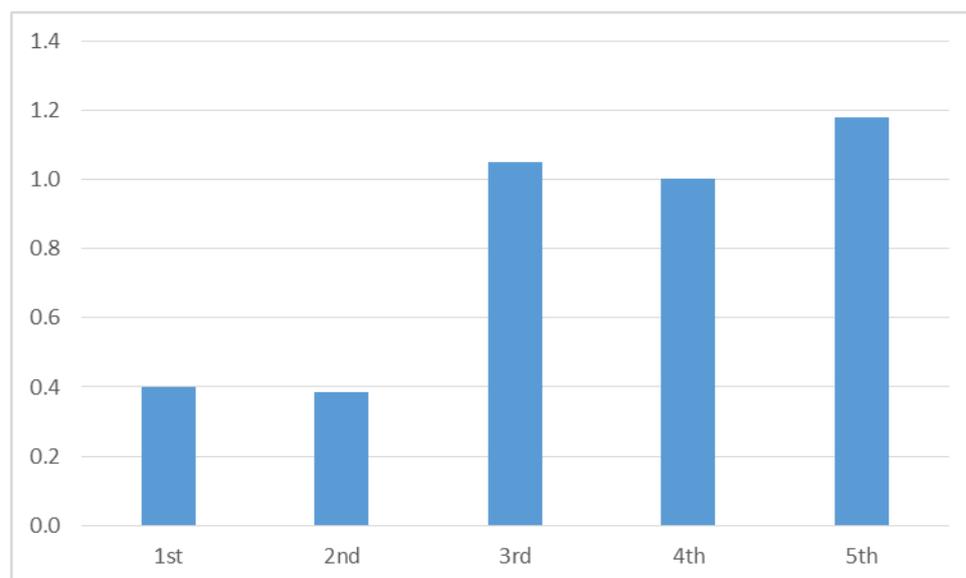


Source: Statistics Unit Household Expenditure Survey/Income Distribution Survey

It is also possible to look at expenditure on medical insurance premiums across the income distribution. The chart below shows that this tends to rise as a share of income, although it is relatively flat between the 3<sup>rd</sup> and 4<sup>th</sup> quintiles. This should not however be seen as a precise indication of ability to use private medical care as it may also be provided as a benefit in kind through employers. While the household expenditure survey does not cover such information it may be a fair assumption to assume that it is primarily focused on those on higher incomes.

### Figure 36: Household expenditure on medical insurance across the income distribution

% of income by income quintile



Source: Statistics Unit Household Expenditure Survey/Income Distribution Survey

The user pay charges indicated by the Health and Social Services Department amount to over £3.0m and are split into three broad areas:

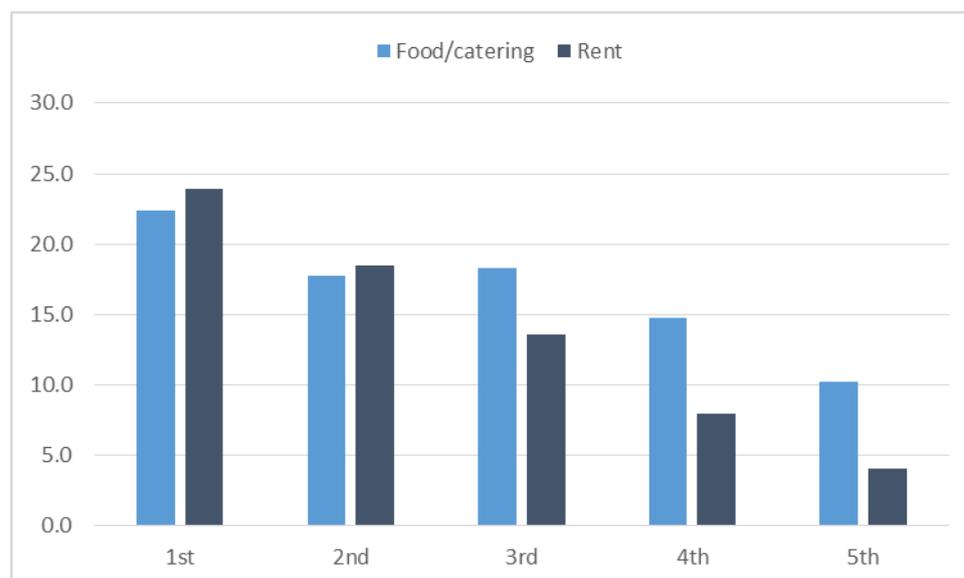
- Hospital charges (£1.2m)
- Environmental health charges (£800k)
- A mixture of other charges including reduced travel subsidies

While the detail of the hospital charges is still being determined it is likely that any such charges will show regressive tendencies as highlighted above. This could partially be offset by protecting certain groups on low income – for example those on income support. However, it will also be the case that those benefitting from private medical insurance will be less likely to bear the cost of any new charges.

Environmental health charges are likely to be incurred on food/catering businesses and also the private sector housing rental sector. The chart below shows that spending on these items falls as a share of income as income rises and that in general terms if such charges lead to higher prices/rents the impact would tend to feed through in a regressive way. In the case of the impact on rents it may be that the social rented sector is not impacted in the same way because it is covered by different regulations which might offset some of the impact on those in the lower quintiles.

### Figure 37: Household expenditure on food/catering and rent across the income distribution

% of income by income quintile



Source: Statistics Unit Household Expenditure Survey/Income Distribution Survey

It is difficult to determine the distributional impact of the remaining health user pays charges as there is not sufficient detail at this stage. However, it could be that in areas such as potential changes to travel subsidies the impact does not conform to the analysis above of general health charges. For example, if the current scheme was changed to focus more on supporting those with recurring travel costs associated with their health care then this might not be a regressive change relative to the current system where there is a general means test in place.

### 3.3 States paying rates

The principle that the States should pay Parish rates on the properties it owns was agreed by the States Assembly in both the Strategic Plan and the MTFP 2016-2019. The Council of Ministers has agreed that the States will start paying Parish rates from 2017 provided a compensating income stream can be found to meet the resulting cost to the States.

The current estimate of the States liability to Parish rates will be approximately £900k per annum (based on the 2015 Parish rates). The income stream under consideration is that the money is raised through the Island Wide Rate (IWR) for non-domestic (commercial) properties.

As mentioned previously in this section there are a number of ways this could feed through the economy. To the extent that the increase in non-domestic IWR is

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passed on to consumers through increased prices, this increase in prices is likely to be regressive in nature across households at different points in the income distribution.

It is not certain that the increase in non-domestic IWR will be passed on to consumers in all circumstances; it depends on the market circumstances applying in each context, as discussed previously in this section. However, this may not change the overall regressive nature if, for example, it leads these businesses to reduce other costs such as those for employment.

The regressive impact outlined above could be tempered by how the additional money is spent by the Parishes, particularly as the Parish of St Helier will be the major beneficiary. The spending is more likely to benefit more individuals at the lower end of the income distribution (than if spent in a rural parish) given the make-up of the St Helier population. However, as previously discussed in this paper assessing the distributional impact of public spending is difficult and it is not yet clear what this additional spending will be on.

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## Section 4: Health charge distributional analysis

### Introduction

In P82/2012 the States agreed that the Council of Ministers should co-ordinate the necessary steps by all relevant Ministers to bring forward for approval proposals for a sustainable funding mechanism for health and social care, by the end of 2014. This sustainable funding mechanism is known as the “health charge”. To date no indication of the structure/format of the health charge has been made public.

MTFP 2016-2019 originally included a target amount of additional revenue from the health charge of £15m in 2018 and £35m in 2019.

The MTFP Addition 2017-2019 now includes a target amount of additional revenue from the health charge of £8 million by 2018, increasing to £15 million in 2019.

There are limited options for raising this amount of additional revenue within the framework of the existing Jersey tax system. It should also be noted that, with the exception of capital taxes – such as capital gains tax and inheritance tax – Jersey already utilises each of main internationally recognised tax revenue raising measures.

This section of the document outlines the distributional analysis associated with each of the potential revenue raising options considered by Ministers for the health charge.

### 4.1 Benchmarking of options

When considered the potential options available to raise the additional revenue required from the health charge the Council of Ministers benchmarked them against the five criteria against which revenue raising measures should be benchmarked (as identified in 2010 Fiscal Strategy Review), namely:

- Fairness
- Economic Efficiency
- Competitiveness
- Administration costs
- Revenue Stability

Furthermore, when considering the potential options the Council of Ministers have kept in mind the long term tax policy principles agreed by the States Assembly in the 2015-2018 Strategic Plan, namely:

Principle 1: Taxation must be necessary, justifiable and sustainable

Principle 2: Taxes should be low, broad, simple and fair

Principle 3: Everyone should make an appropriate contribution to the cost of providing services, while those on the lowest incomes are protected

Principle 4: Taxes must be internationally competitive

Principle 5: Taxation should support economic, environmental and social policy

As part of the process of considering the “fairness” of the potential options, the Council of Ministers have specifically considered the distributional impact analysis of the potential options across the income spectrum.

#### **4.2 Distributional analysis – preferred options**

Having considered the potential options in detail, it appears that there are two options which are receiving more detailed consideration from the Council of Ministers: (i) a new income based charge which mirrors the long term care (“LTC”) contribution and (ii) an increase in GST. The distributional impact of these two proposals is shown and discussed below.

*Option (i): the introduction of a new income based charge which mirrors the LTC contribution*

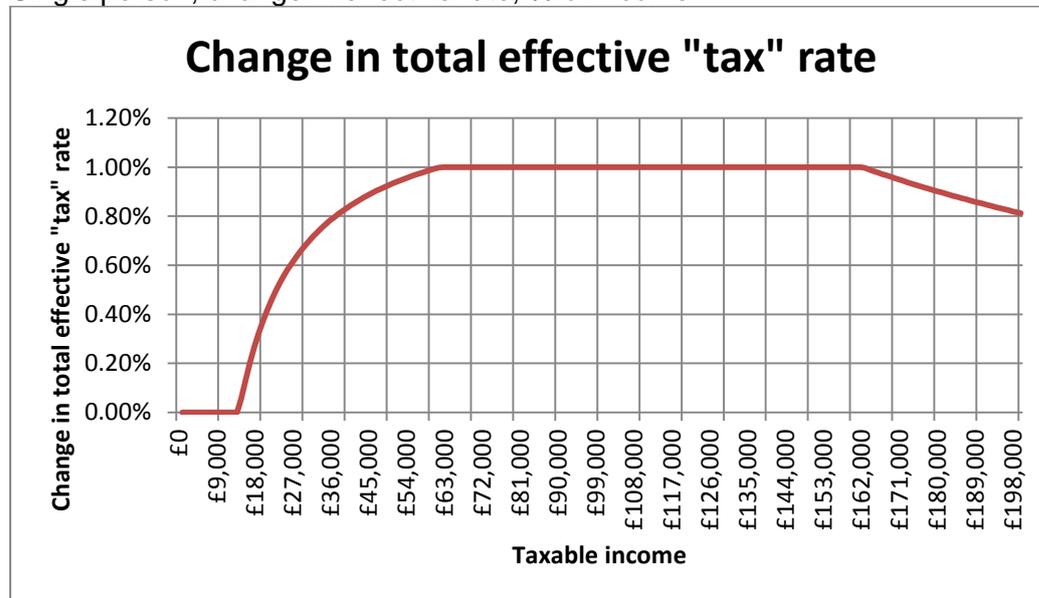
For a single person a 1% income based charge mirroring the LTC contribution would be broadly progressive across the whole income distribution but would have the following distributional impacts:

- there would be no impact on those people with incomes below the exemption limits
- for those on the marginal tax rate the effective rate would gradually rise as to 1% income raises (progressive for these income levels)
- for those on the standard tax rate of 20% the effective rate would be 1% for all incomes (subject to the next caveat) (proportional for these income levels)

- for those on the standard tax rate of 20% and above the £164k cap utilised for the LTC contribution the effective rate would gradually fall as a proportion of income as income rises (regressive for these income levels).

**Figure 38: Change in total effective tax rate from introduction of a new income based charge which mirrors the LTC contribution at 1%**

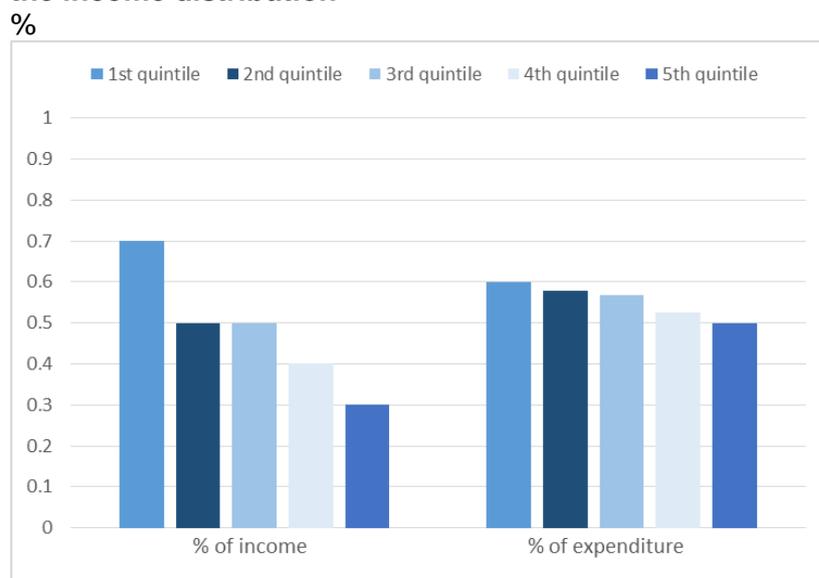
Single person, change in effective rate, % of income



*Option (ii): increase GST*

The distributional impact of GST is summarised in the chart below. It is important to look at the impact as a proportion income and expenditure and that while the degree varies slightly by the measure chosen, GST is mildly regressive. This is mainly due to the effect on those households on the lowest incomes, which spend a larger proportion of their income on essential items such as food and domestic energy. Those on higher incomes tend to save more and GST therefore represents a lower proportion of income/expenditure because they do not spend all their income in any one year.

**Figure 39: Increase of 1% in GST as a share of income and expenditure across the income distribution**



Source: States of Jersey Statistics Unit/Economics Unit calculations

### 4.3 Distributional analysis – wider options

The following distributional analysis has been prepared on the following basis:

- Analysis of the distributional impact of the existing (i.e. 2016) income based measures has been produced in order to provide context
- Distributional analysis has been prepared for:
  - Option A: increase LTC charge or introduce new LTC based charge
  - Option B: increase marginal rate of income tax from 26% to 28%
  - Option C: increase social security contributions below the standard earnings limit
  - Option D: increase social security contributions above the standard earnings limit
- To help with the comparability of the analysis, each measure analysed below is set at the level/rate required to raise approximately £15m per annum.
- In respect of the income based measures (income tax, social security contributions and the Long Term Care (“LTC”) contribution) graphs have been produced which outlined the impact on the person’s effective tax rate across the income spectrum (analysis capped at income of £200,000 per annum).
- In respect of the income based measures the distributional analysis has been prepared for four different type of households, namely:
  - Household 1: single person – working age

Household 2: single person – aged 65+

Household 3: married couple –working age (assumed income split equally between spouses)

Household 4: married couple – aged 65+ (assumed income split equally between spouses)

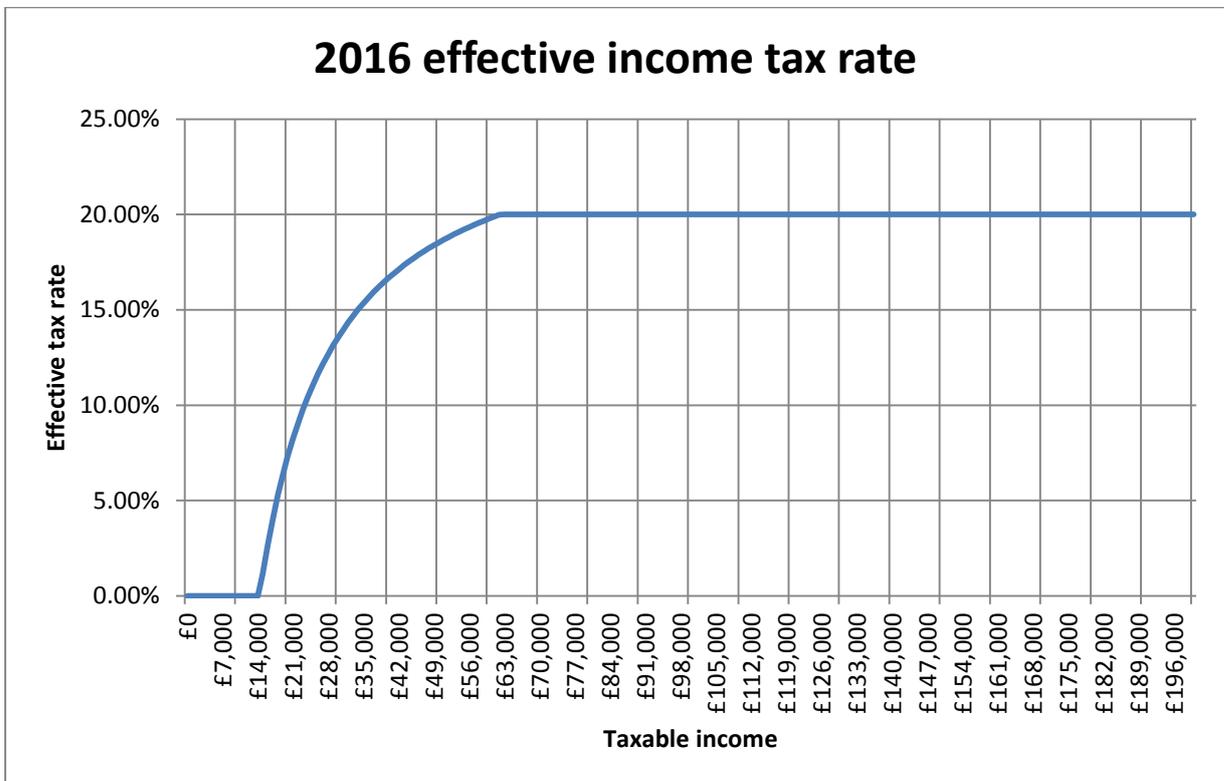
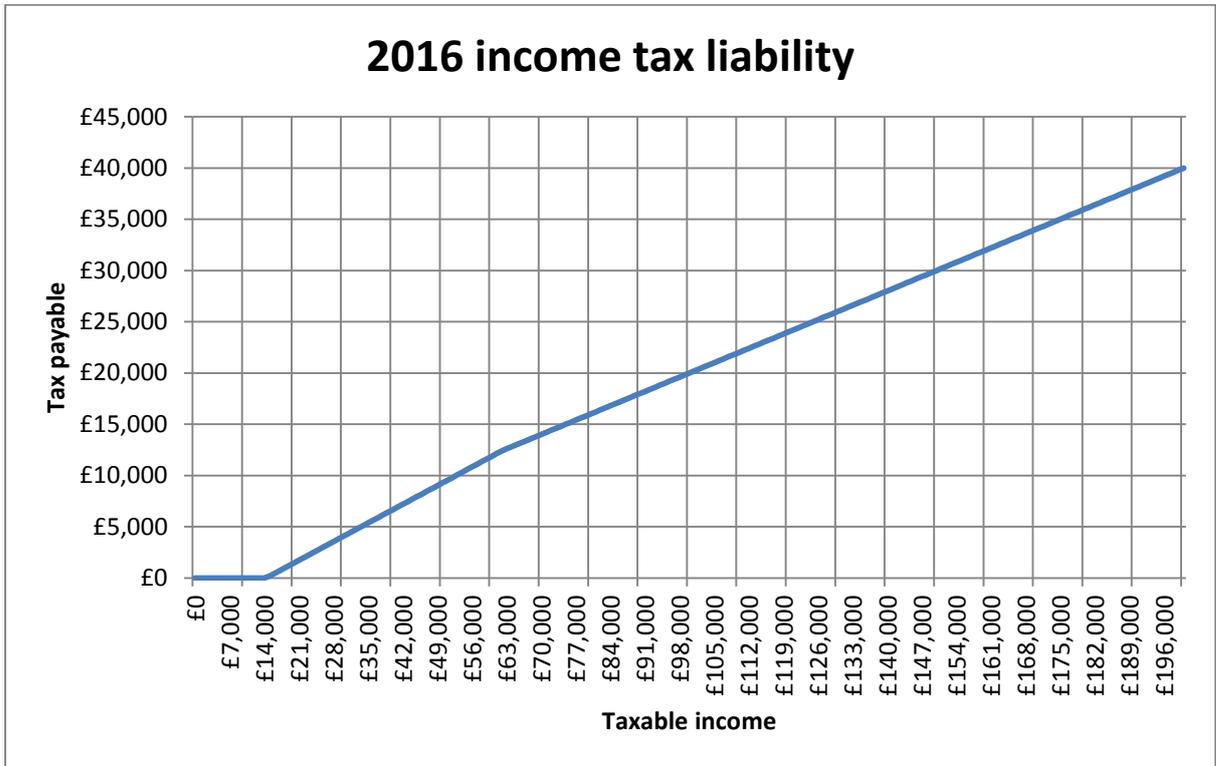
- Each of these households are entitled to no tax allowance other than (i) the applicable exemption threshold; and (ii) in the context of married couples, the application of the second earners allowance

## Household 1: single person – working age

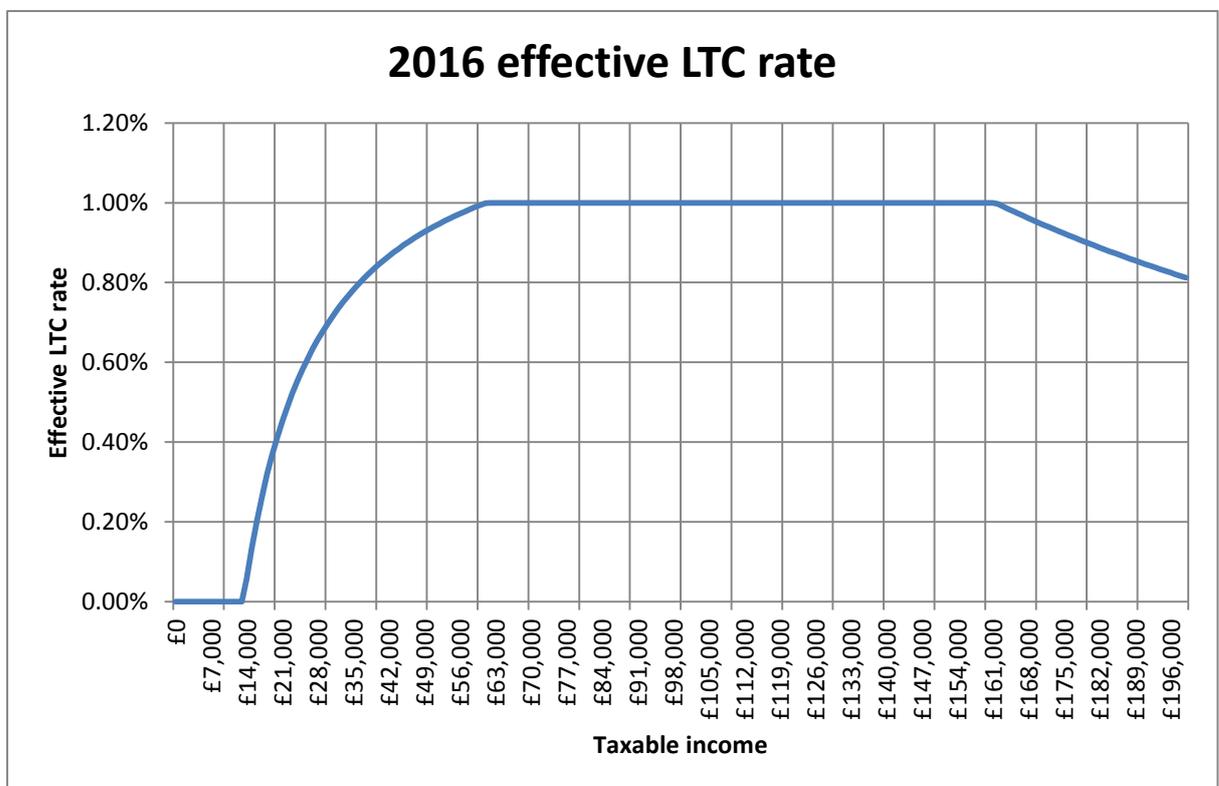
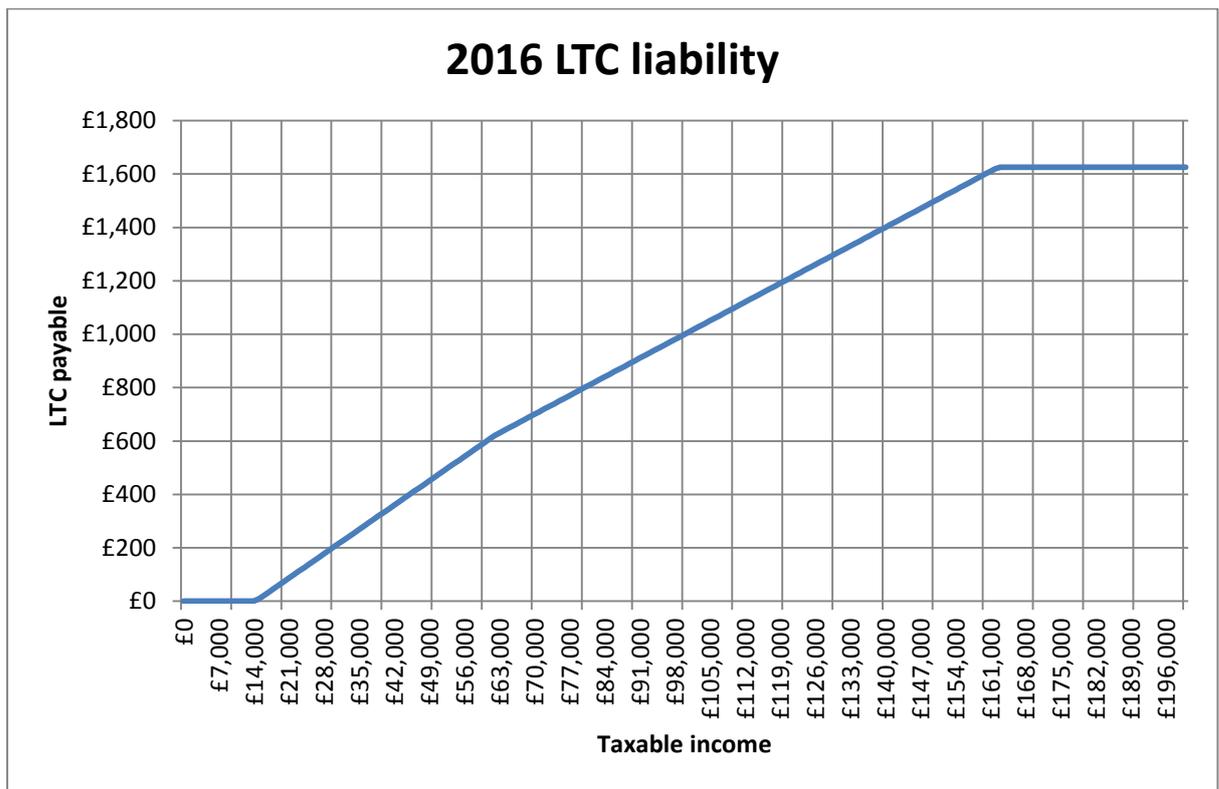
### 2016 Baseline Analysis

**Baseline for 2016 year of assessment**

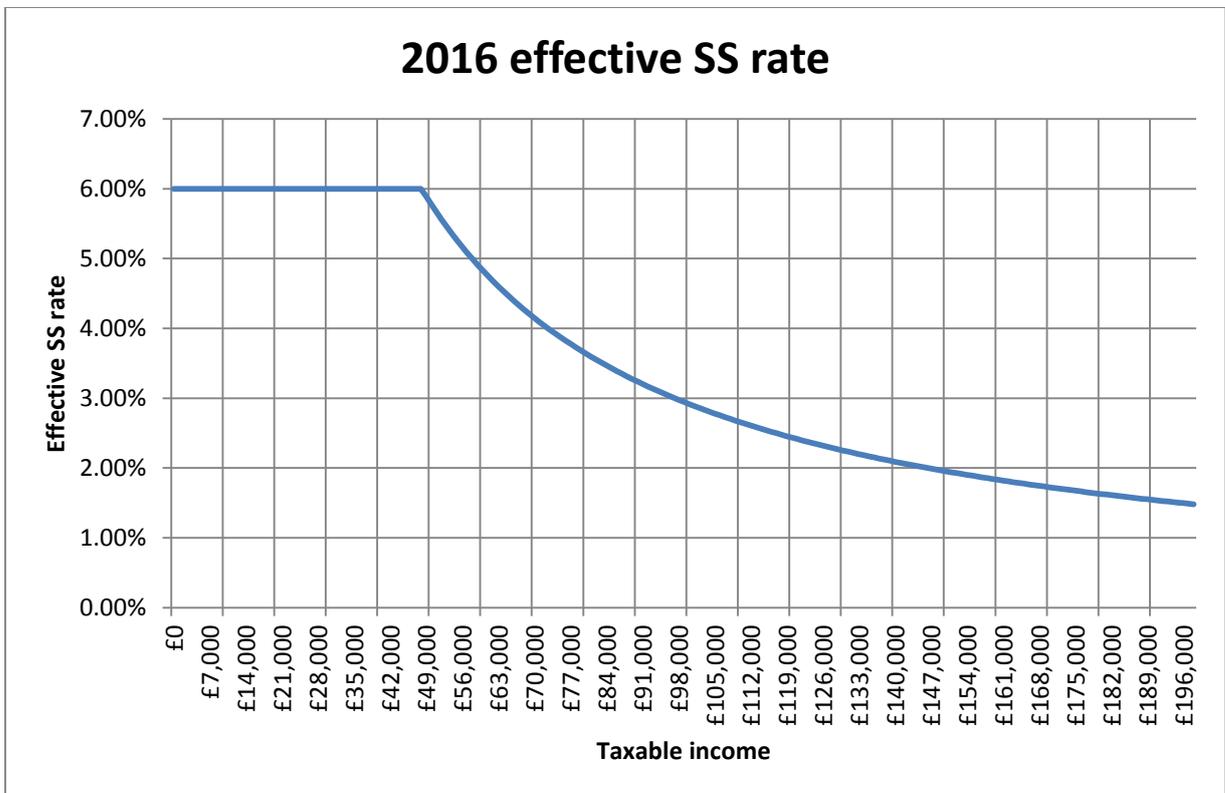
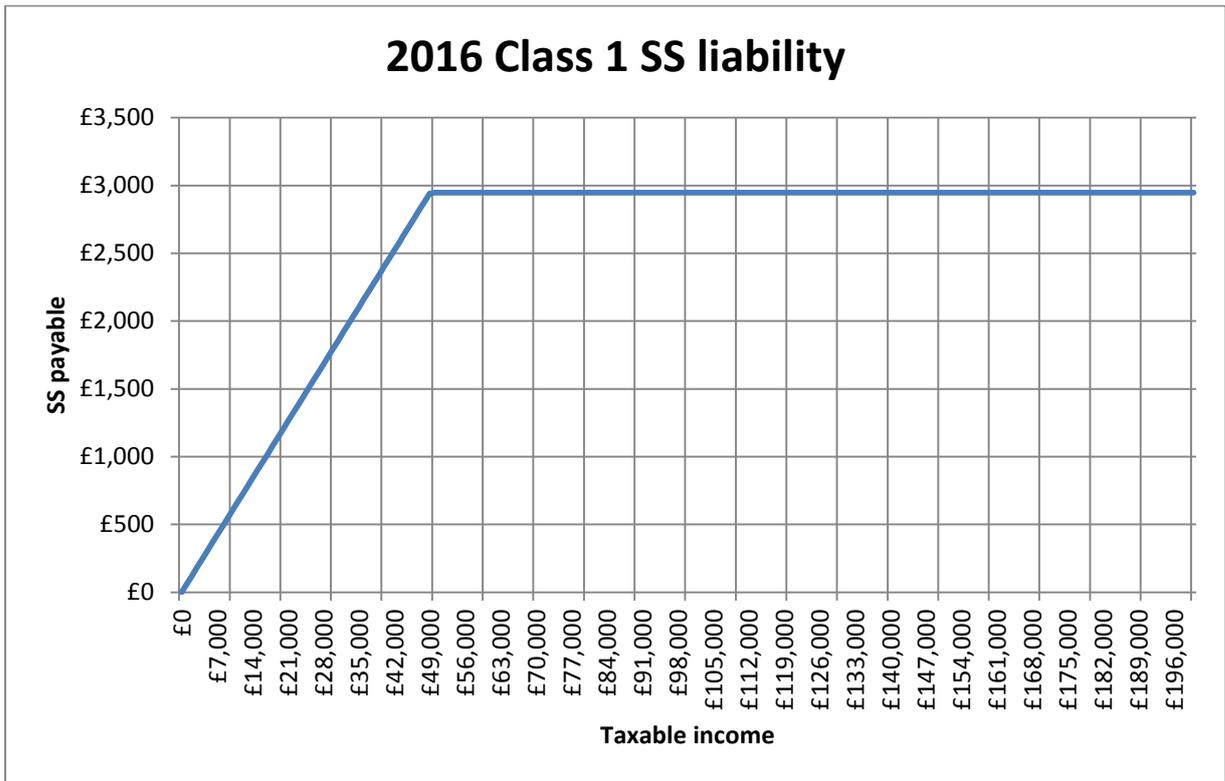
*2016 Baseline: single person/working age – Income tax*



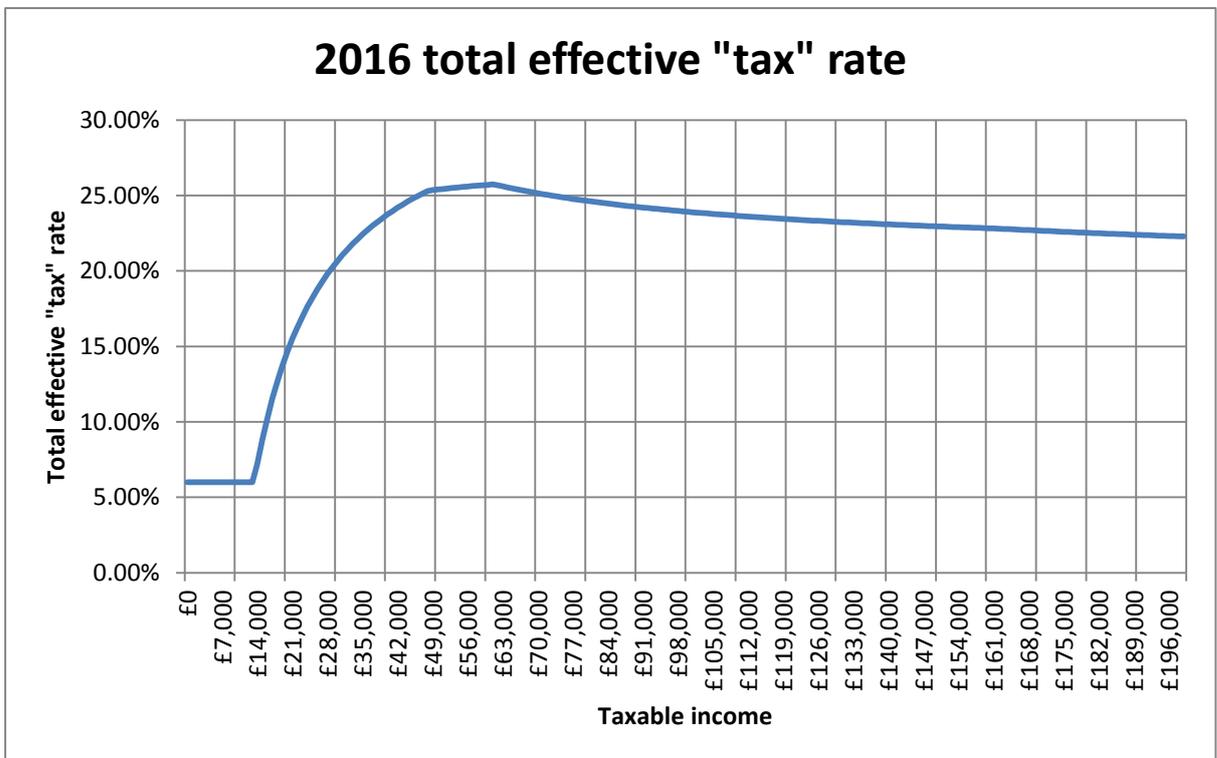
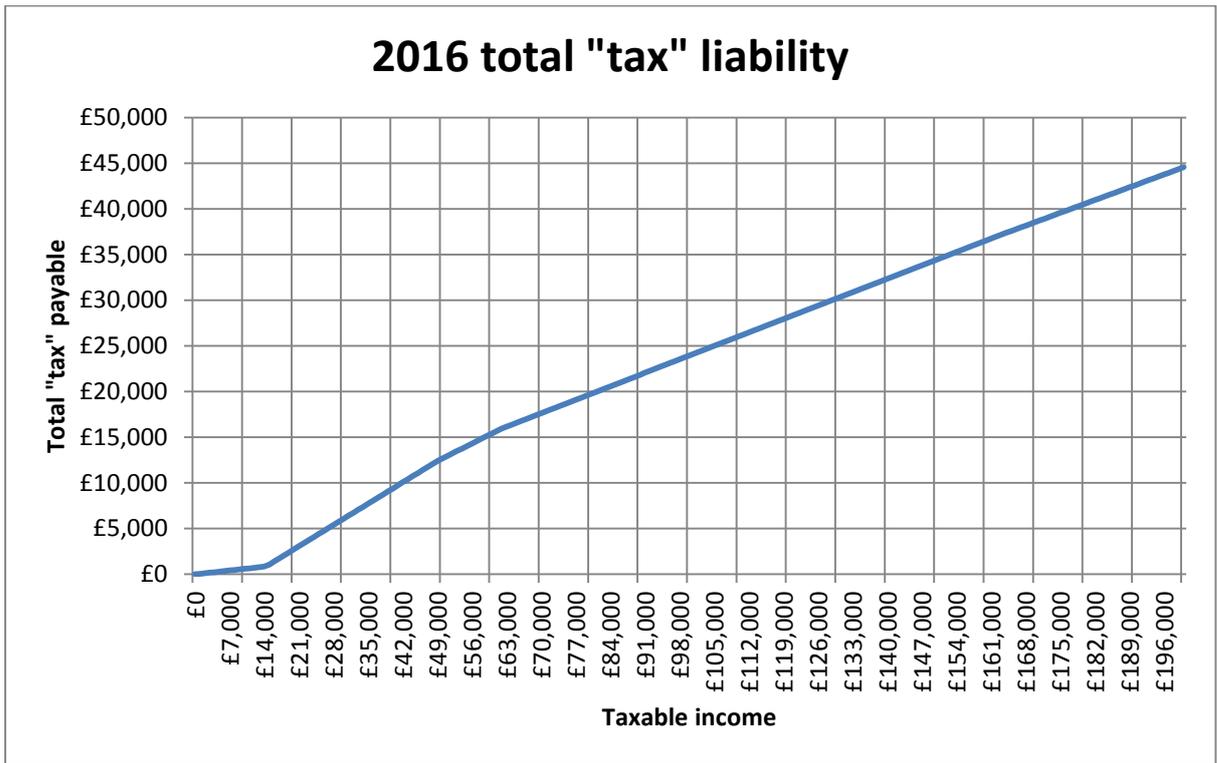
2016 Baseline: single person/working age – Long term care contribution



2016 Baseline: single person/working age – Social Security contributions



2016 Baseline: single person/working age – Overall tax position

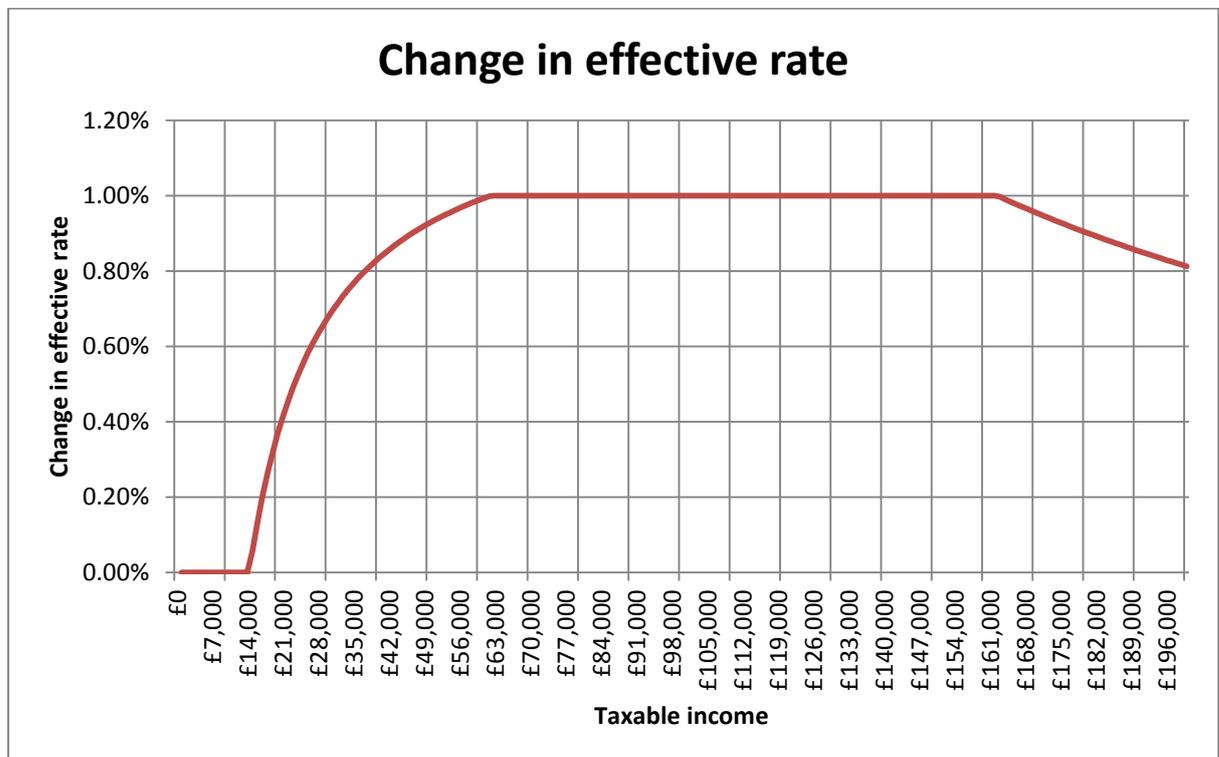
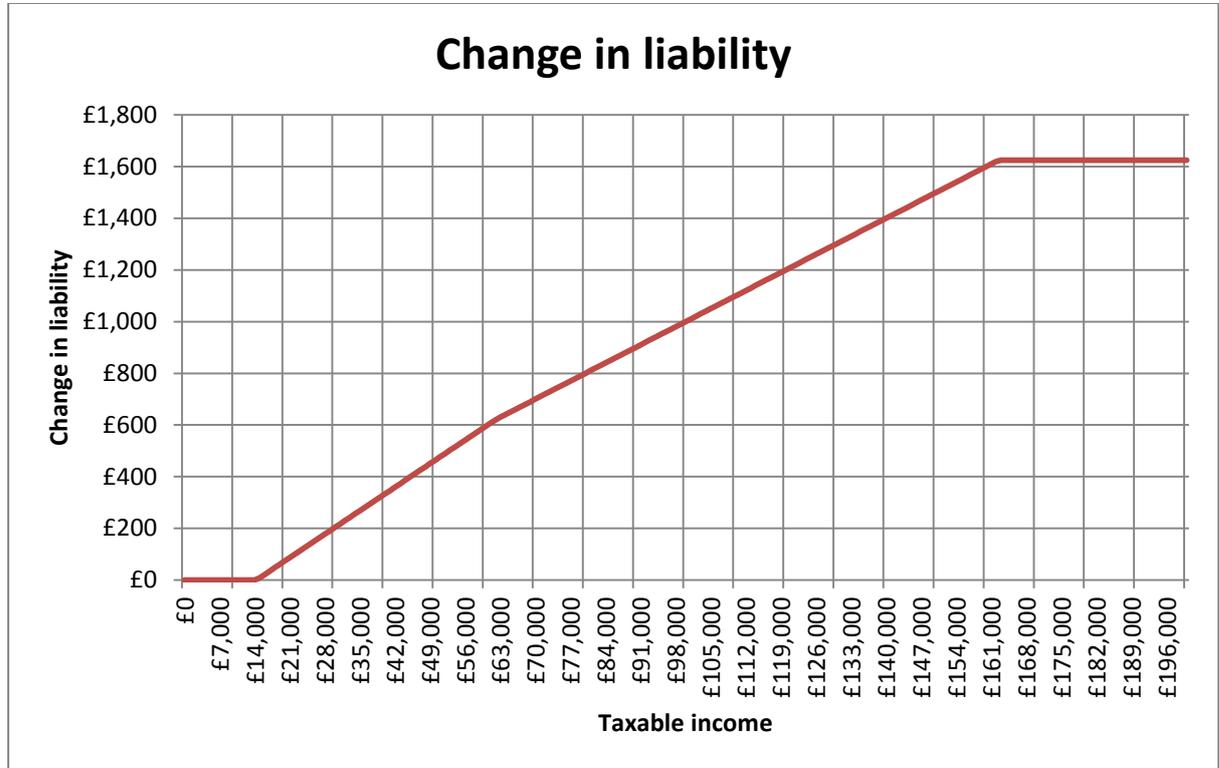


Household 1: single person – working age

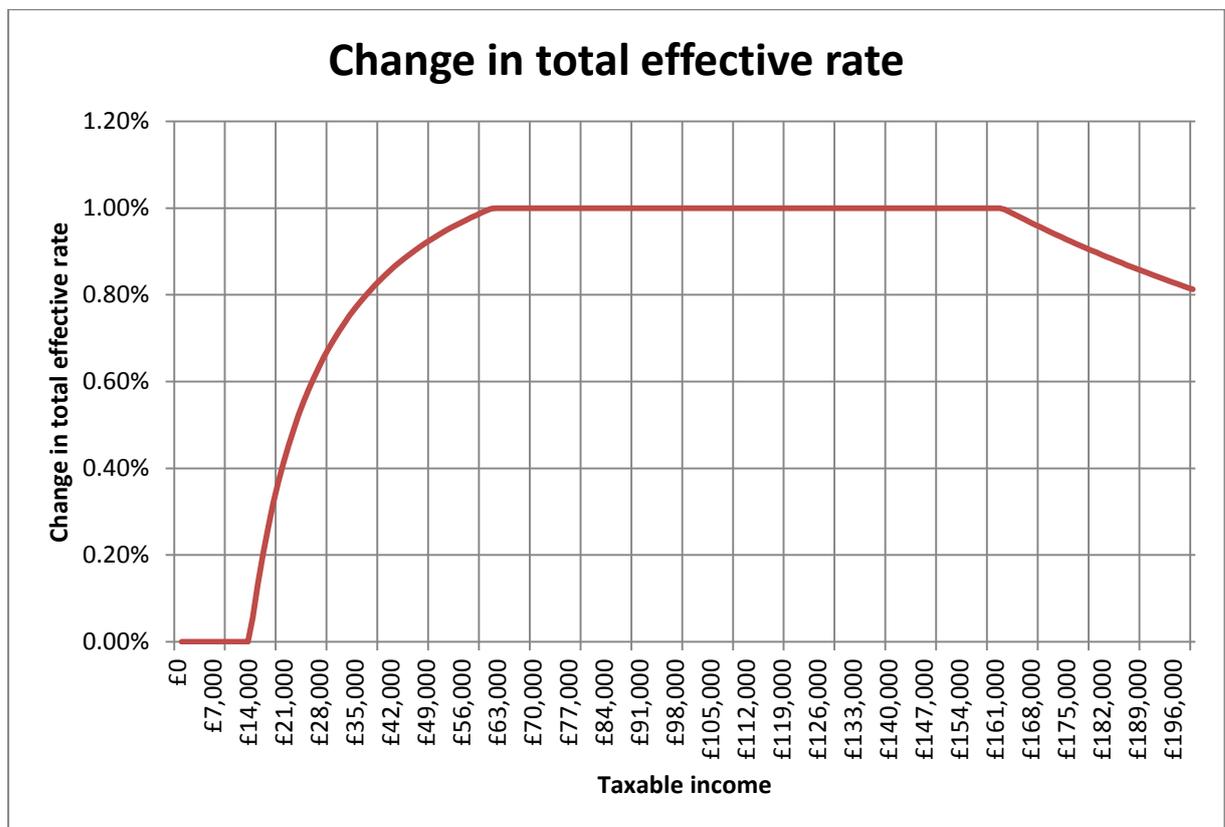
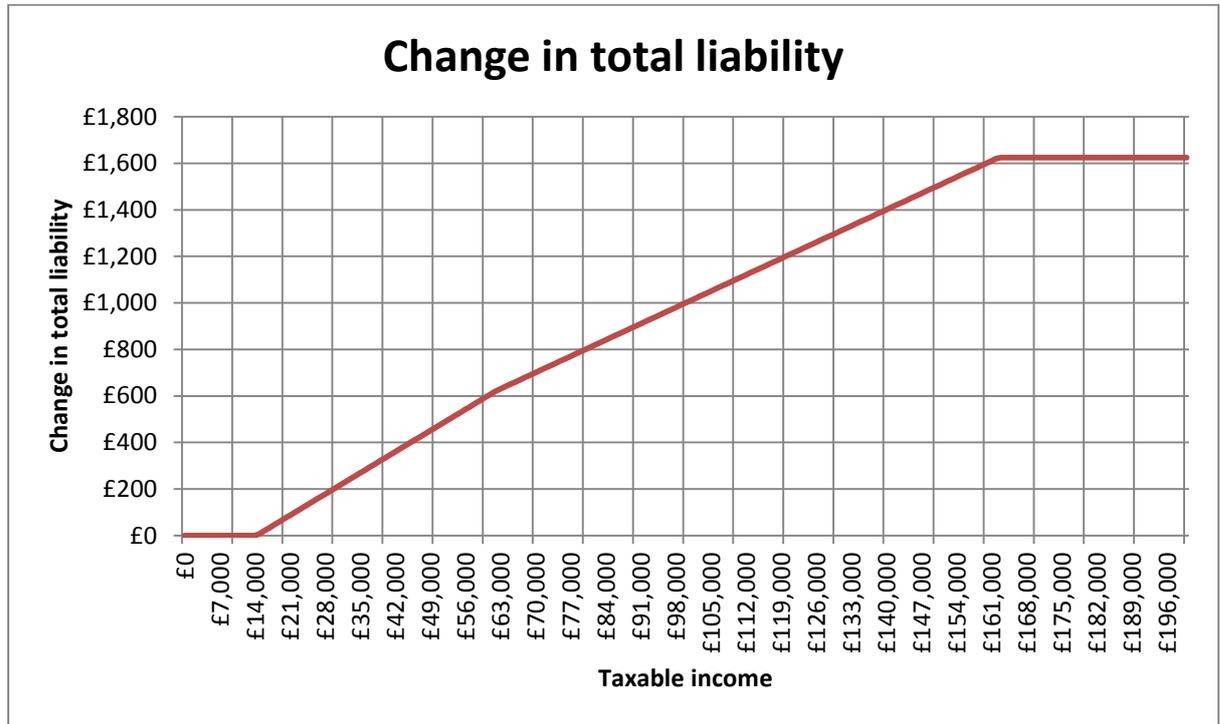
Option –introduce new LTC type charge

Option: introduce new LTC type charge

*Option: Introduce new LTC type charge at 1%: single person/working age – Long Term Care contributions*



Option: Introduce new LTC type charge at 1%: single person/working age – Overall tax position

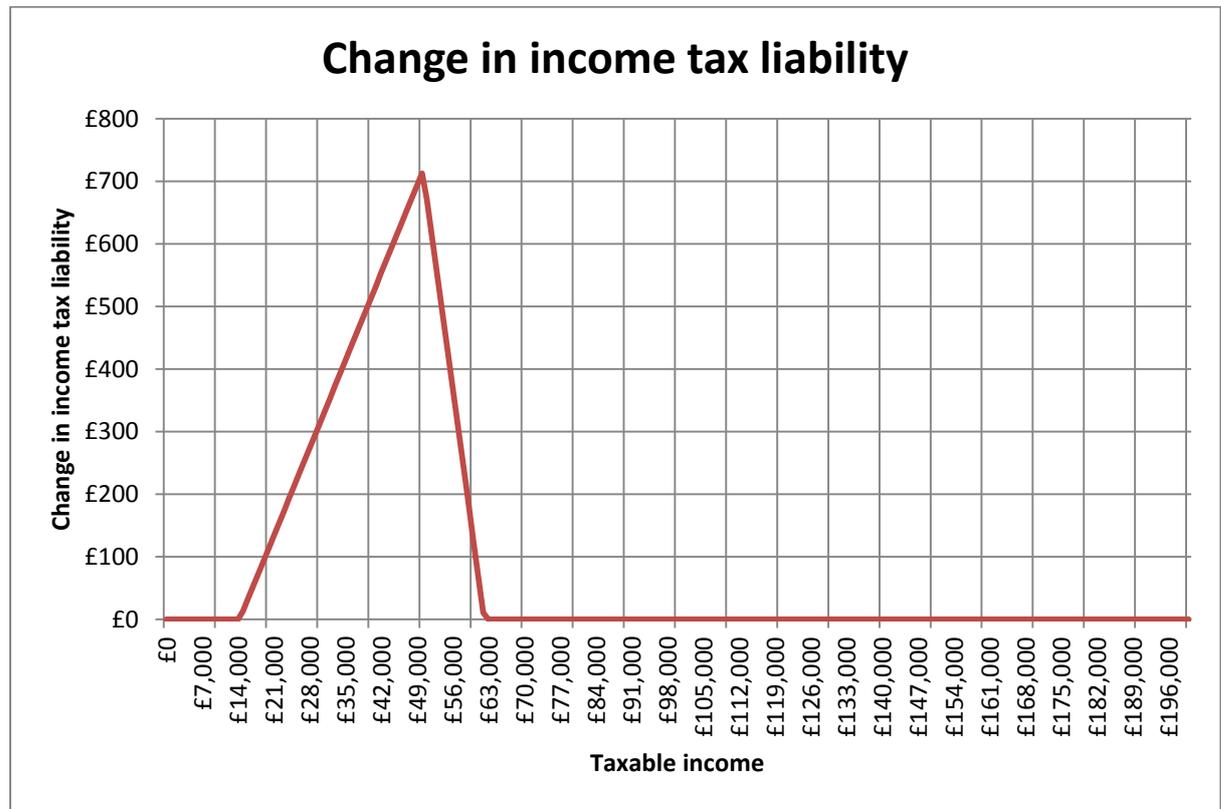


Household 1: single person – working age

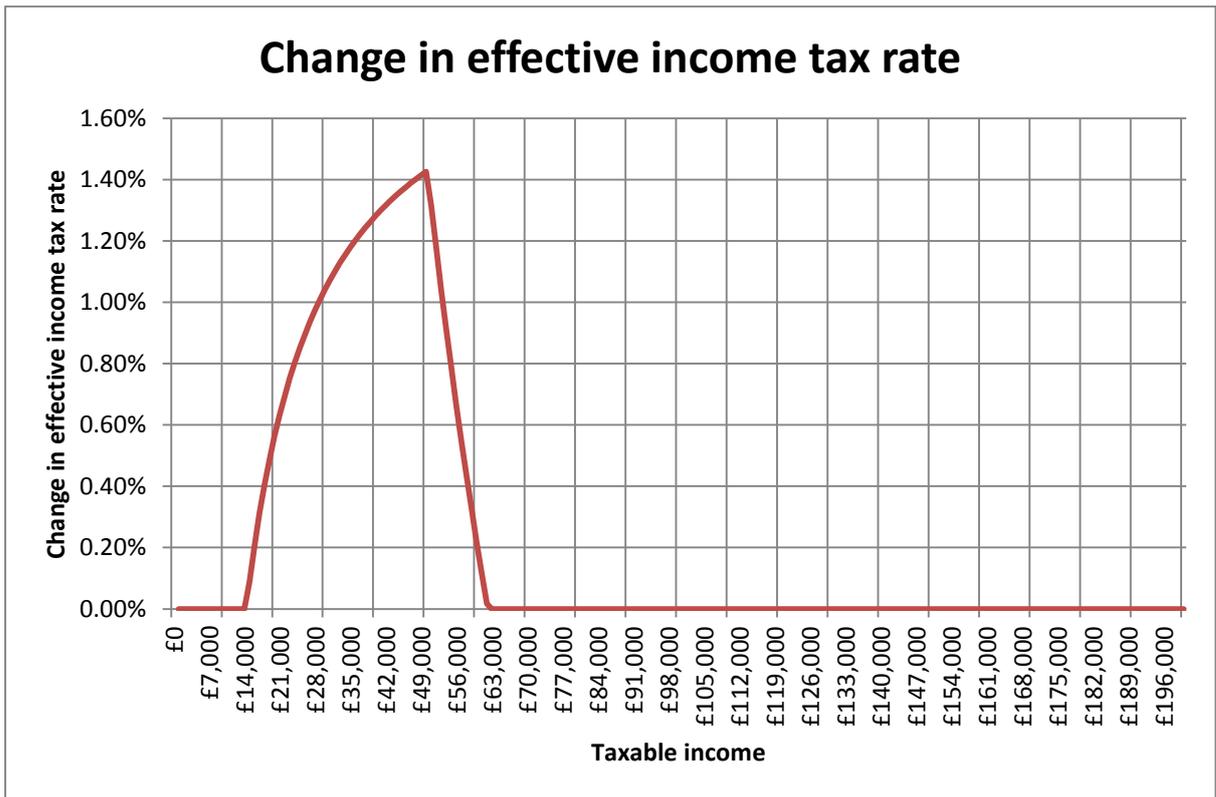
Option – increase marginal rate of income  
tax from 26% to 28%

Option: increase marginal rate of income tax from 26% to 28%<sup>21</sup>

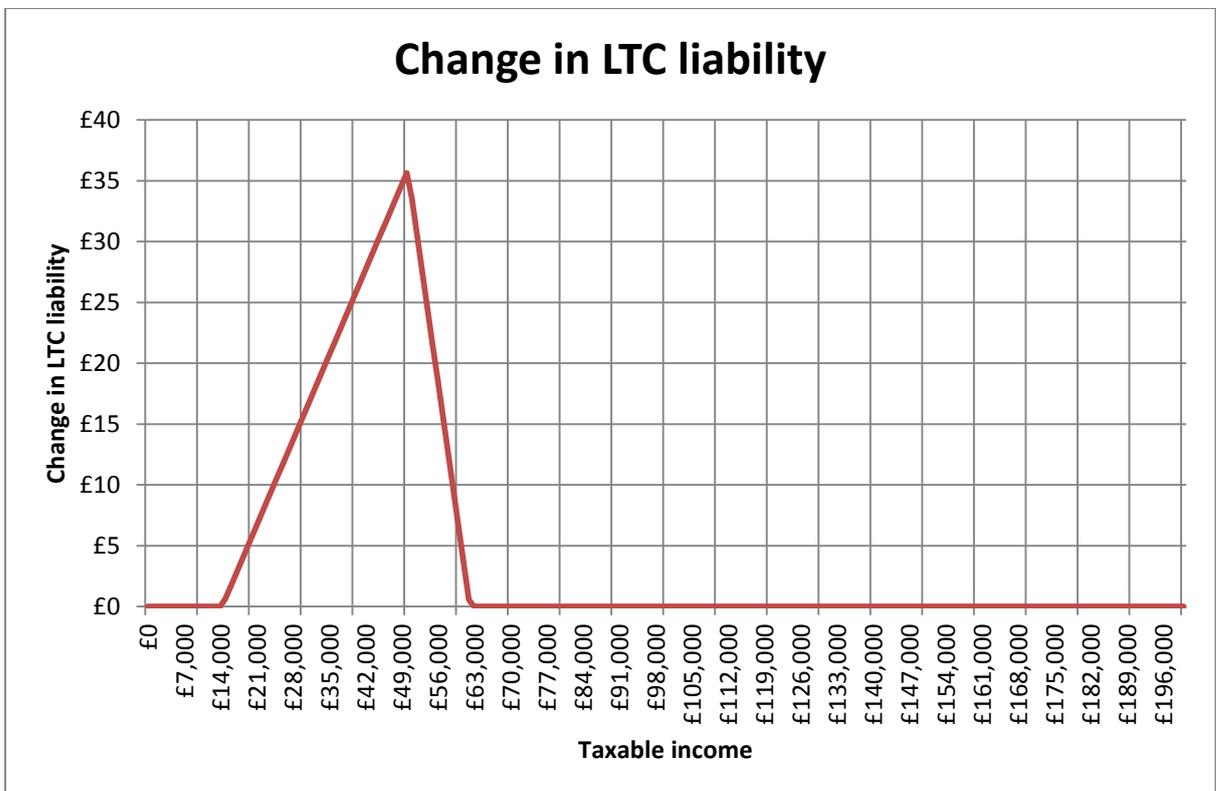
*Option: Increase MR of income tax by 2%: single person/working age – Income tax*

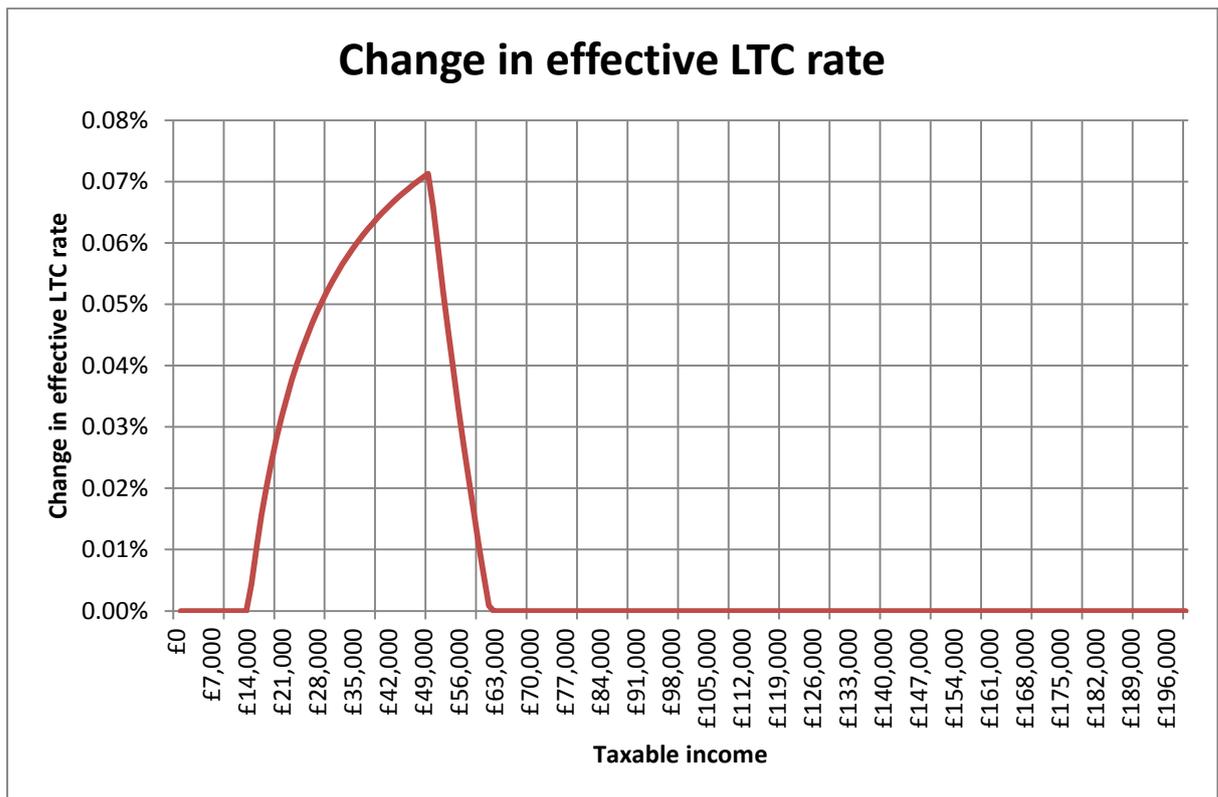


<sup>21</sup> Increasing the marginal rate of income tax to 28% will necessitate increasing the marginal rate of long term care contributions to 1.4%. The two marginal rates are interlinked.

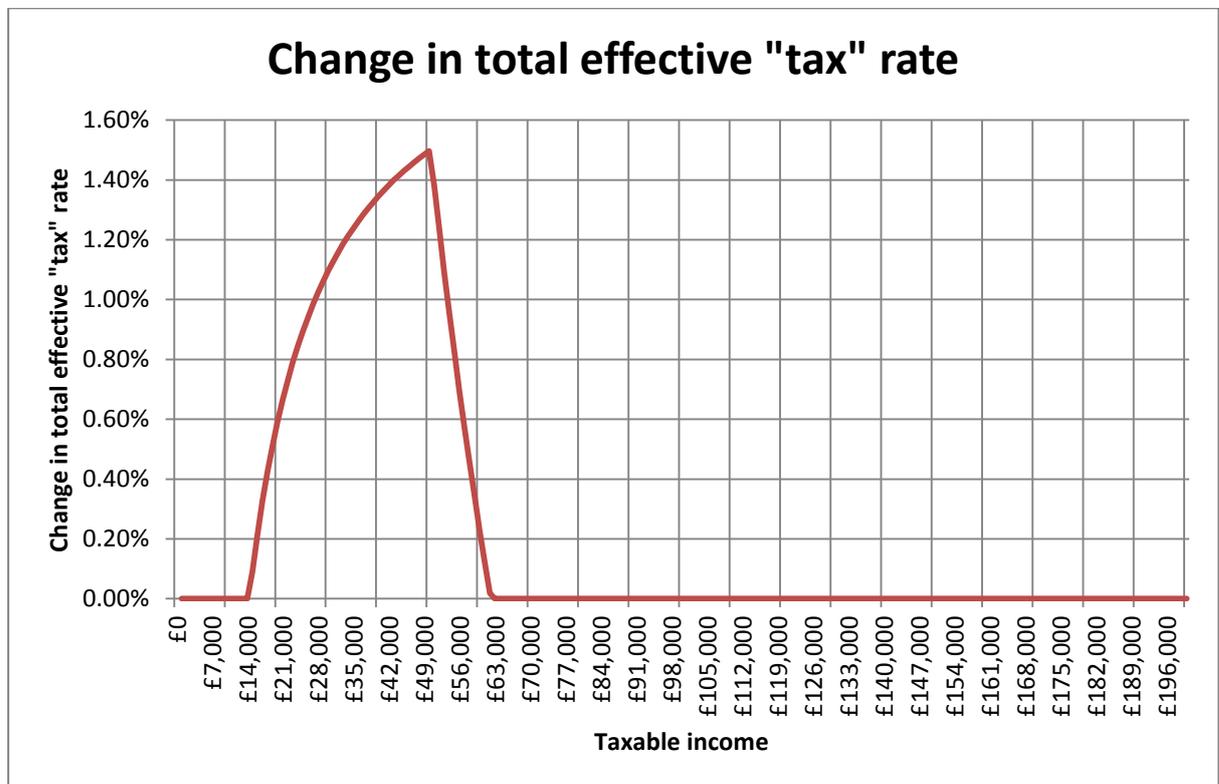
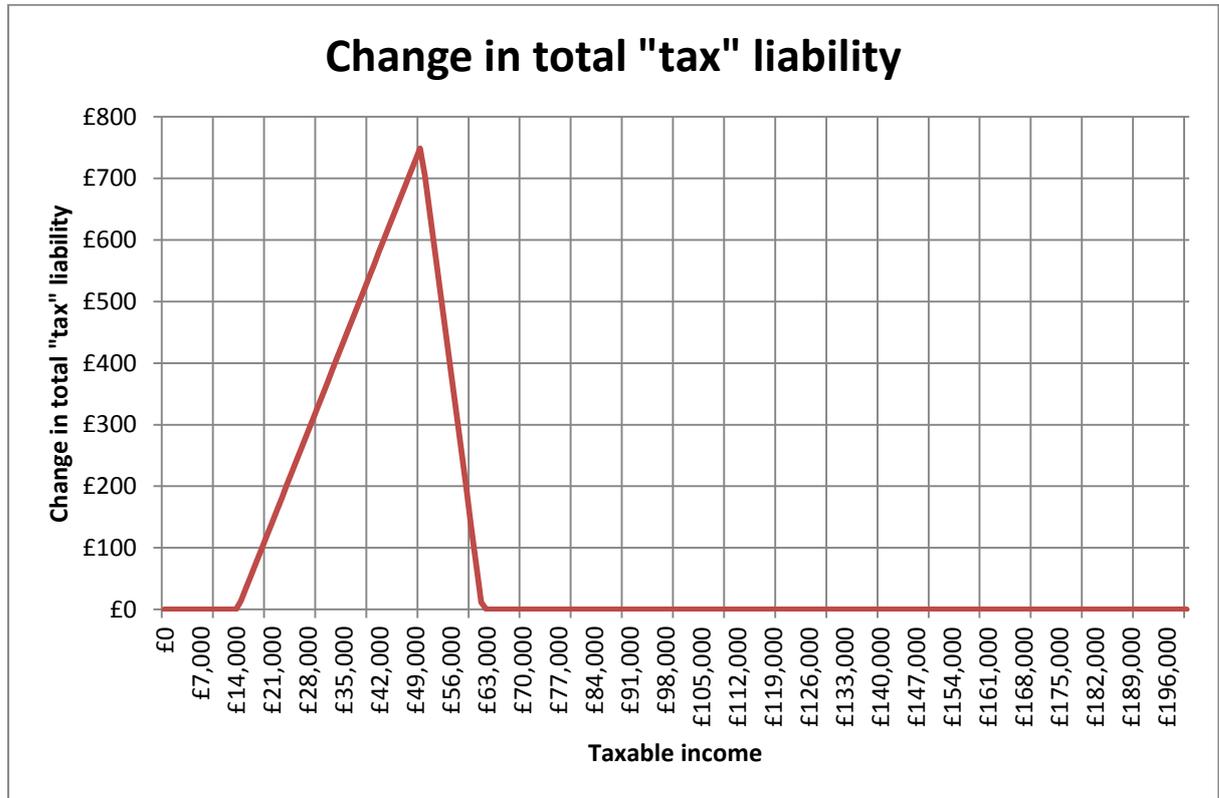


Option: Increase MR of income tax by 2%: single person/working age – Long term care contributions





Option: Increase MR of income tax by 2%: single person/working age – Overall tax position

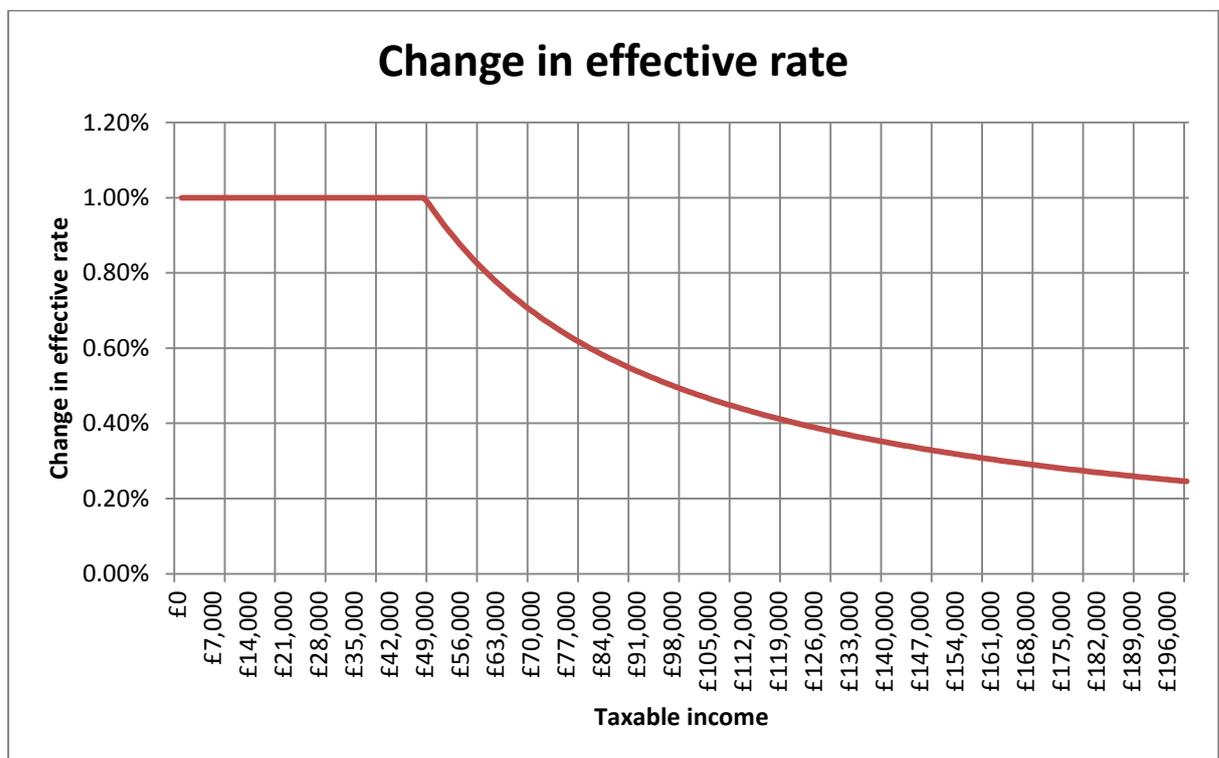
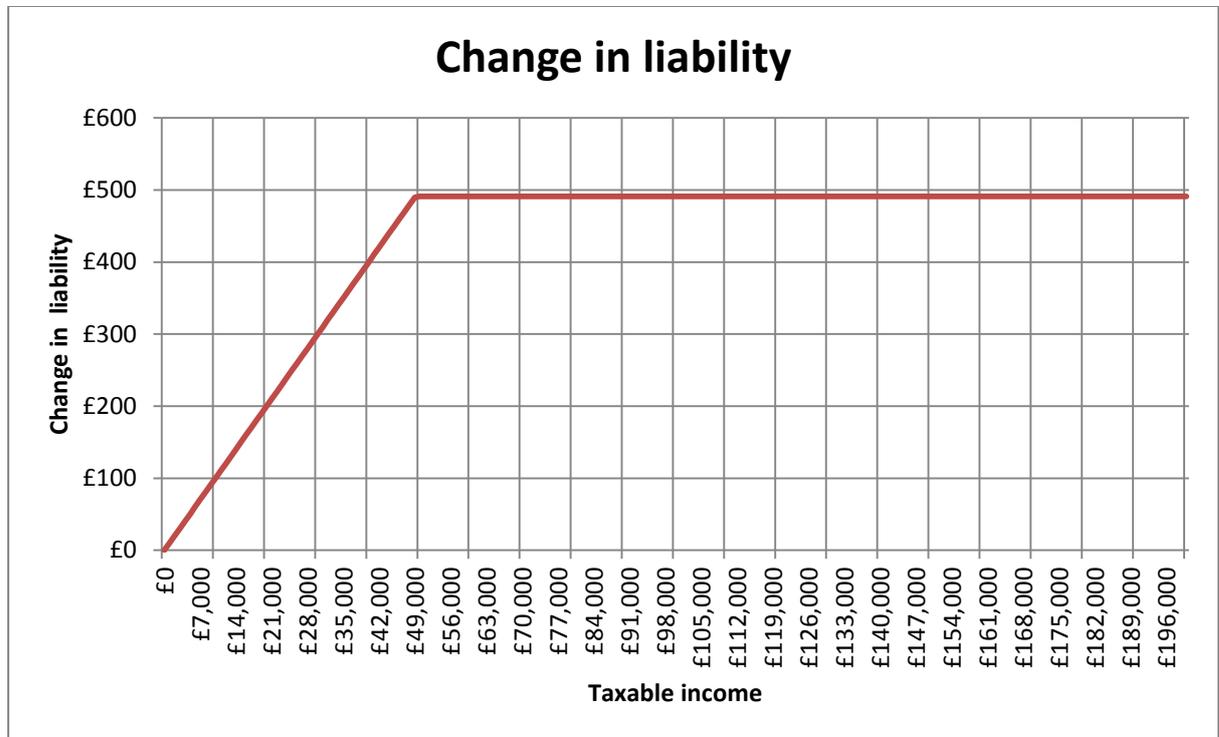


## Household 1: single person – working age

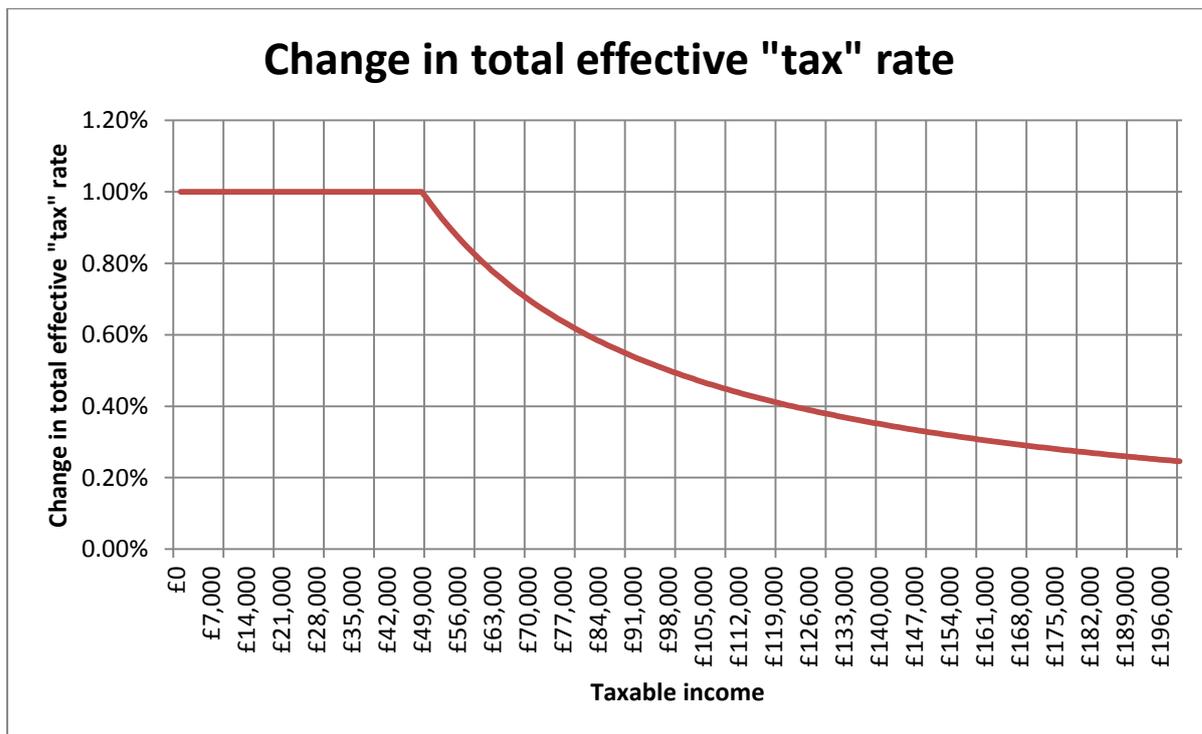
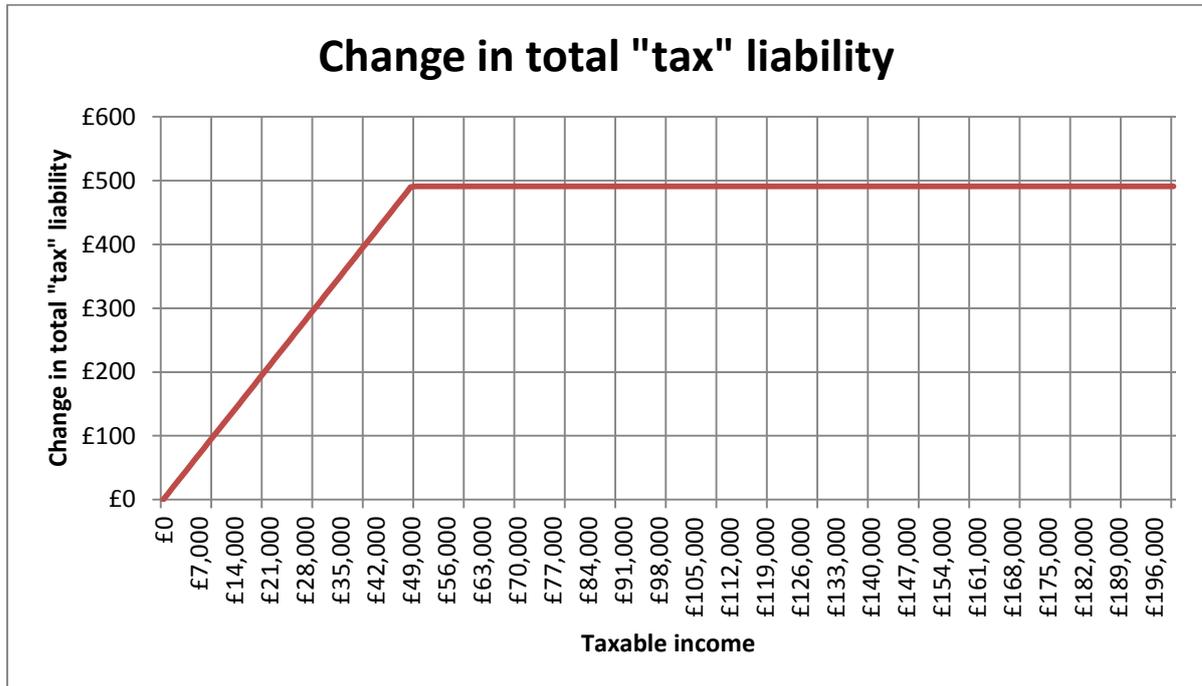
Option – introduce social security type charge below the standard earnings limit

Option: introduce social security type charge below the standard earnings limit

*Option: Introduce SS type charge below SEL by 1%: single person/working age – Social Security contributions*



Option: Introduce SS type charge below SEL by 1%: single person/working age – Overall tax position

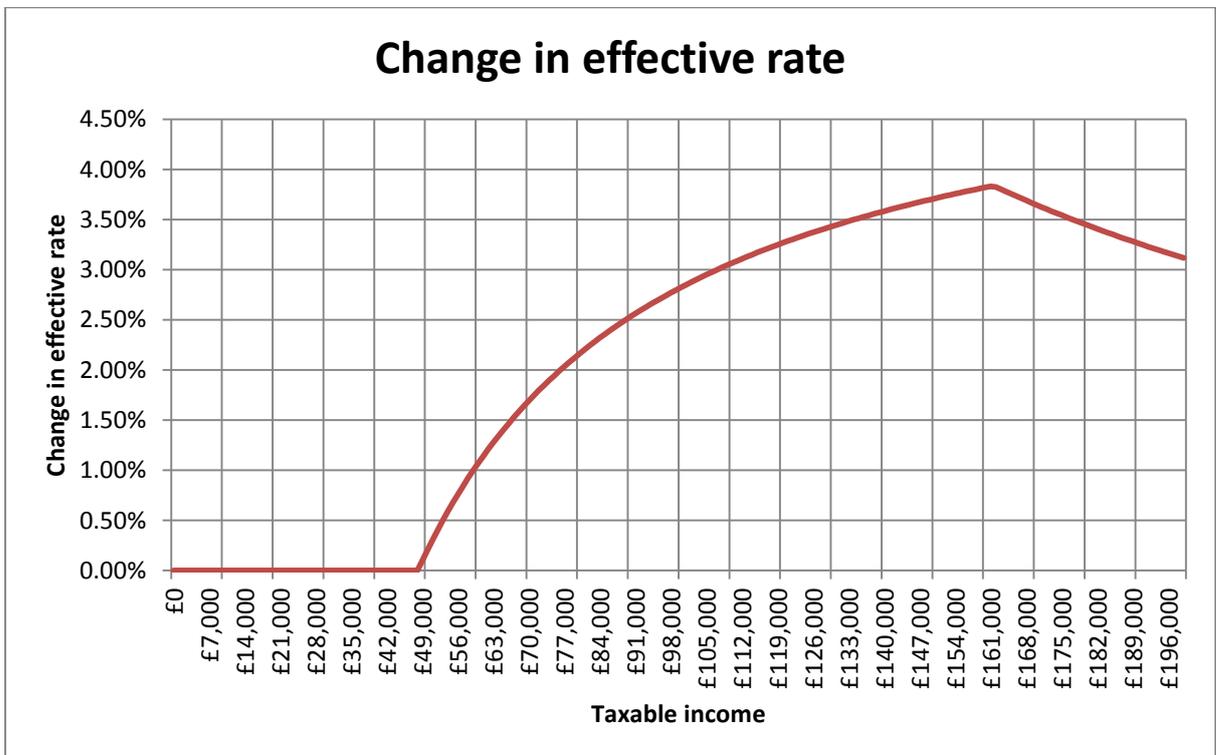
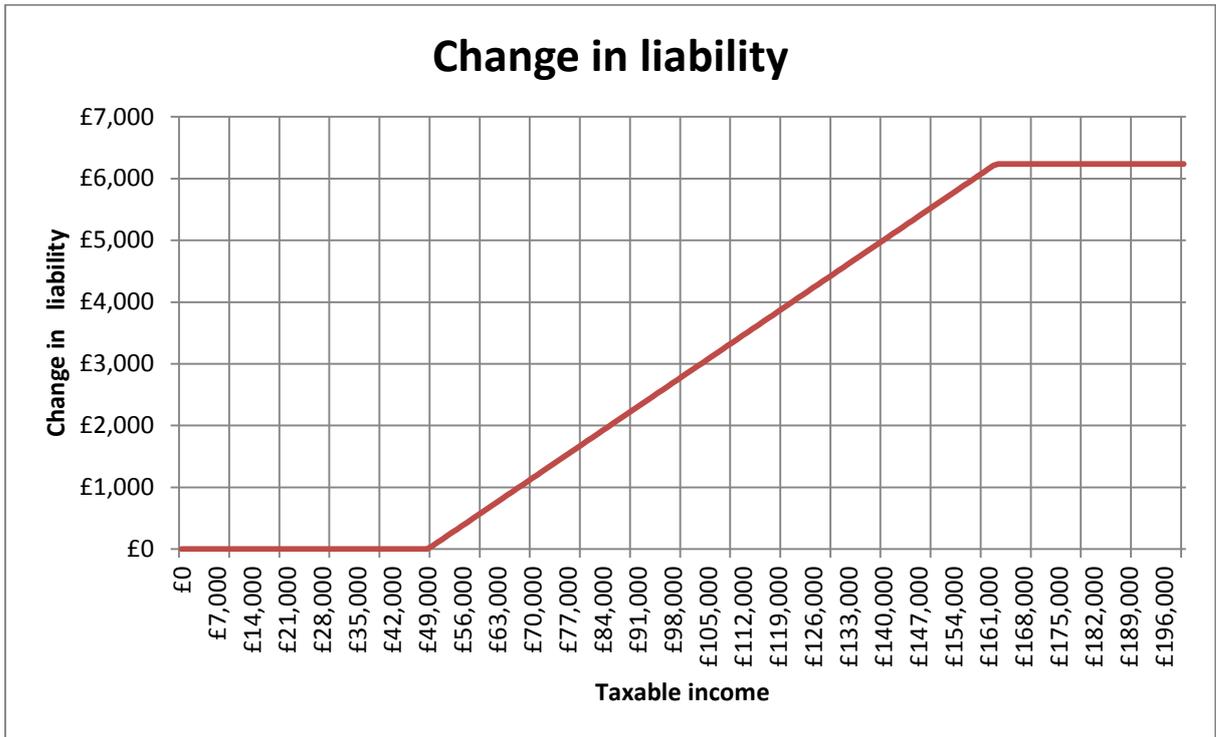


## Household 1: single person – working age

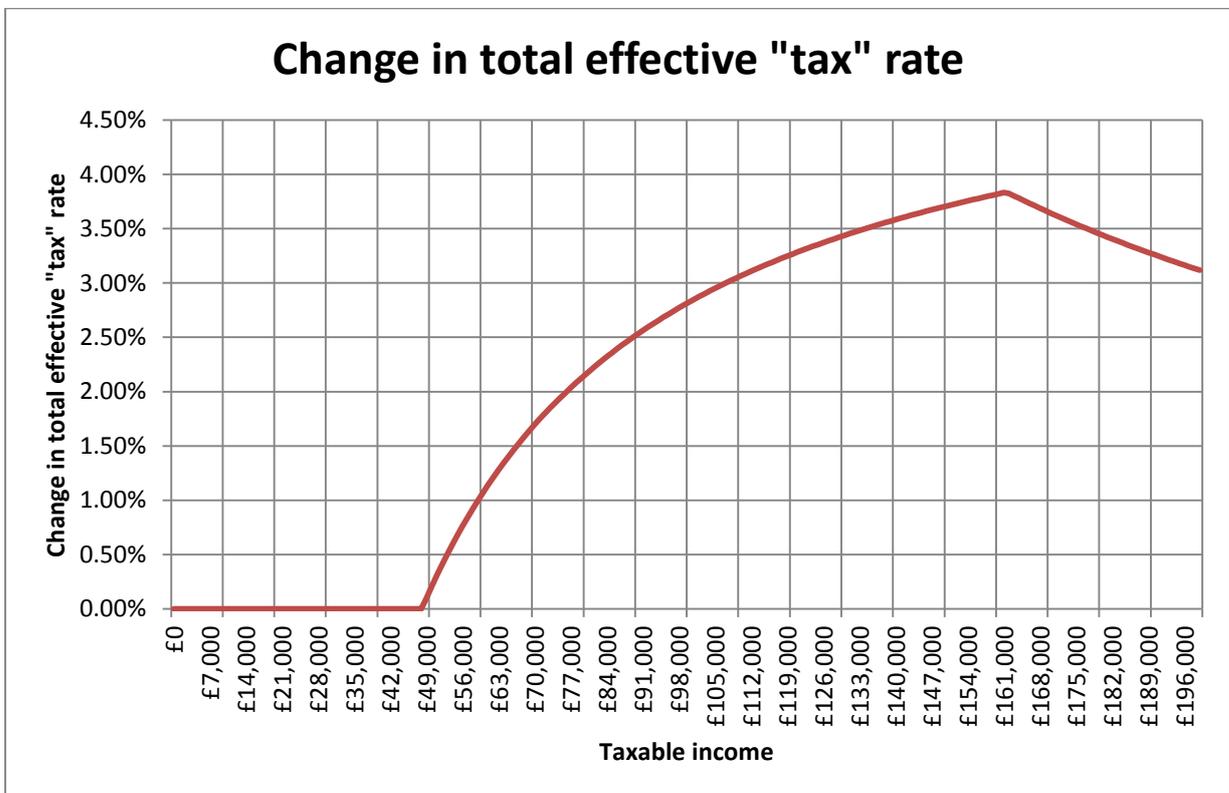
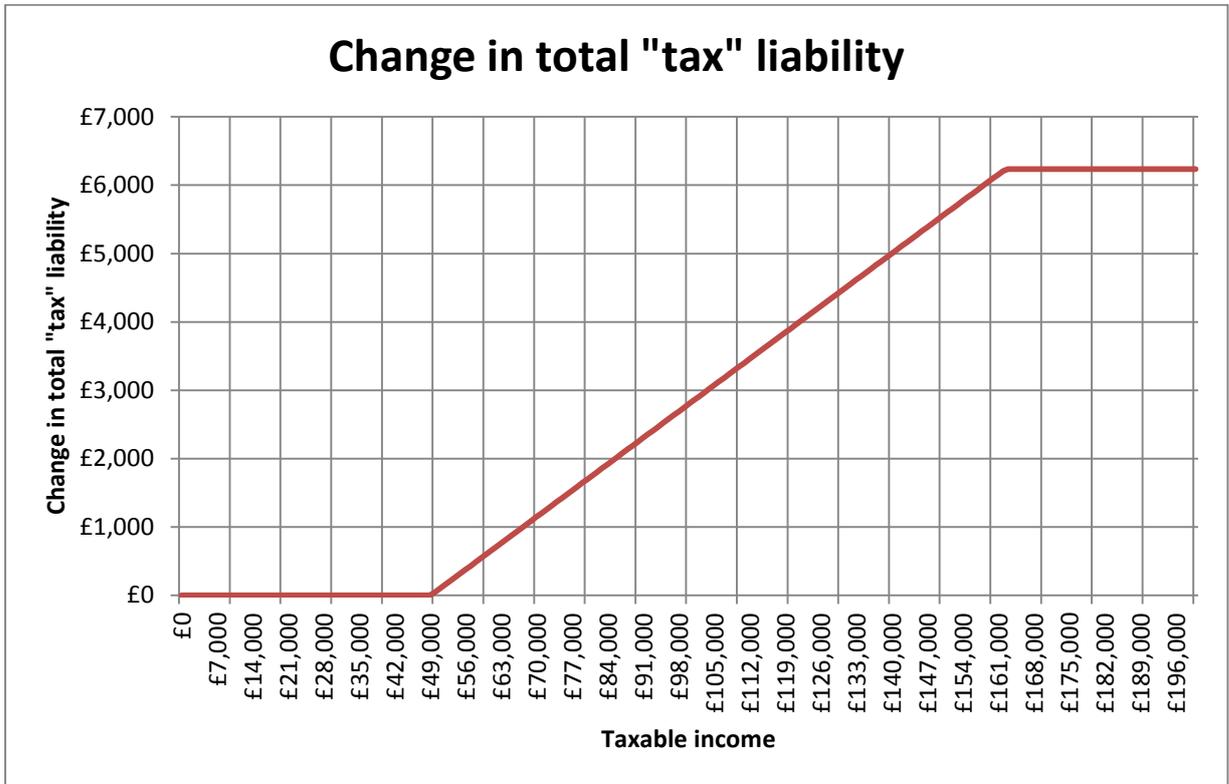
Option – introduce social security type charge above the standard earnings limit

Option: increase Social Security contributions above the standard earnings limit

Option: Introduce SS type charge above SEL of 5.5%: single person/working age



Option: Introduce SS type charge above SEL of 5.5%: single person/working age –  
 Overall tax position

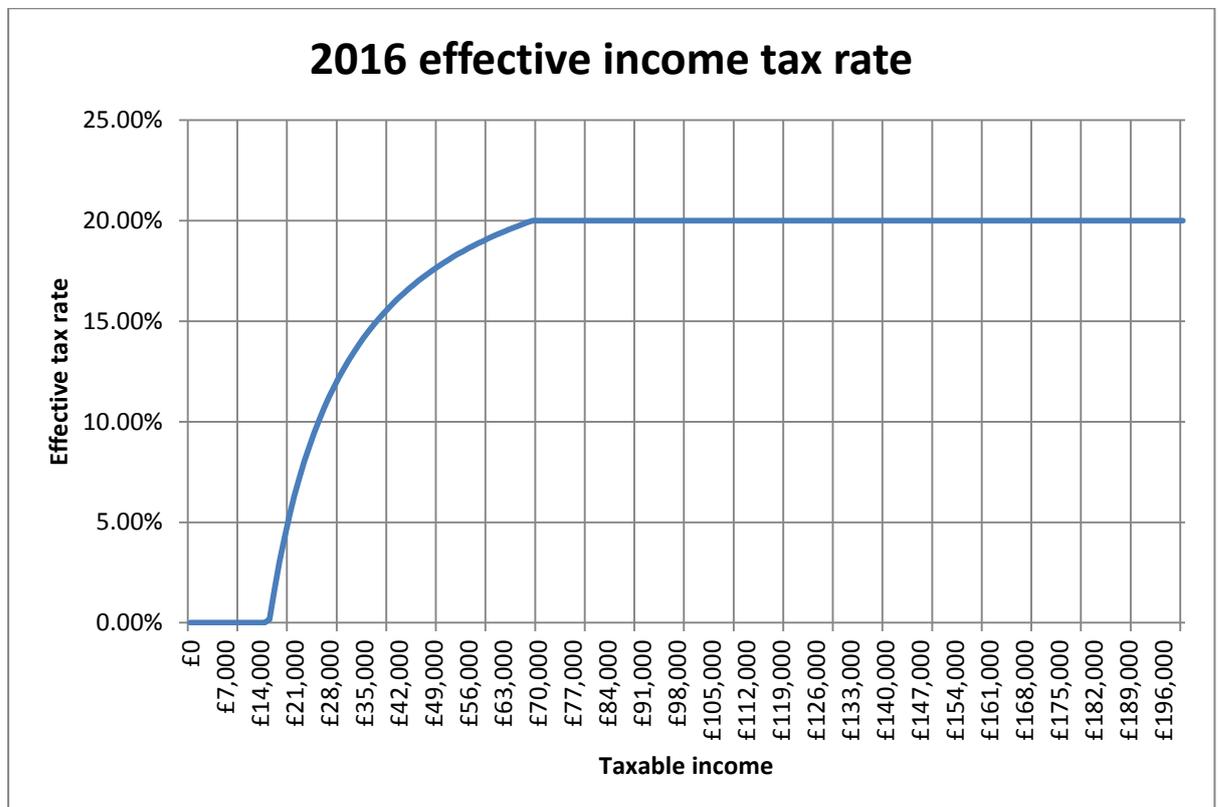
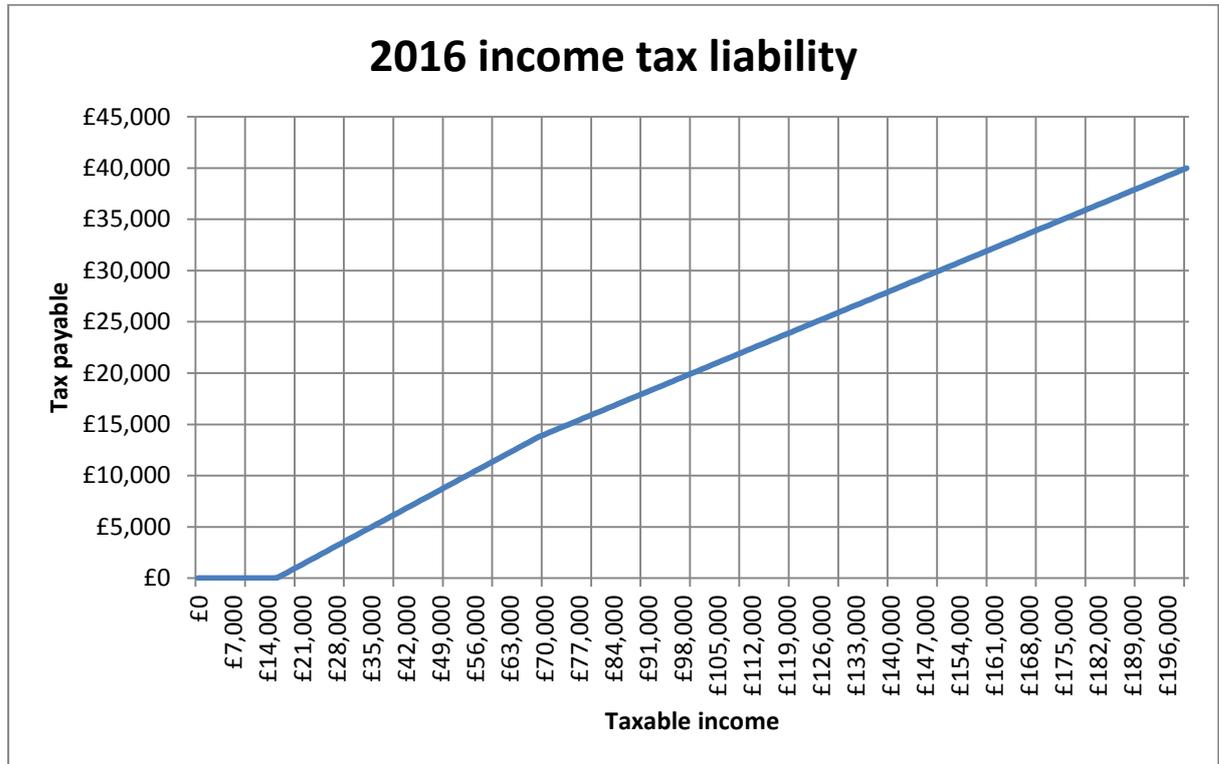


## Household 2: single person – 65+

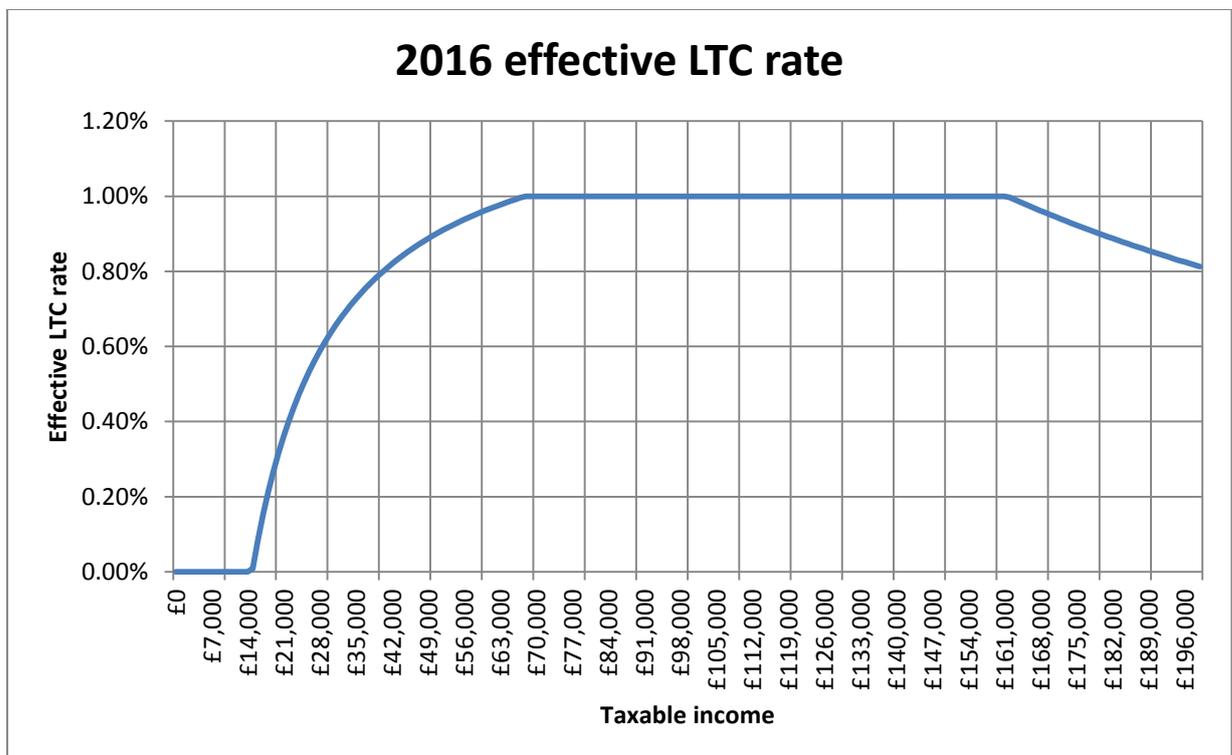
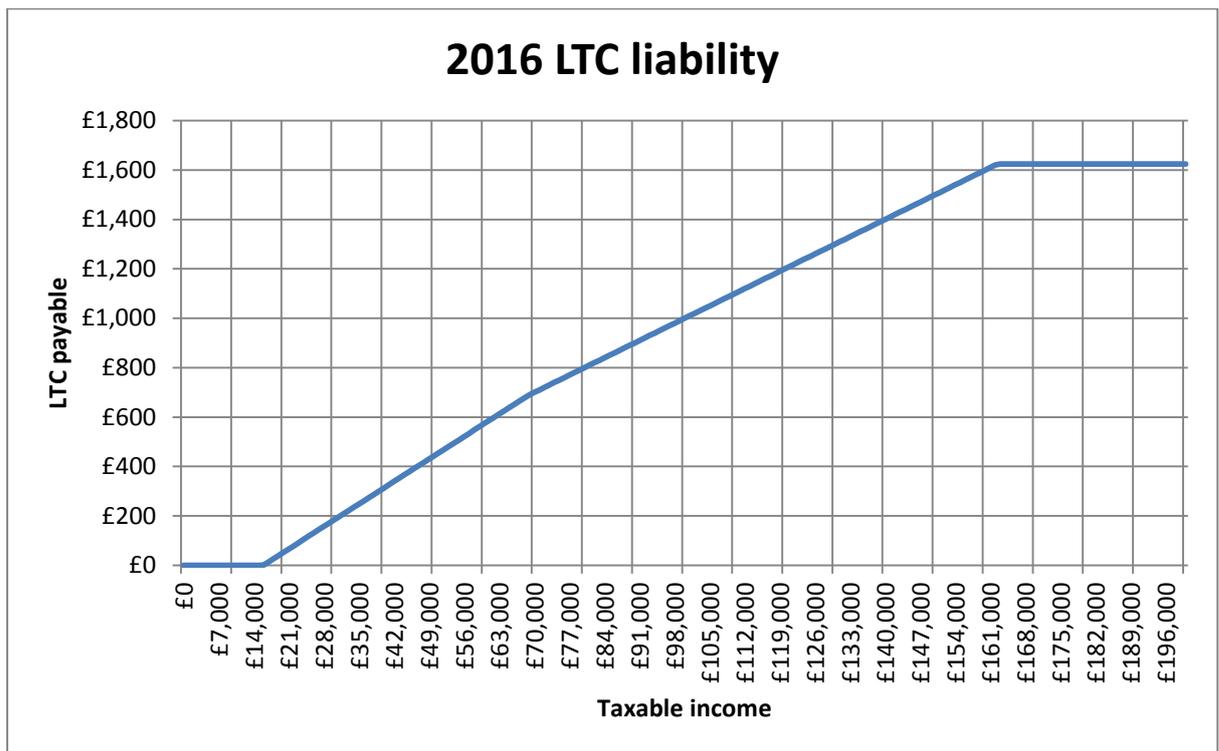
### 2016 Baseline Analysis

Baseline for 2016 year of assessment

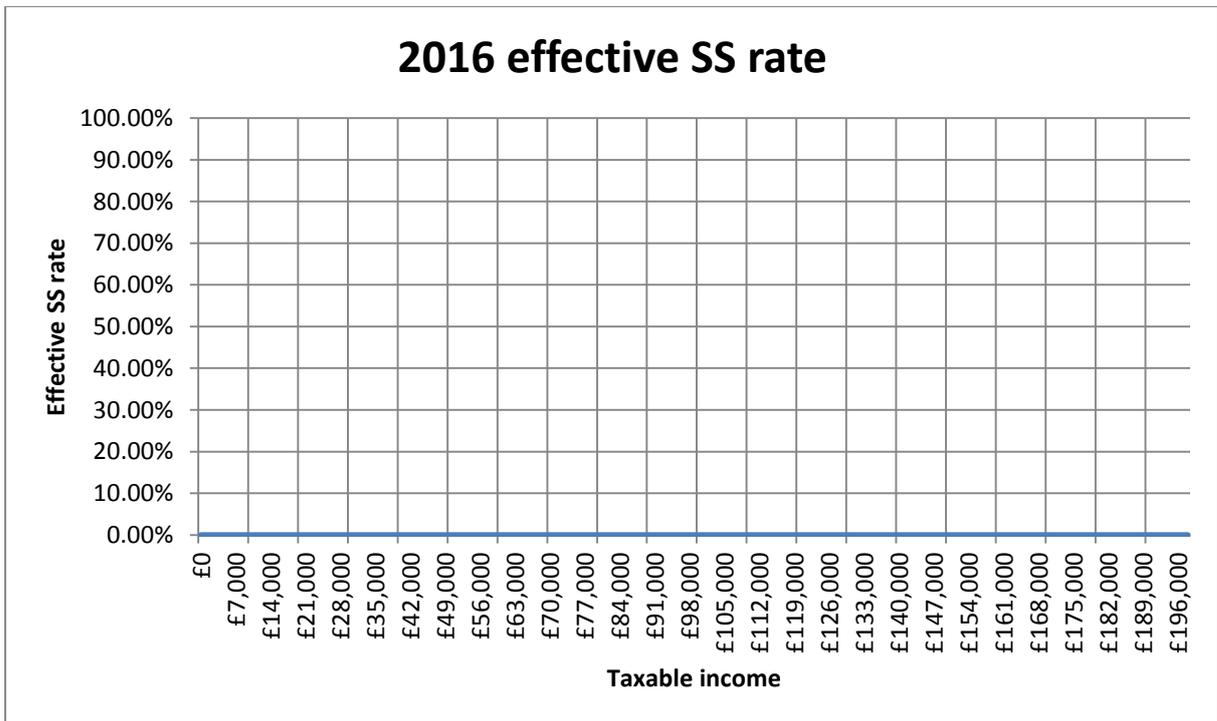
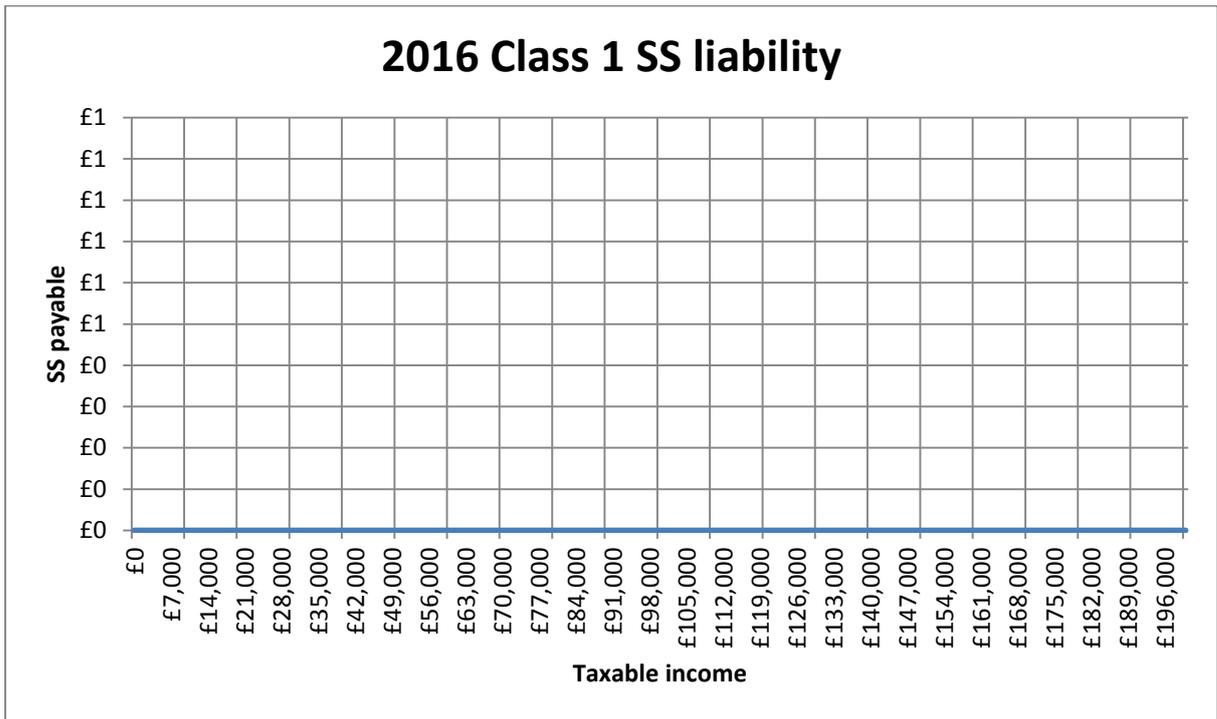
2016 Baseline: single person/65+ – Income tax



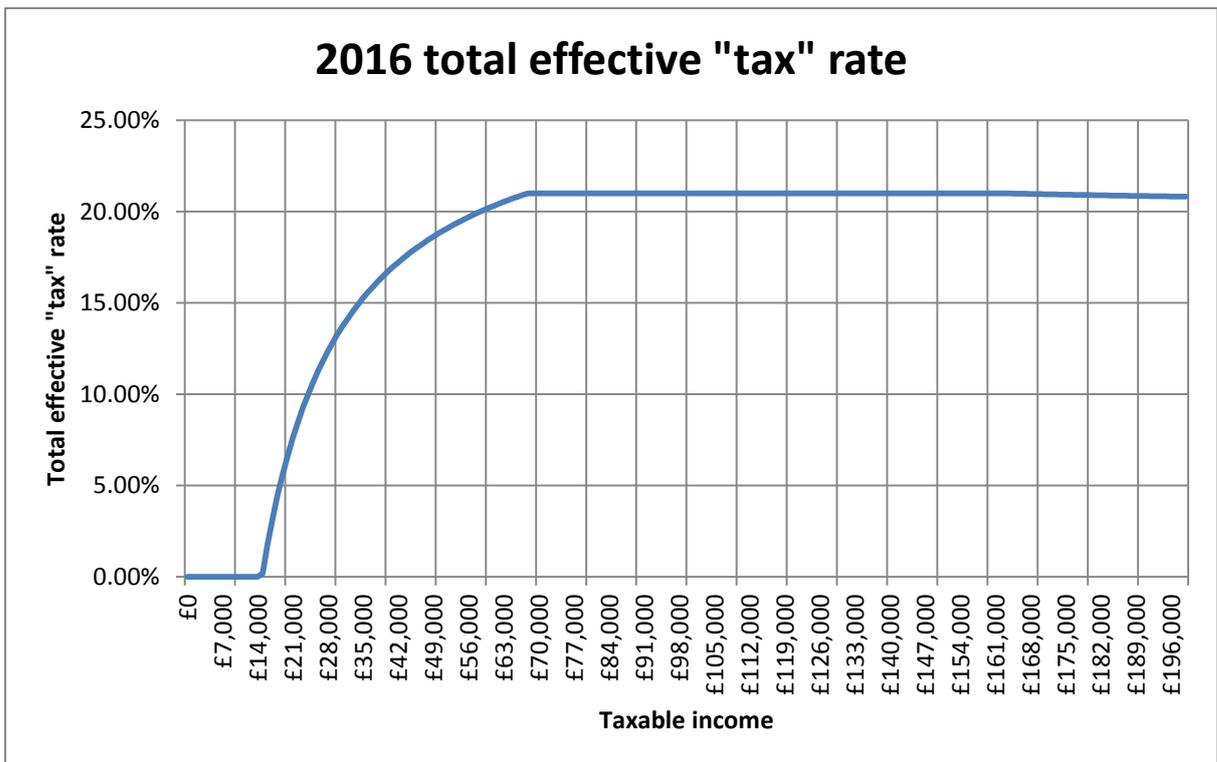
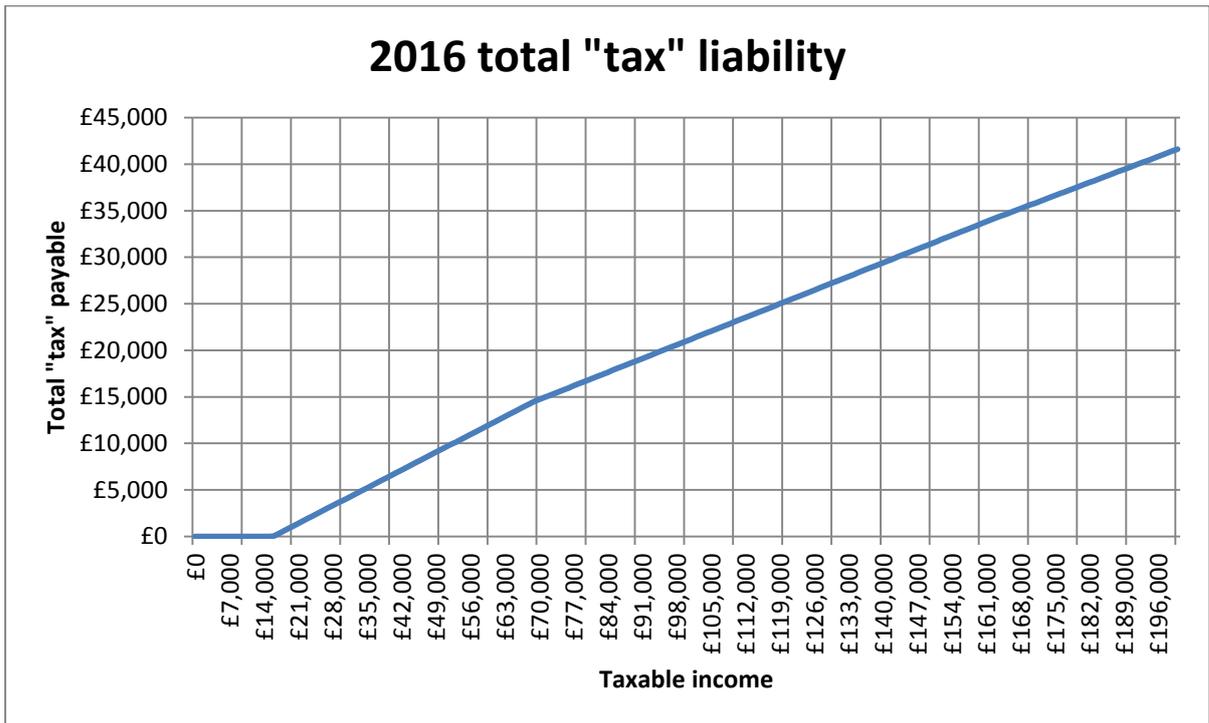
2016 Baseline: single person/65+ – Long term care contribution



2016 Baseline: single person/65+ – Social Security contributions



2016 Baseline: single person/65+ – Overall tax position

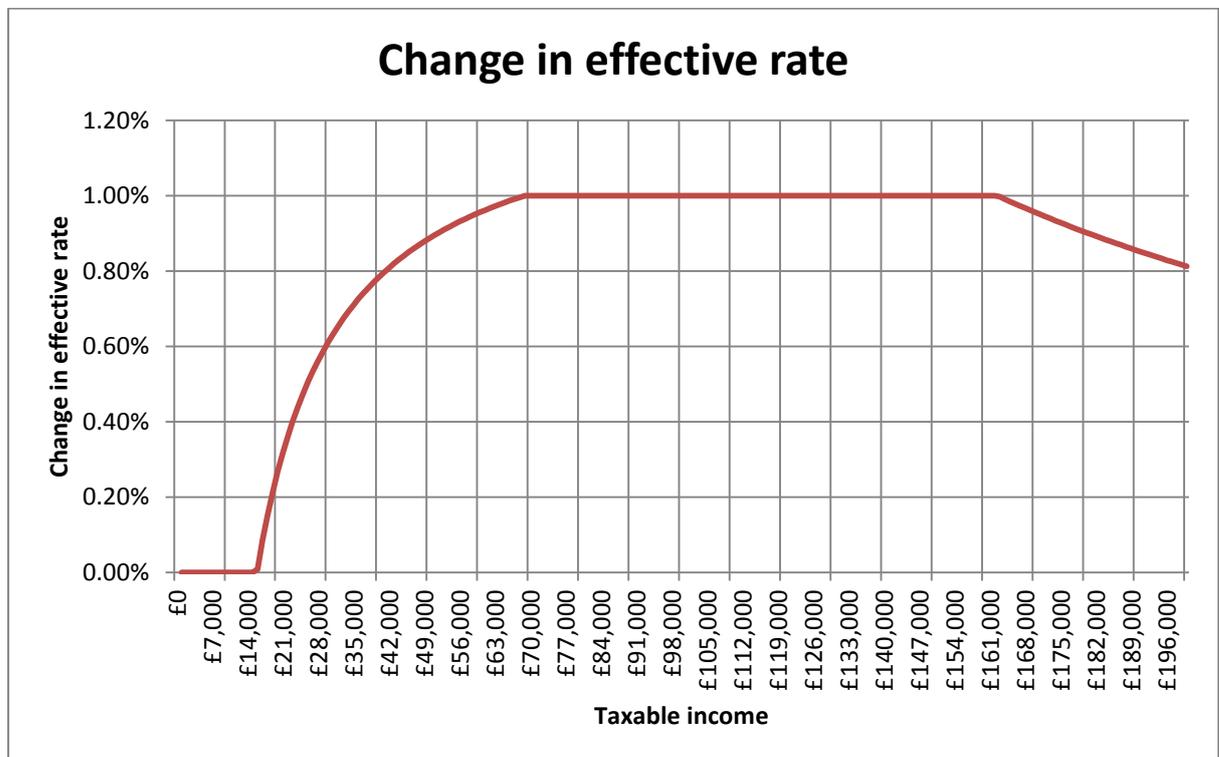
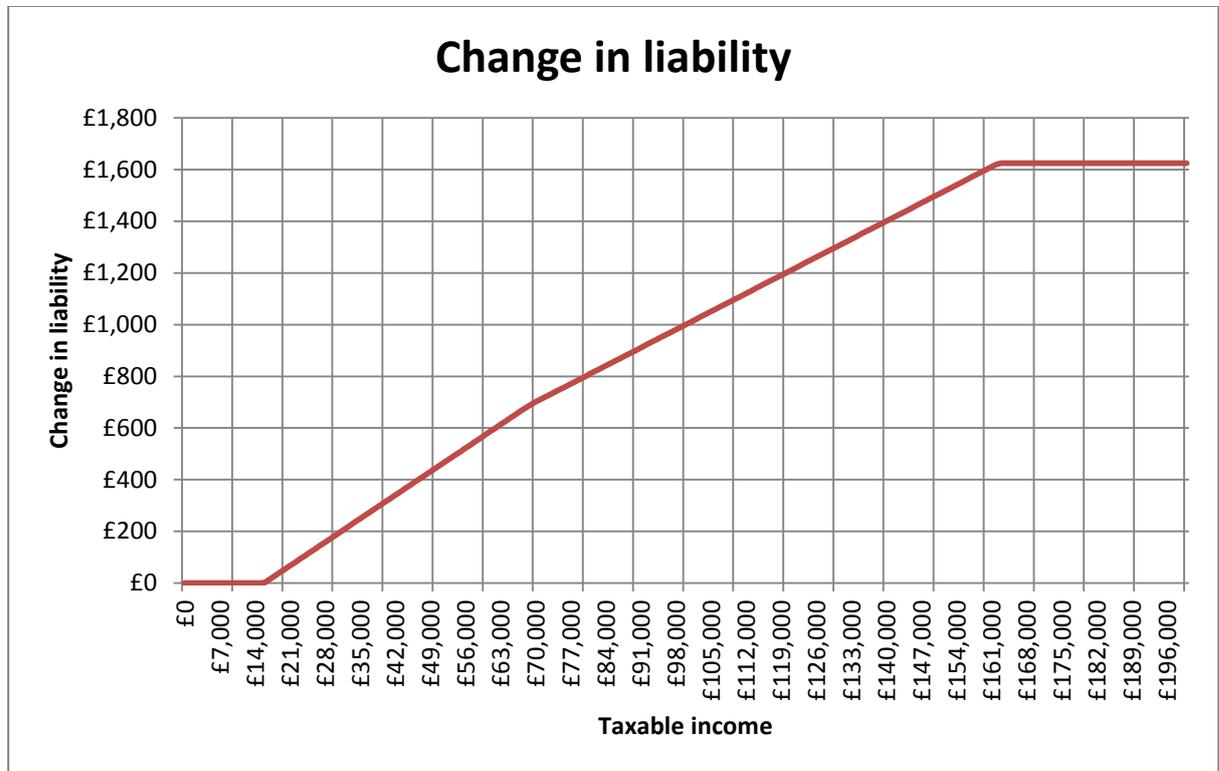


## Household 2: single person – 65+

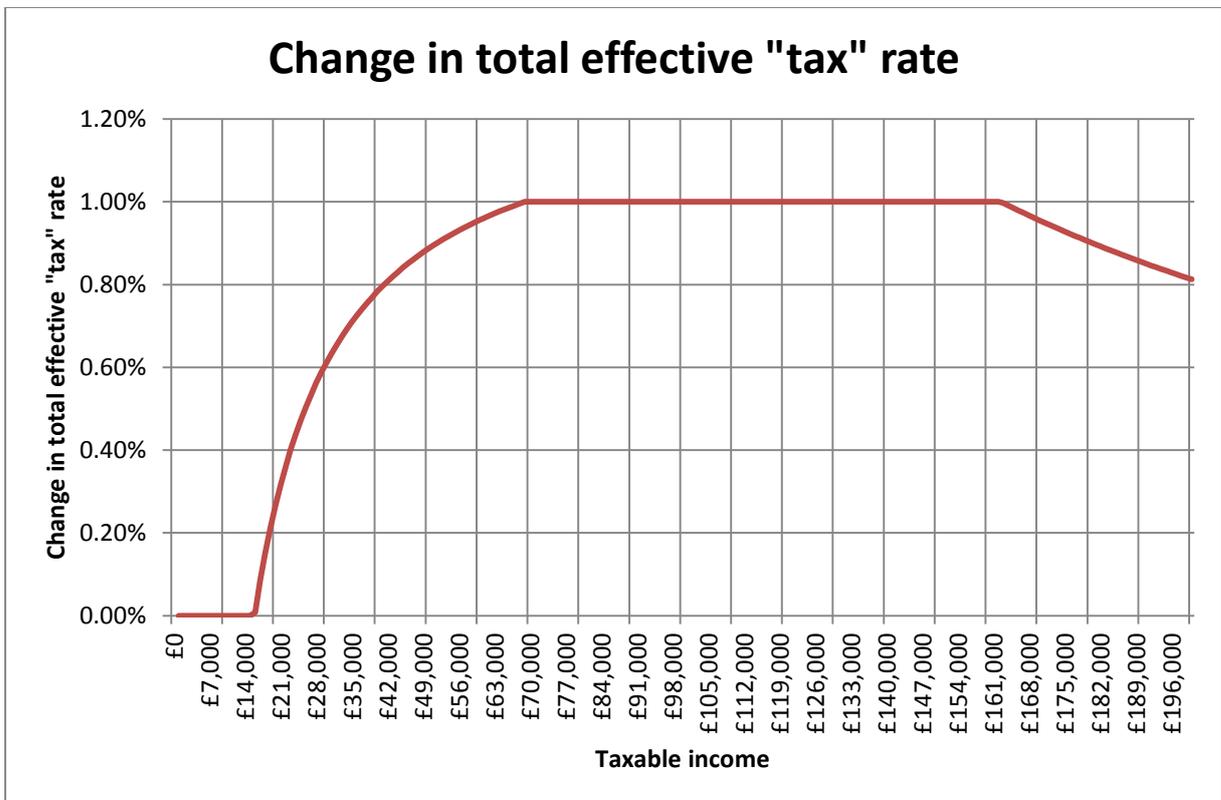
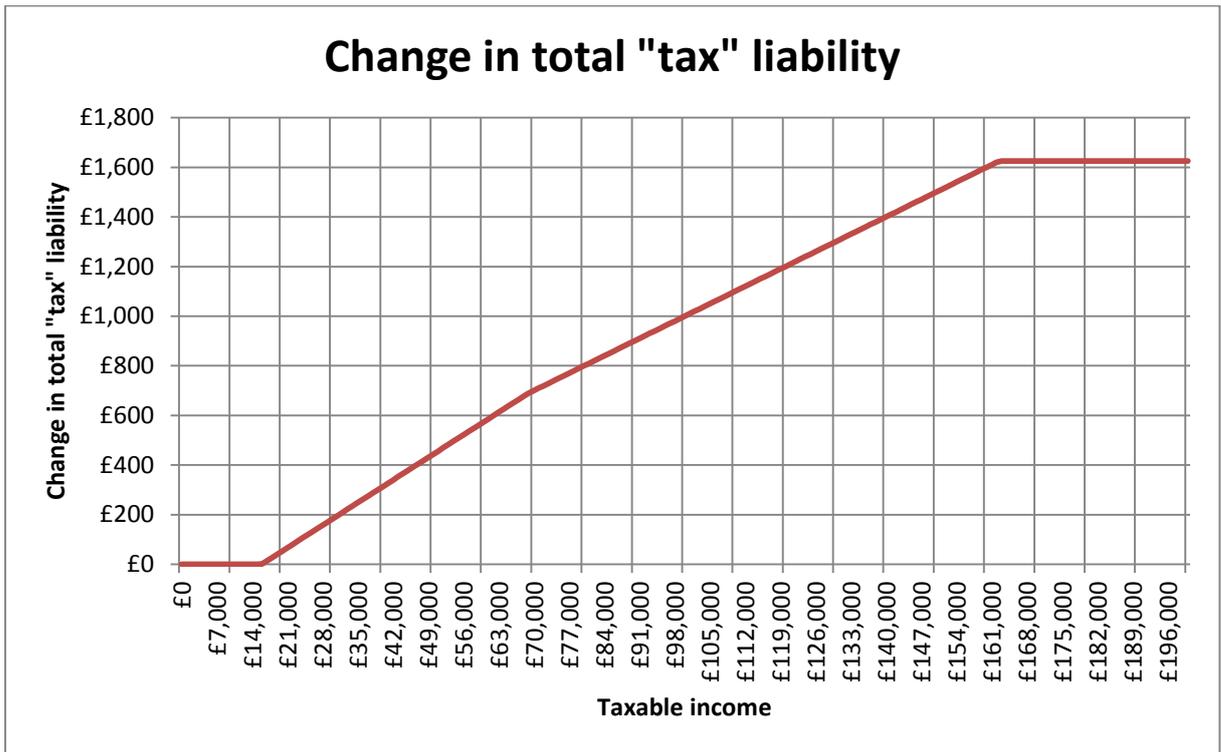
Option –introduce new LTC type charge

Option: introduce new LTC type charge

Option: Introduce new LTC type charge at 1%: single person/65+ – Long Term Care contributions



Option: Introduce new LTC type charge at 1%: single person/65+ – Overall tax position

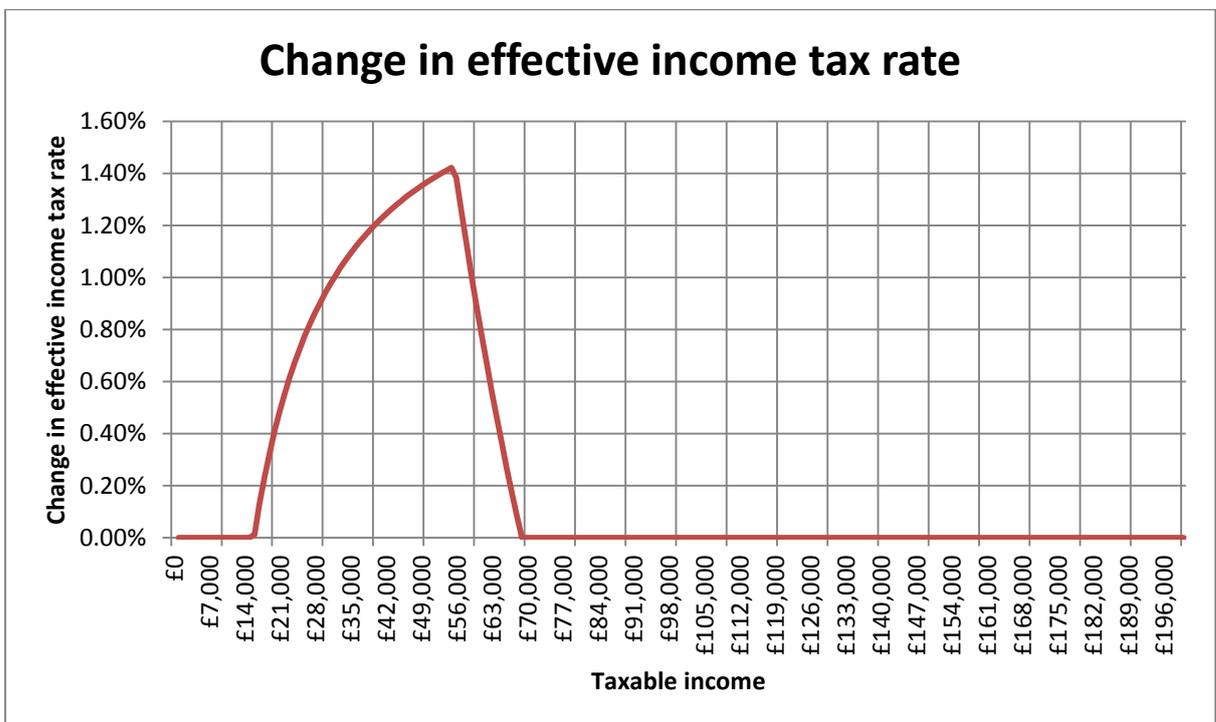
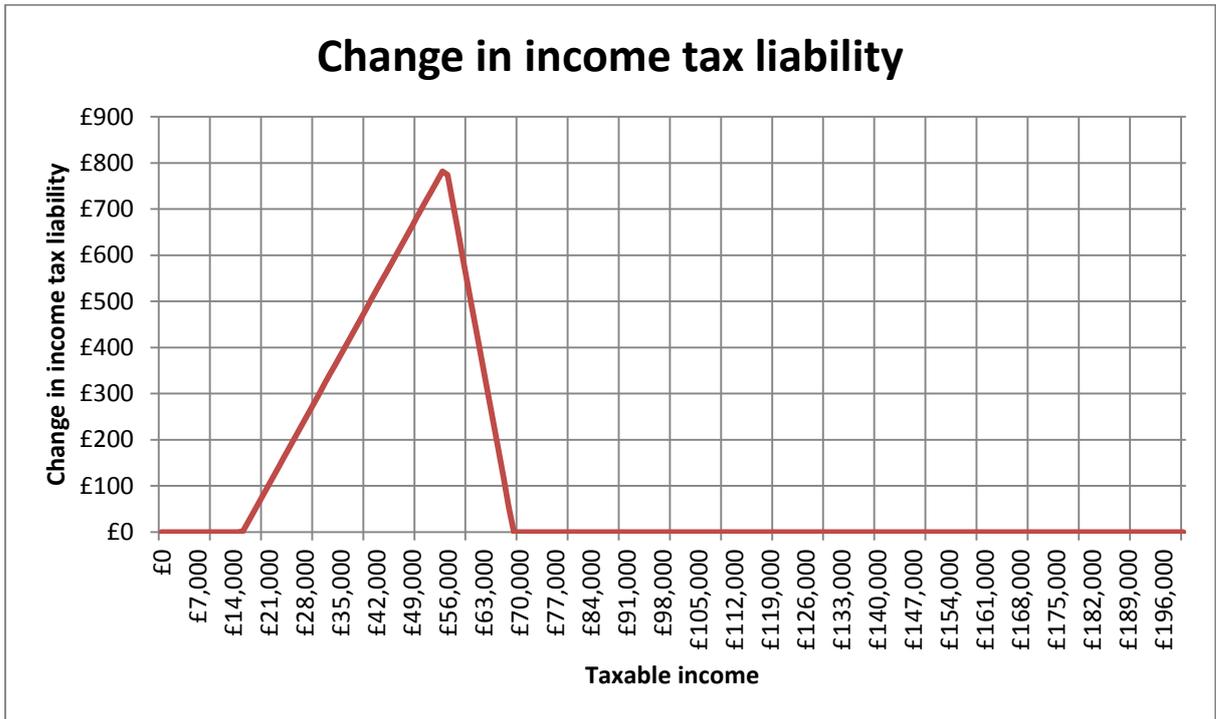


## Household 2: single person – 65+

Option – increase marginal rate of income tax from 26% to 28%

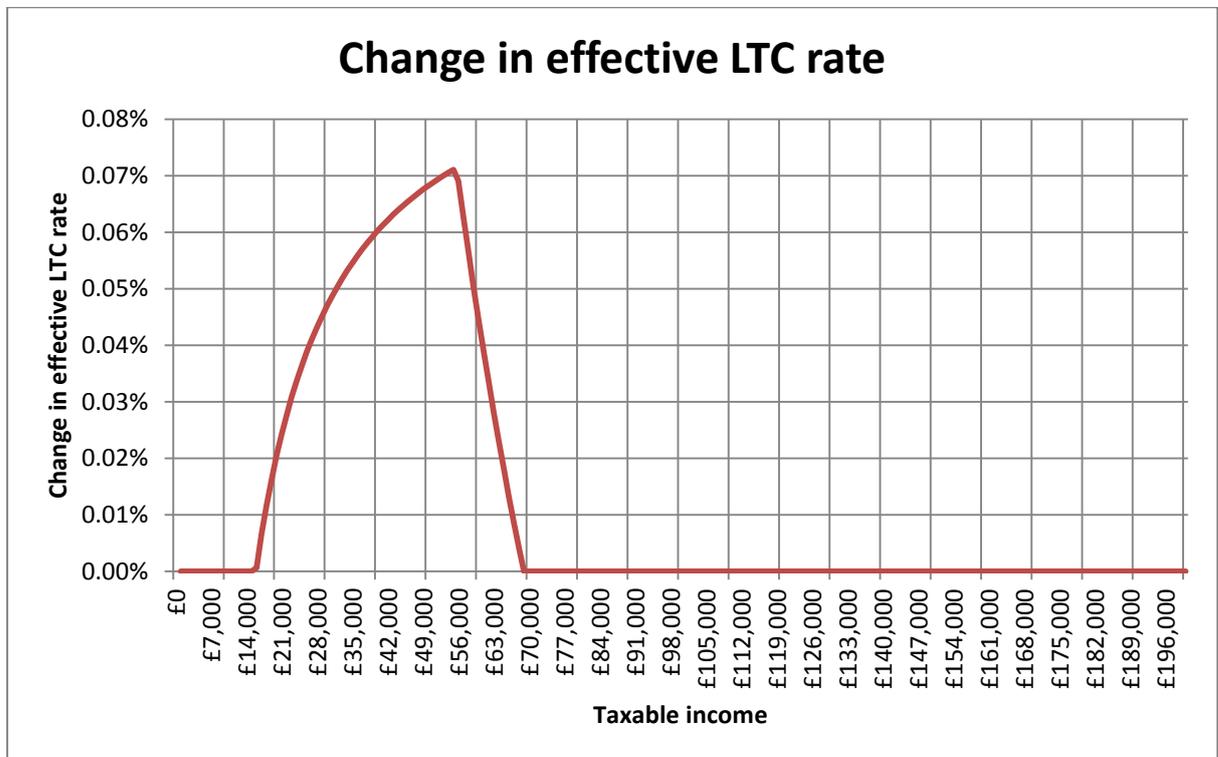
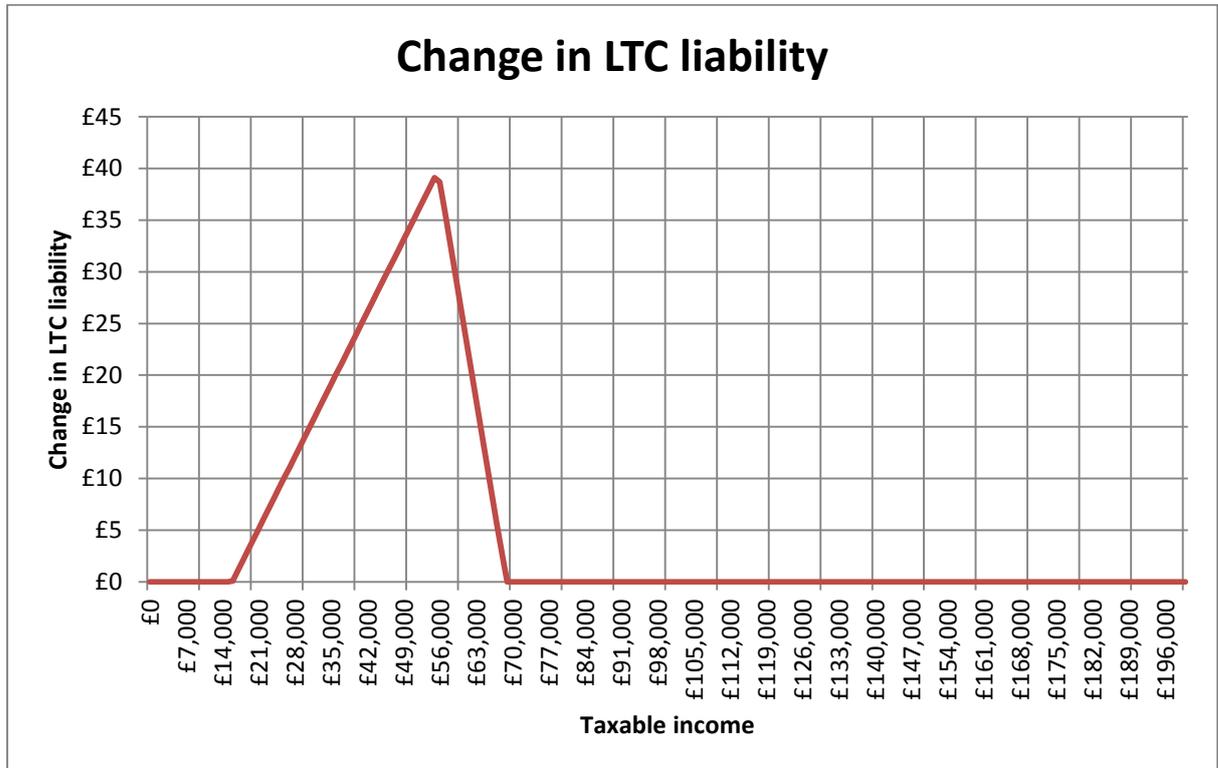
Option: increase marginal rate of income tax from 26% to 28%<sup>22</sup>

Option: Increase MR of income tax by 2%: single person/65+ – Income tax

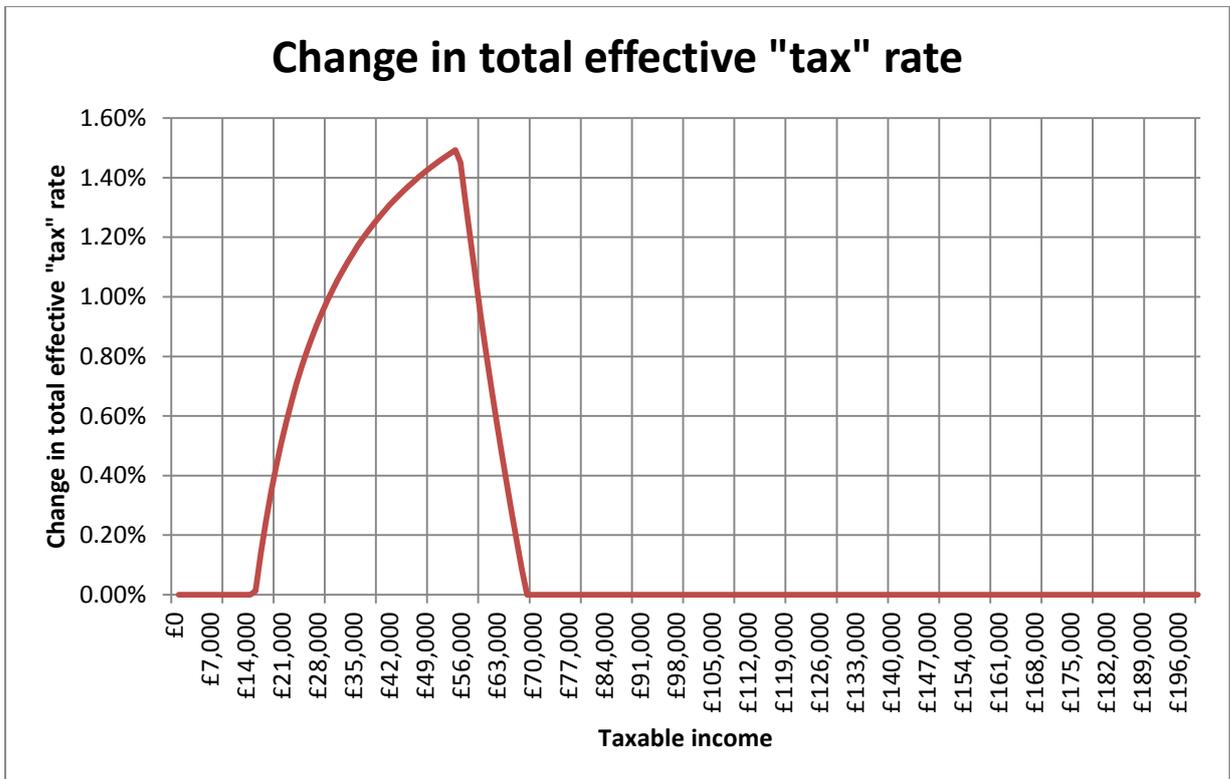
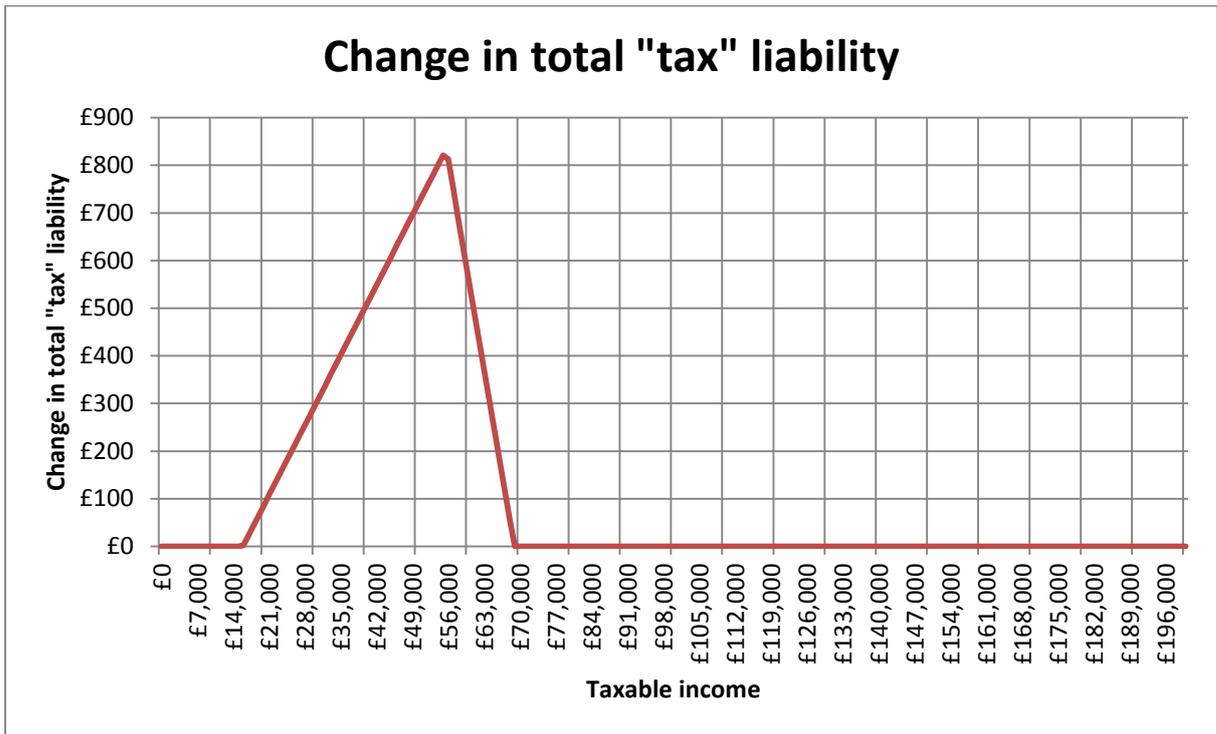


<sup>22</sup> Increasing the marginal rate of income tax to 28% will necessitate increasing the marginal rate of long term care contributions to 1.4%. The two marginal rates are interlinked.

Option: Increase MR of income tax by 2%: single person/65+ – Long term care contributions



Option: Increase MR of income tax by 2%: single person/65+ – Overall tax position

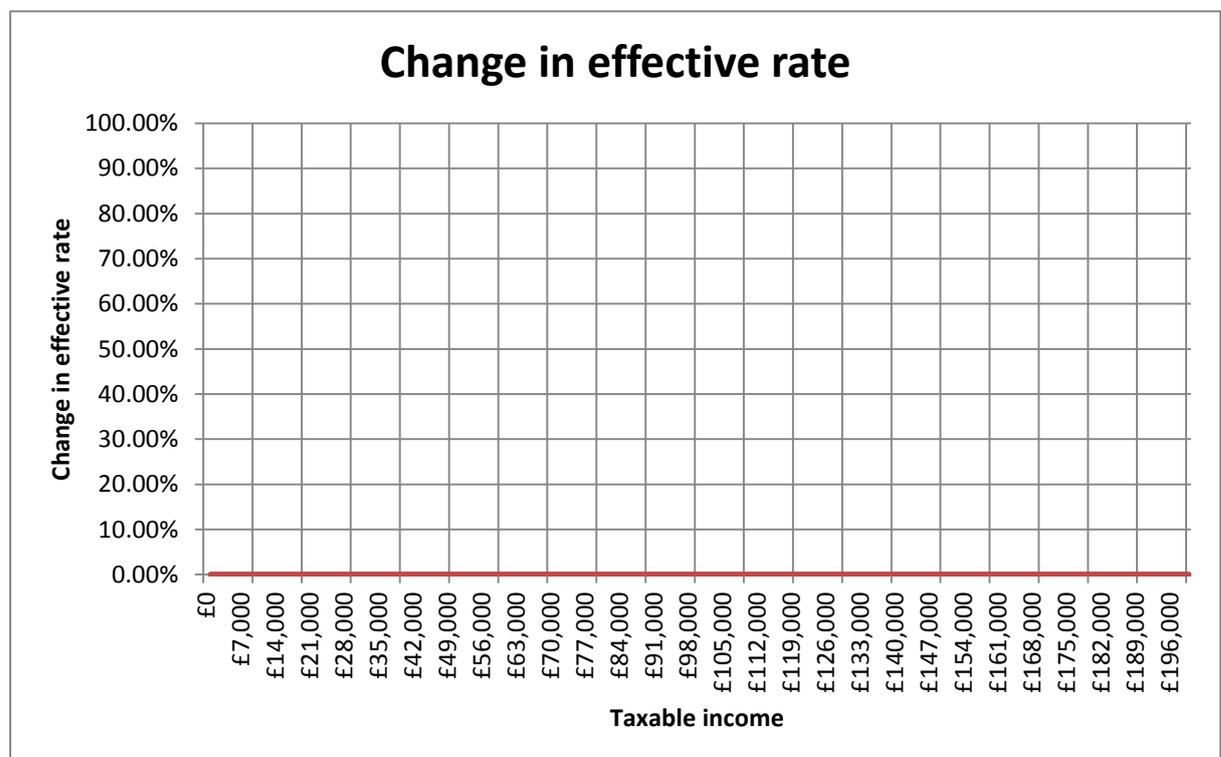
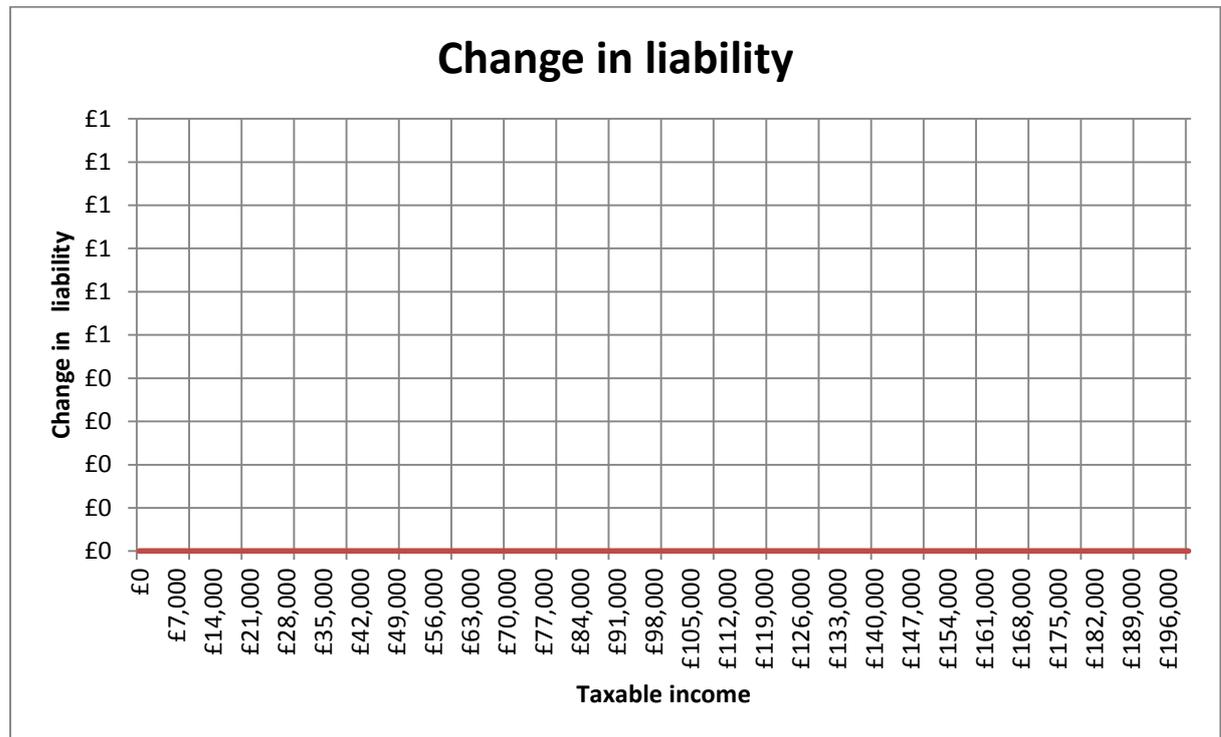


## Household 2: single person – 65+

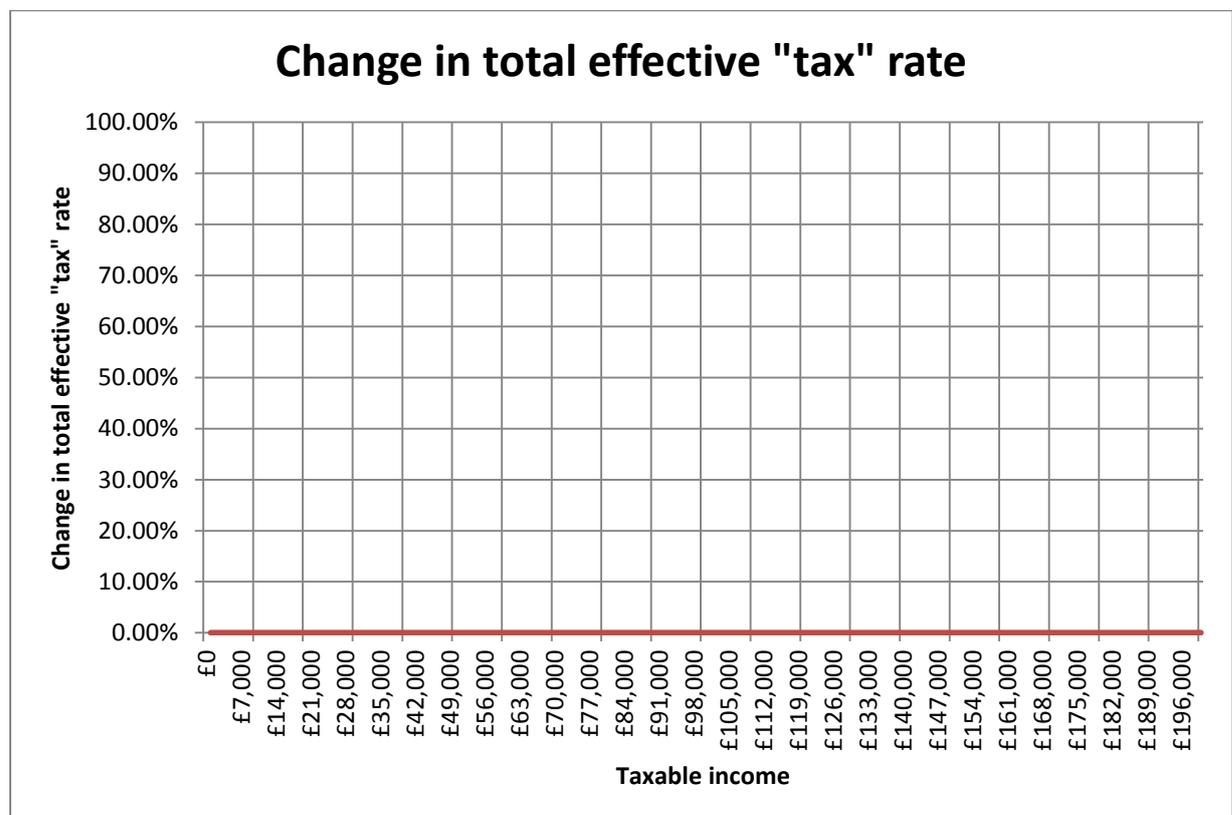
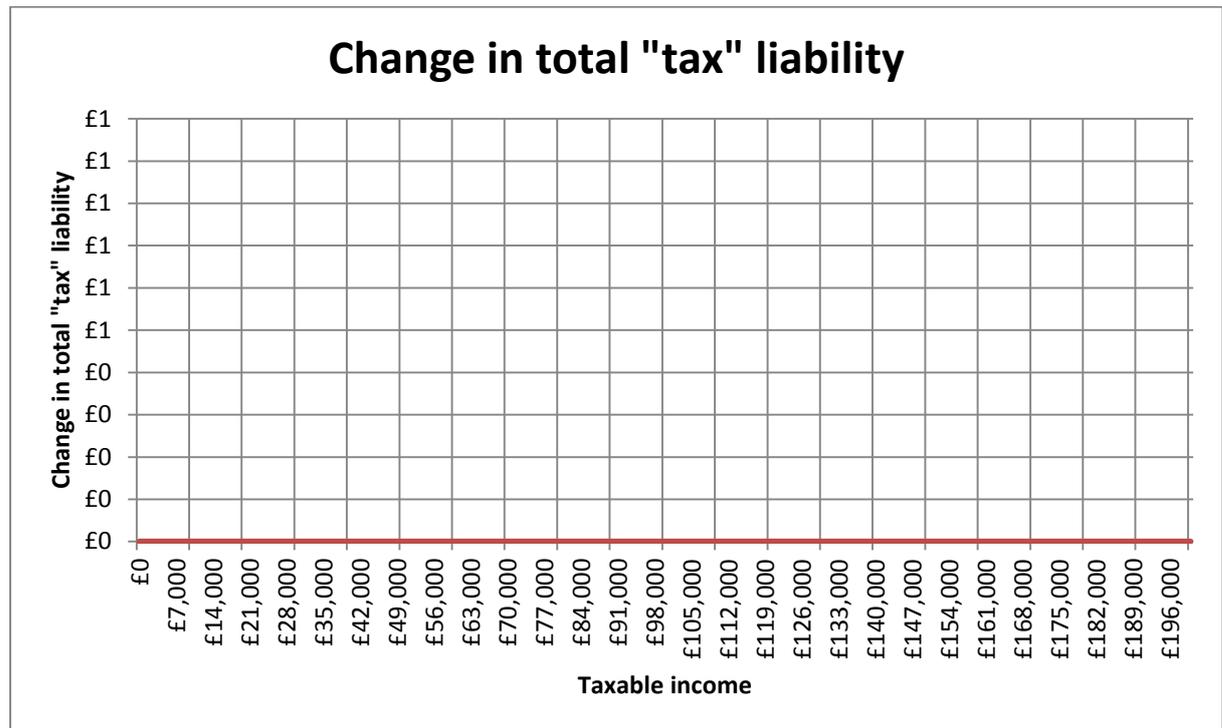
Option – introduce social security type charge below the standard earnings limit

Option: introduce Social Security type charge below the standard earnings limit

*Option: Introduce SS type charge below SEL of 1%: single person/65+*



Option: Introduce SS type charge below SEL by 1%: single person/65+ – Overall tax position

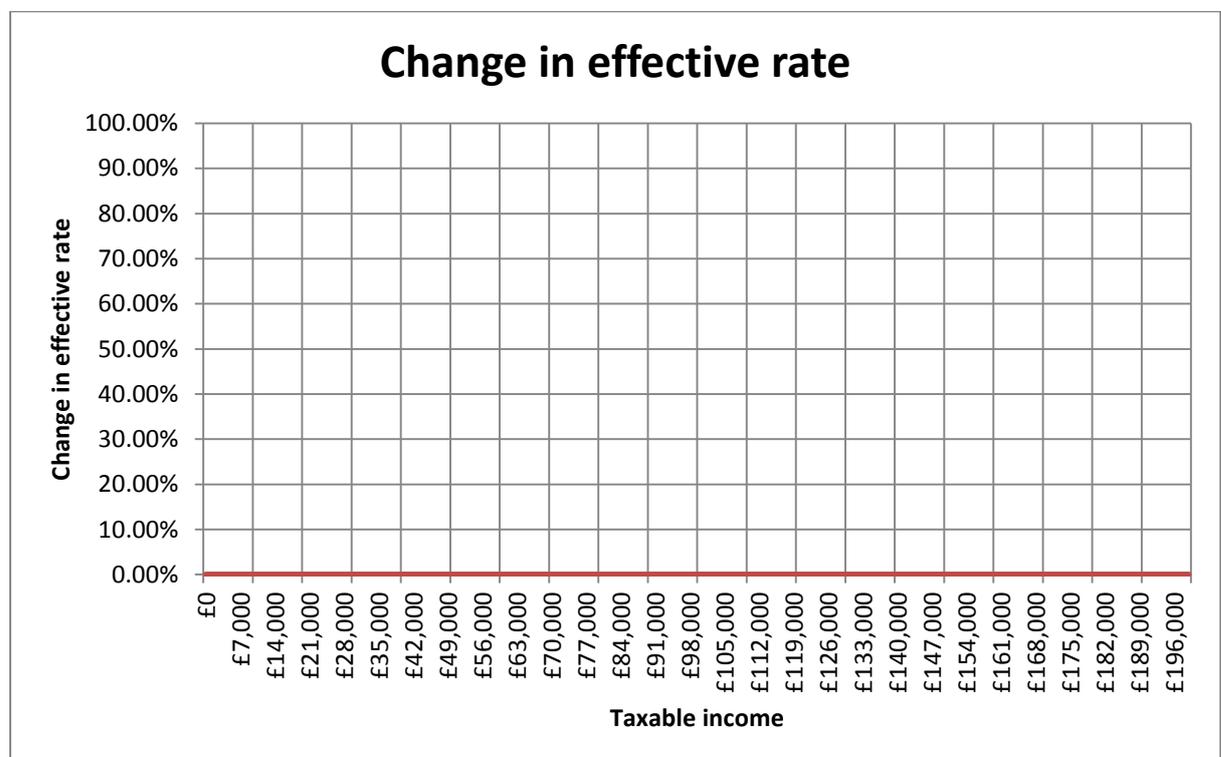
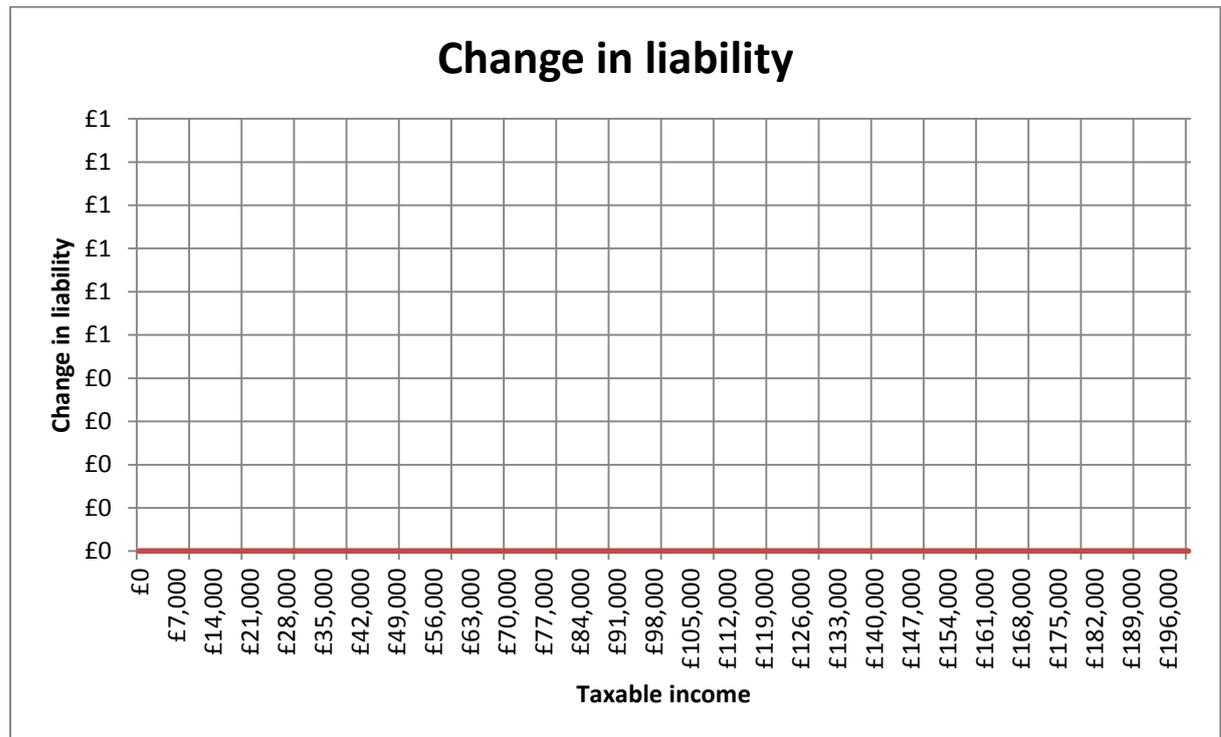


## Household 2: single person – 65+

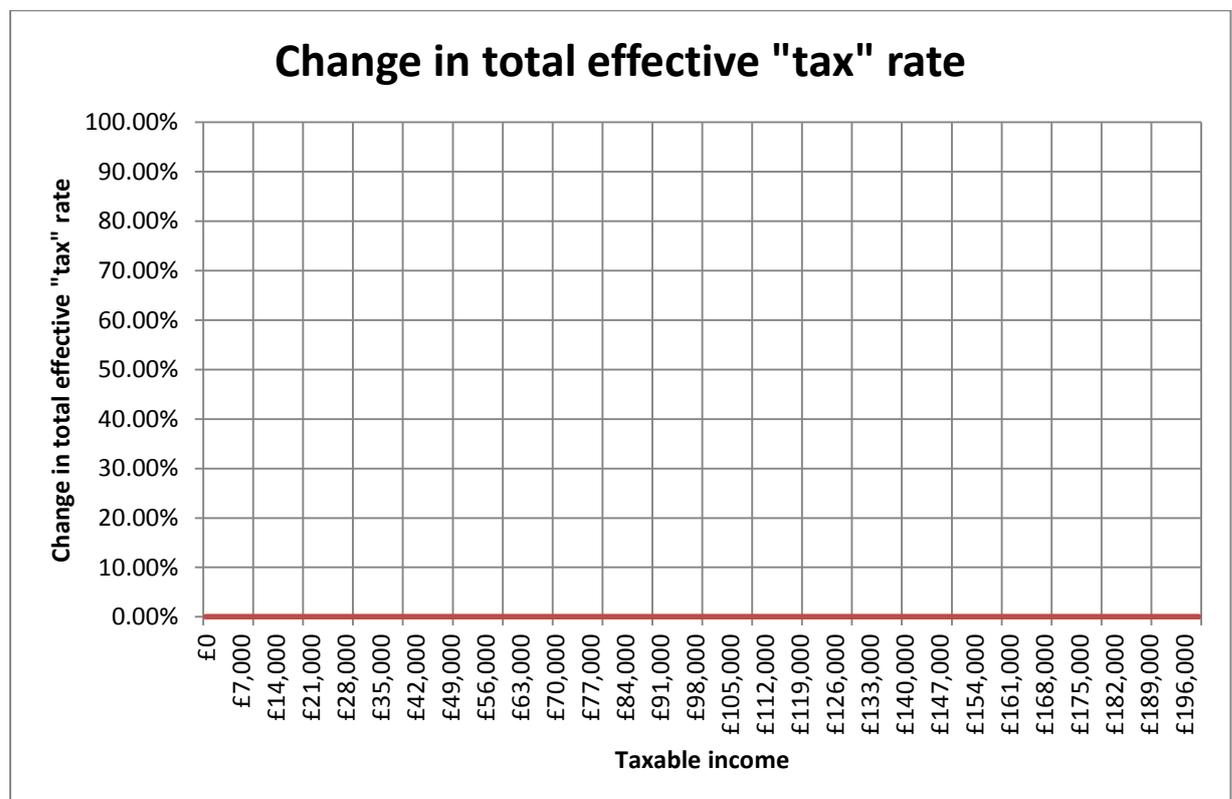
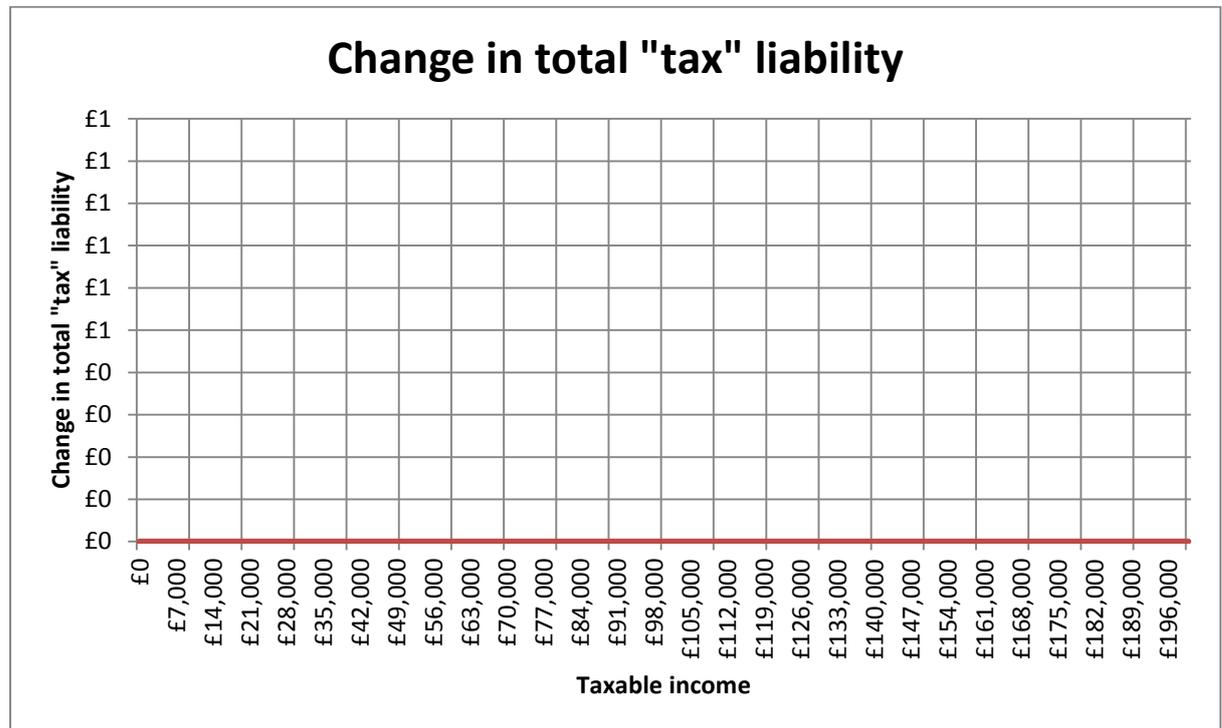
Option – introduce social security type charge above the standard earnings limit

Option: introduce Social Security type charge above the standard earnings limit

*Option: Introduce SS type charge above SEL by 5.5%: single person/65+*



Option: Introduce SS type charge above SEL by 5.5%: single person/65+ – Overall tax position

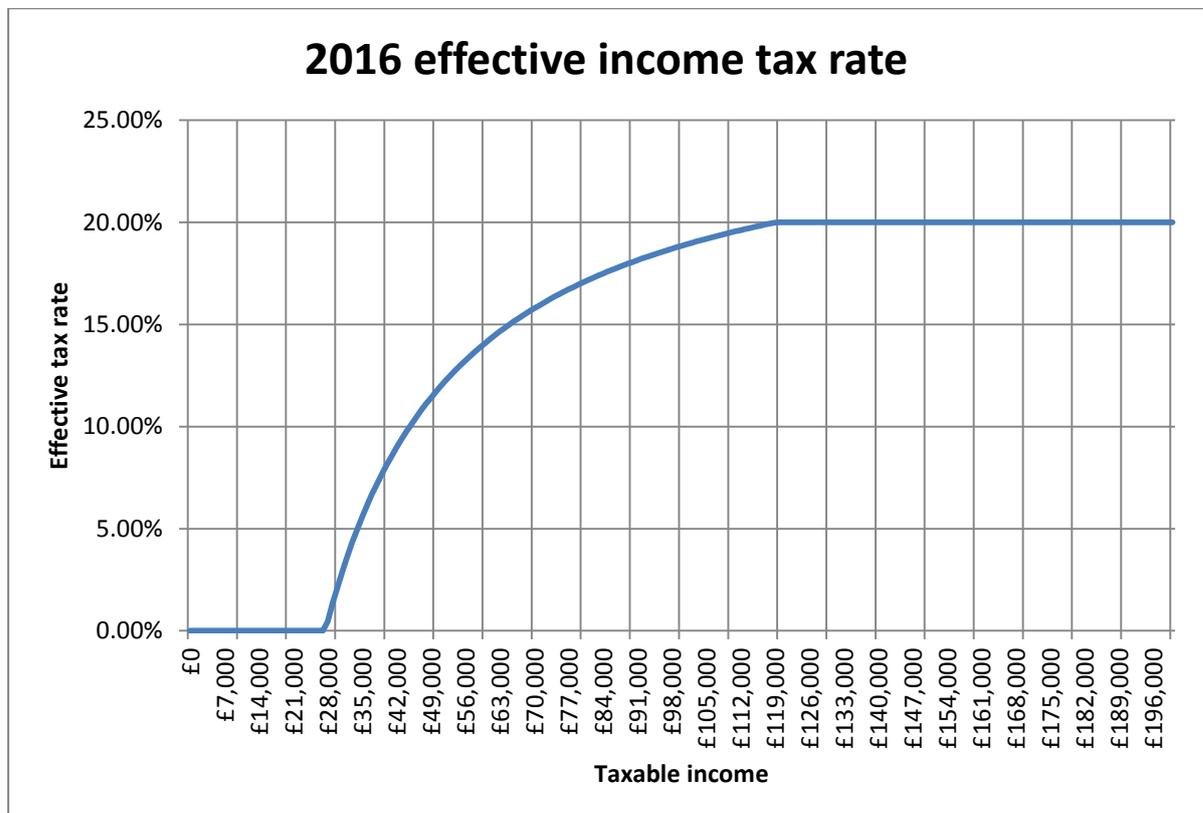
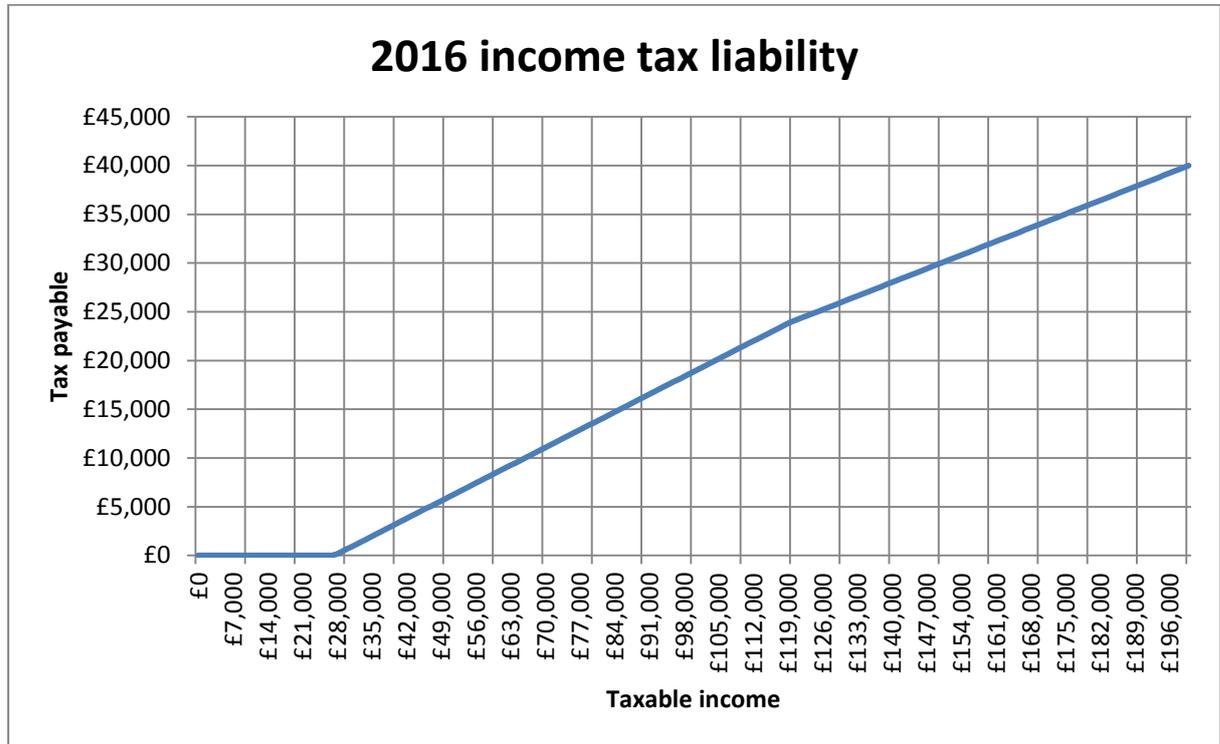


Household 3: married couple –working  
age (assumed income split equally  
between spouses)

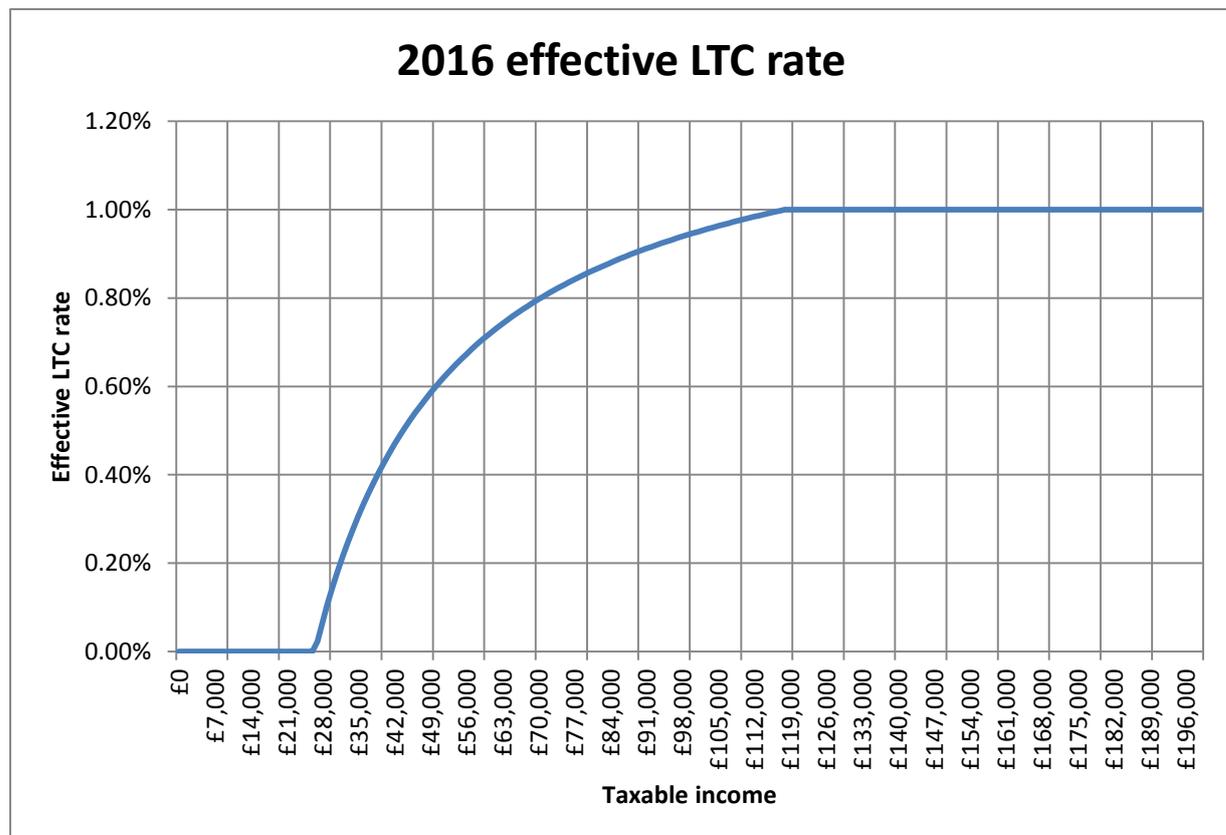
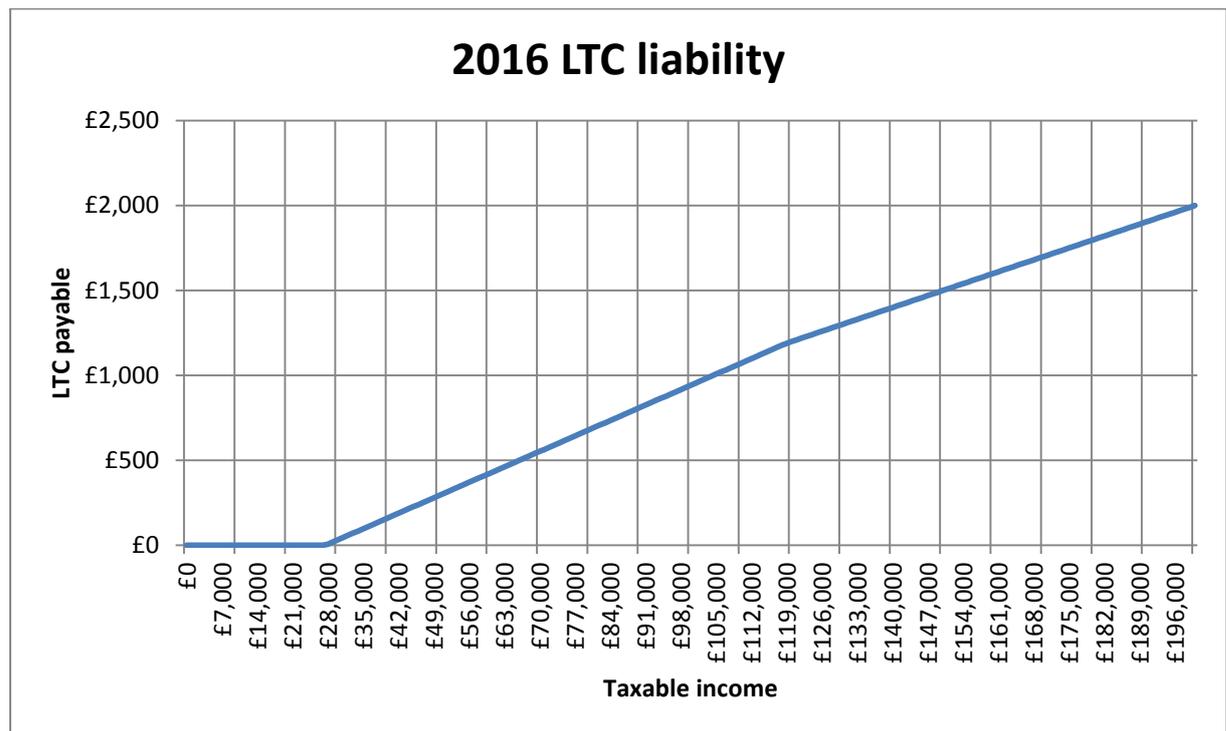
## 2016 Baseline Analysis

Baseline for 2016 year of assessment

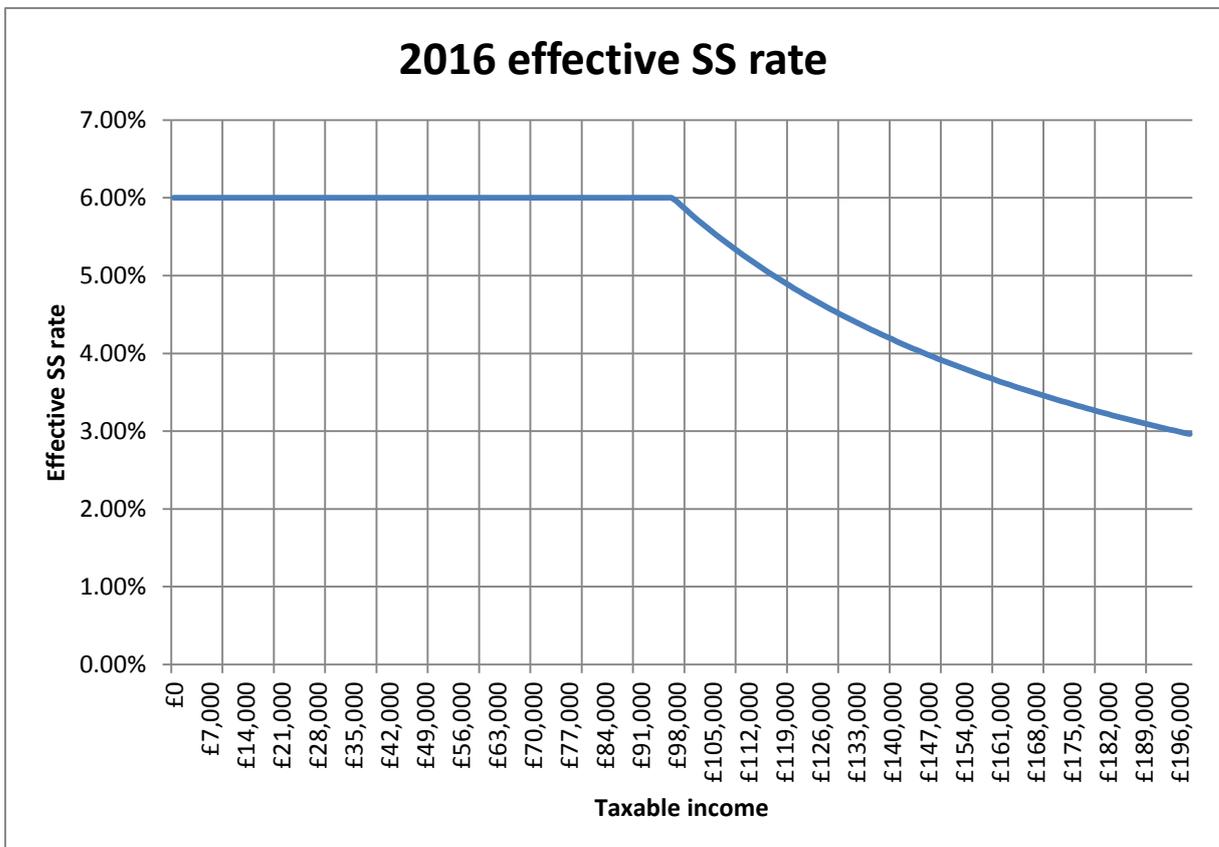
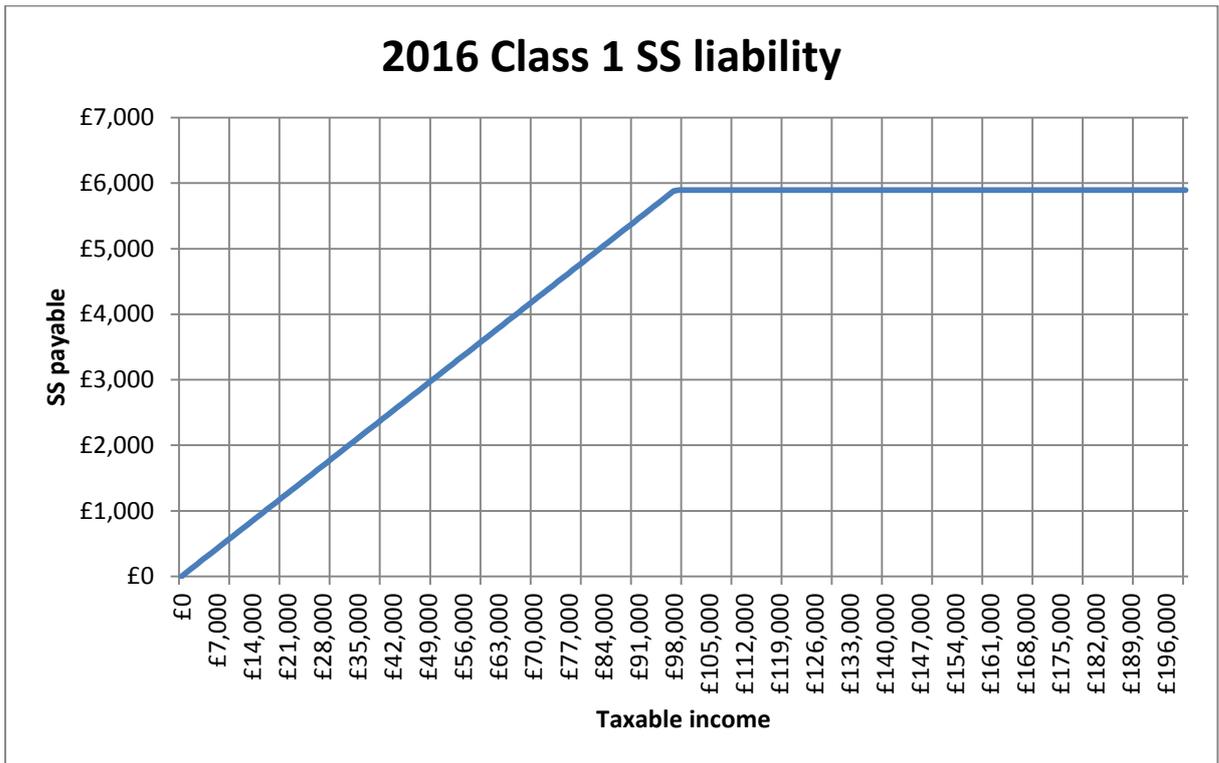
2016 Baseline: married couple/working age – Income tax



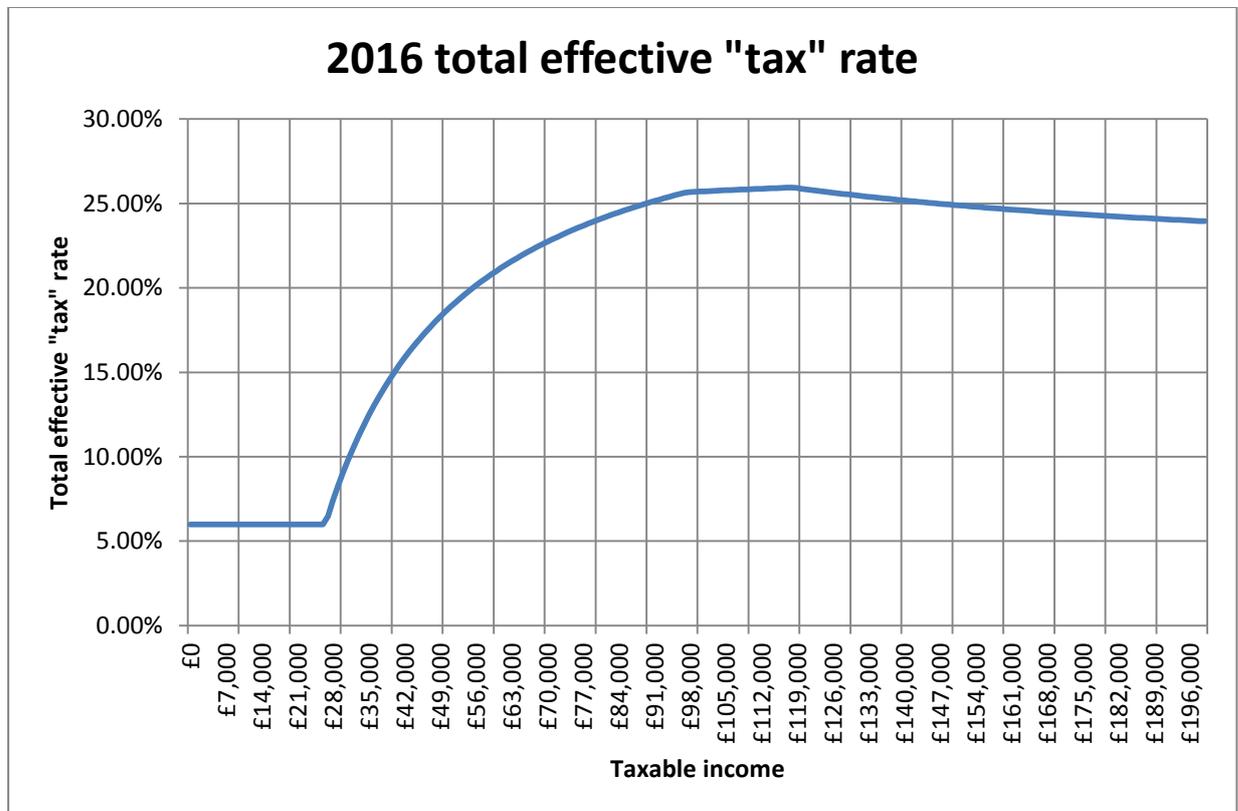
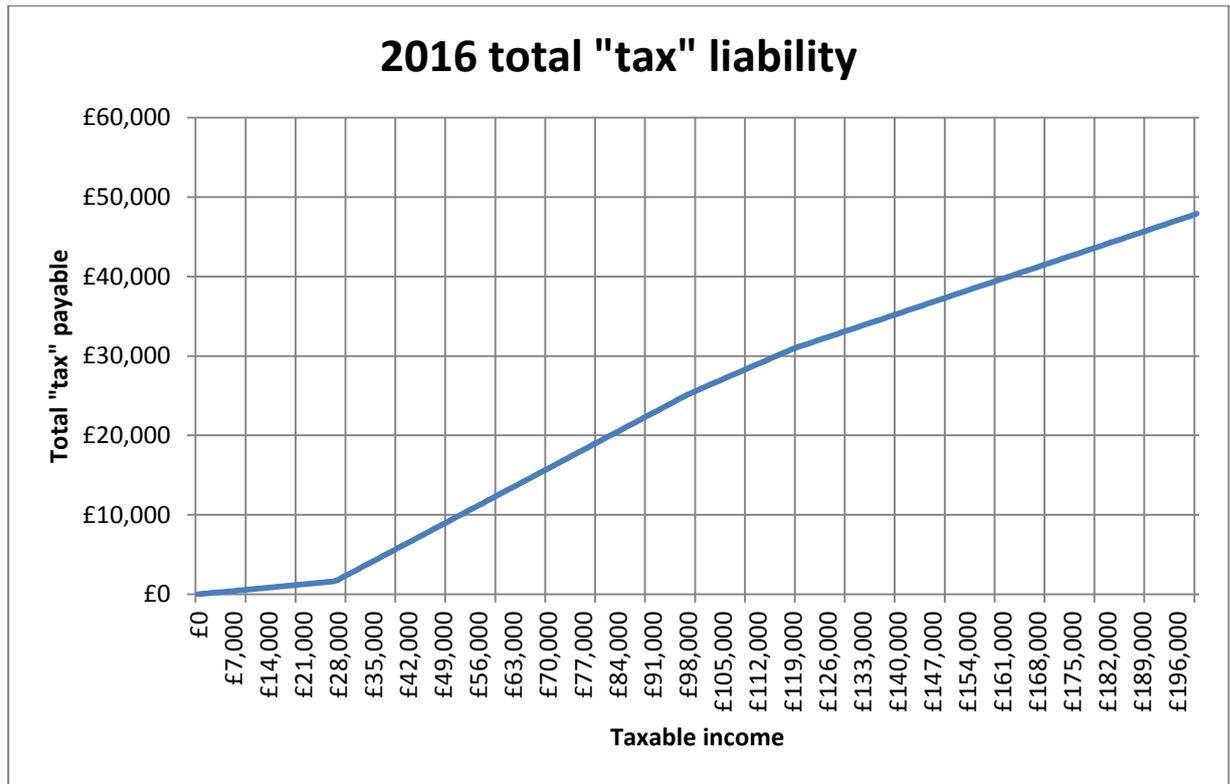
2016 Baseline: married couple/working age – Long term care contribution



2016 Baseline: married couple/working age – Social Security contributions



2016 Baseline: married couple/working age – Overall tax position

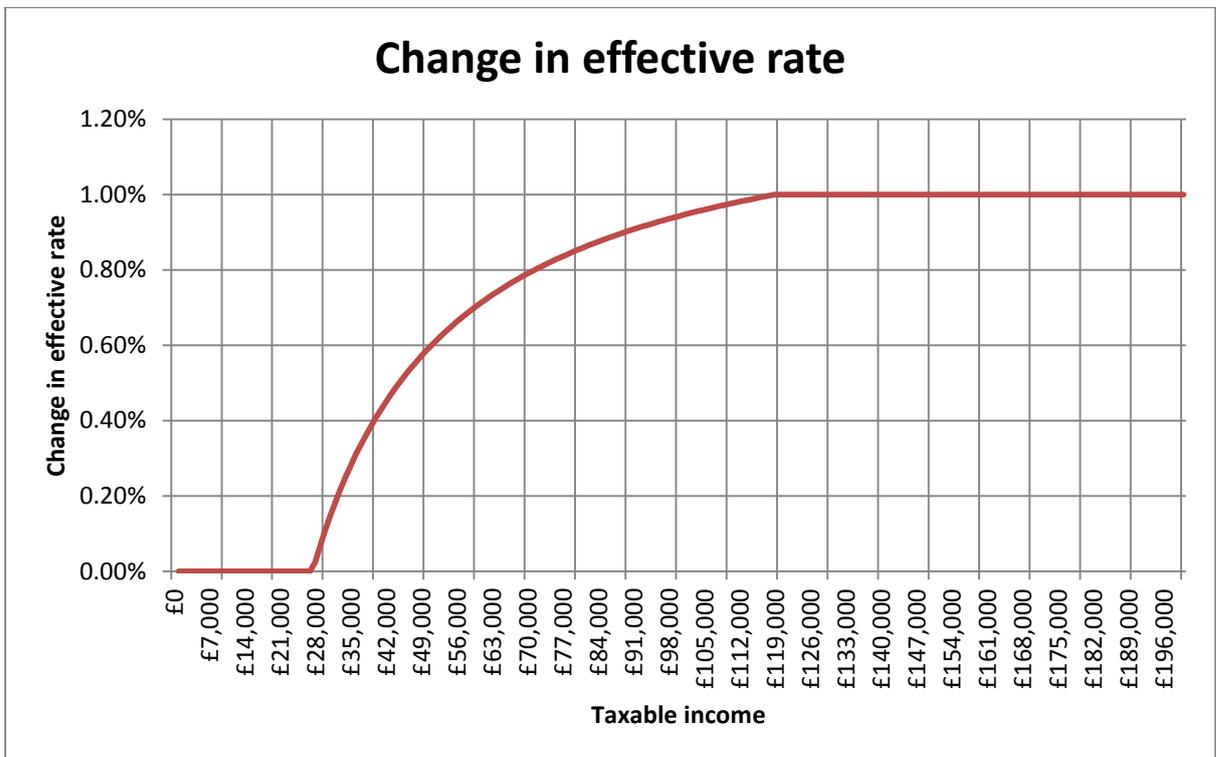
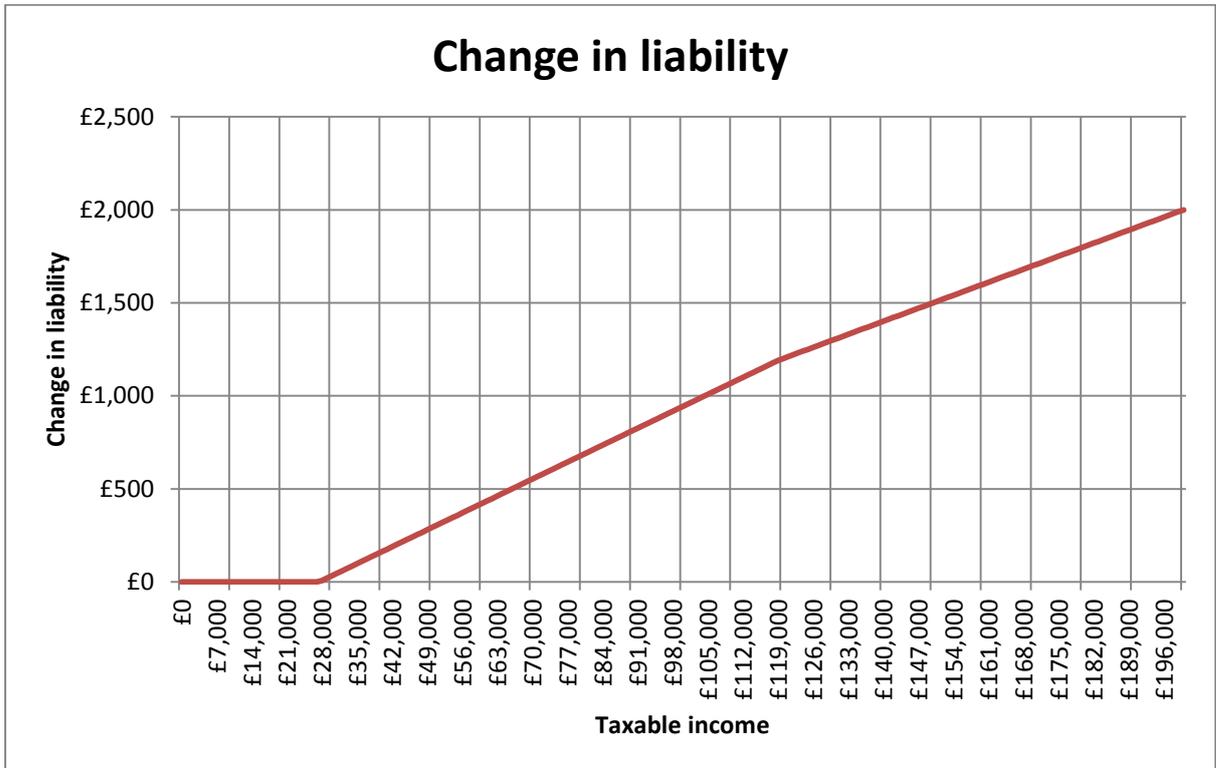


Household 3: married couple –working  
age (assumed income split equally  
between spouses)

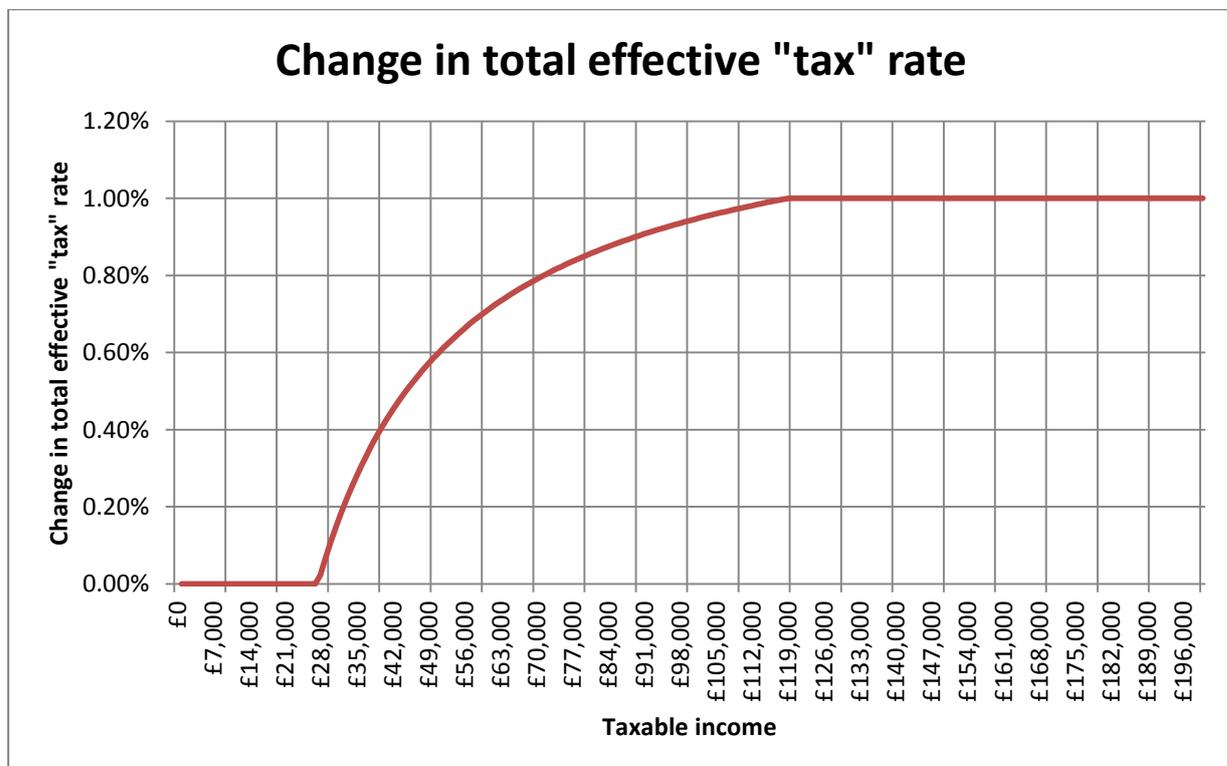
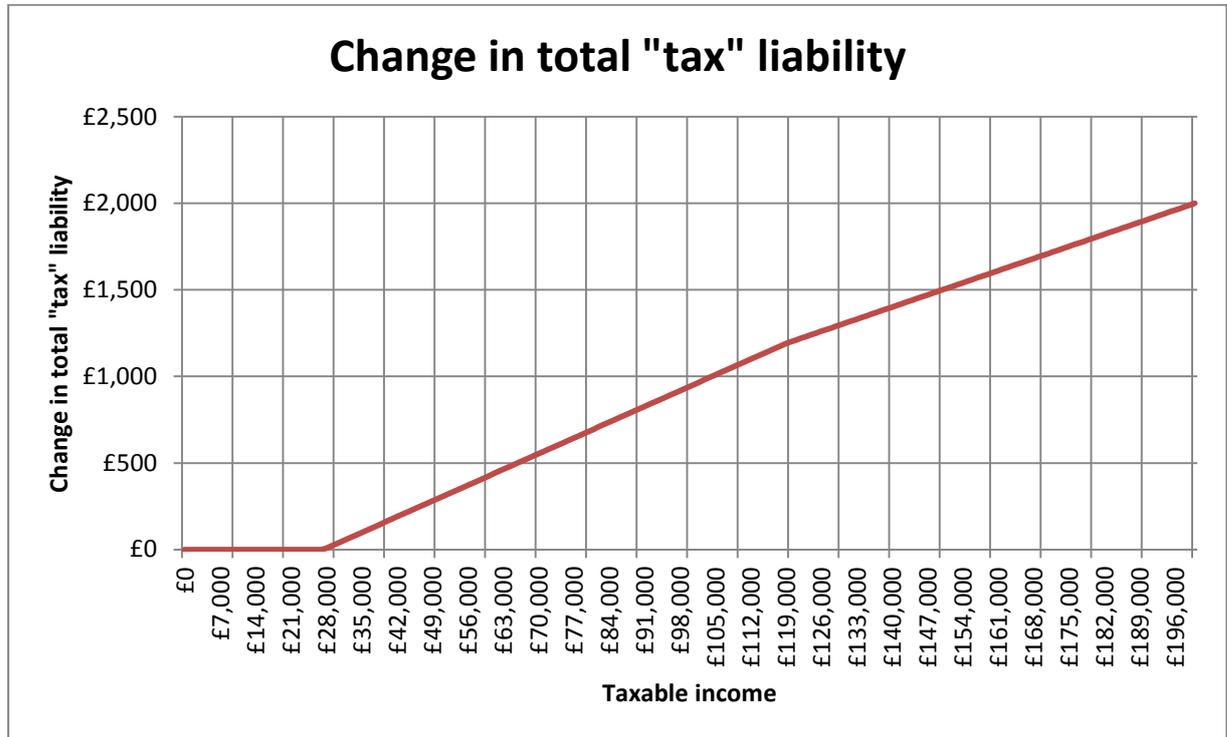
Option – introduce new LTC type charge

Option: introduce LTC type charge

Option: Introduce LTC type charge of 1%: married couple/working age



Option: Introduce new LTC type charge of 1%: married couple/working age – Overall tax position

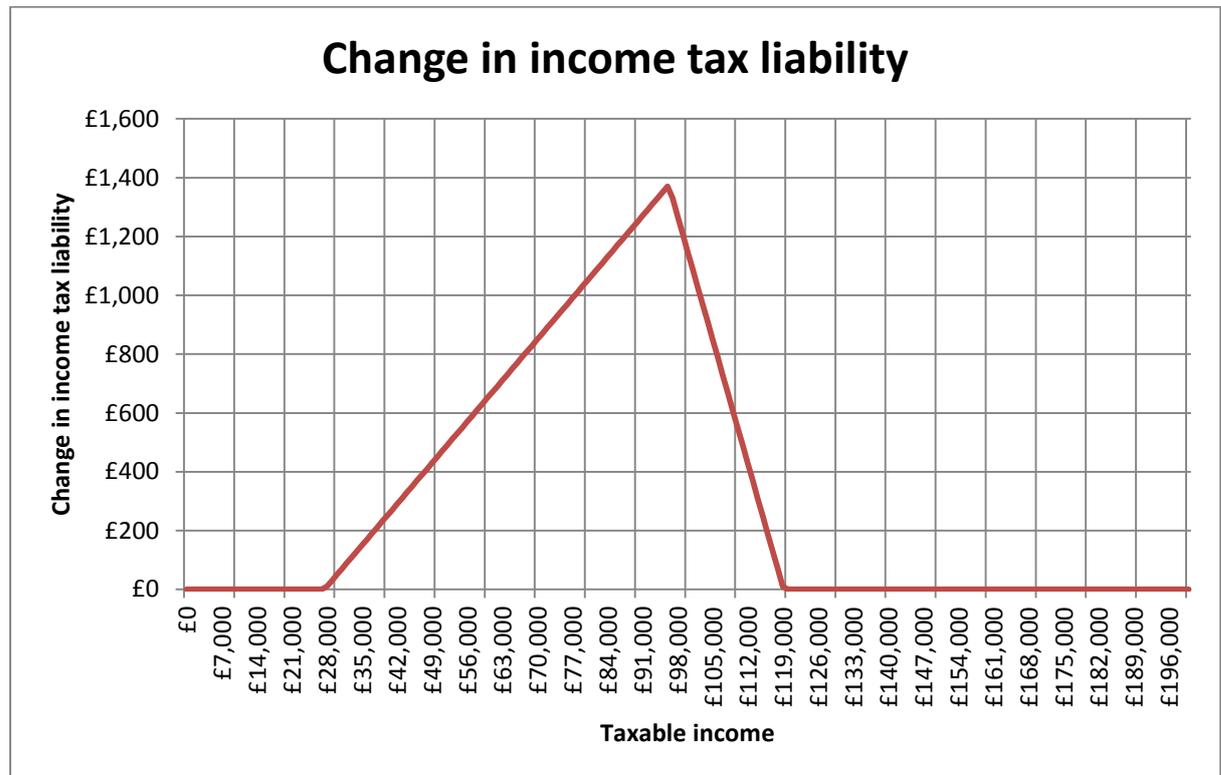


Household 3: married couple –working  
age (assumed income split equally  
between spouses)

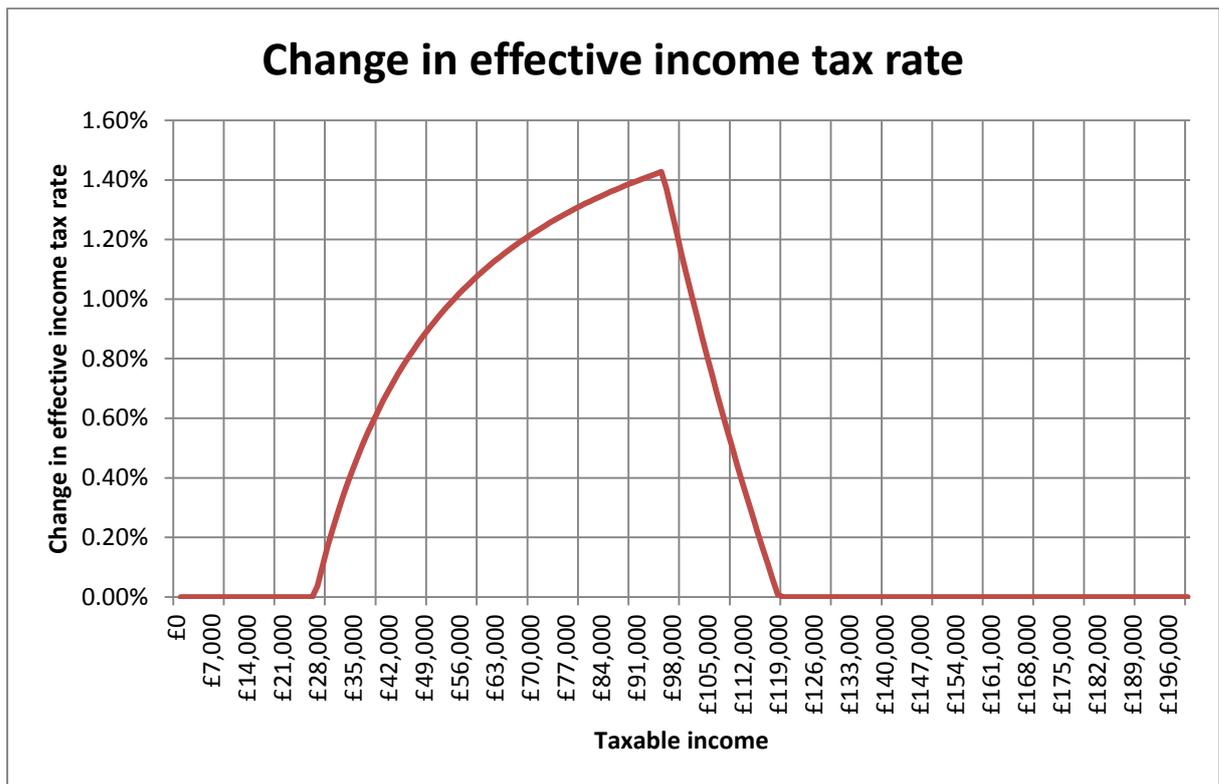
Option – increase marginal rate of income  
tax from 26% to 28%

Option increase marginal rate of income tax from 26% to 28%<sup>23</sup>

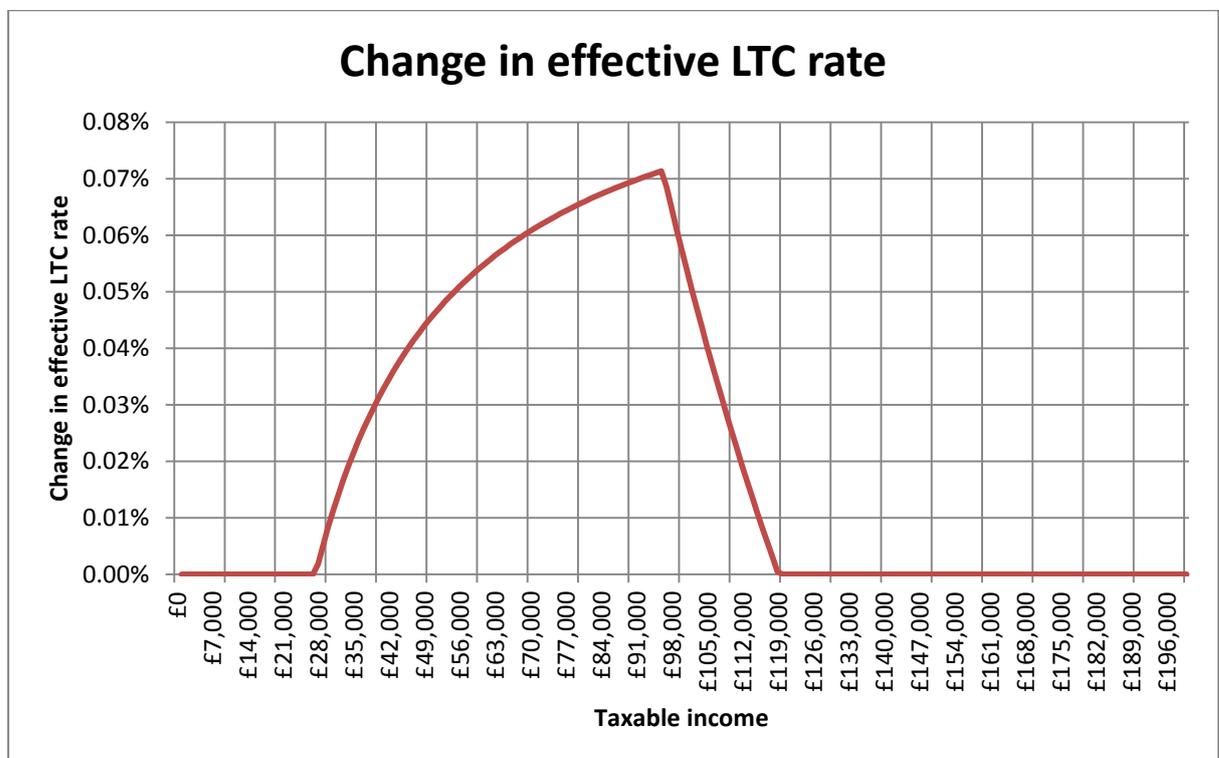
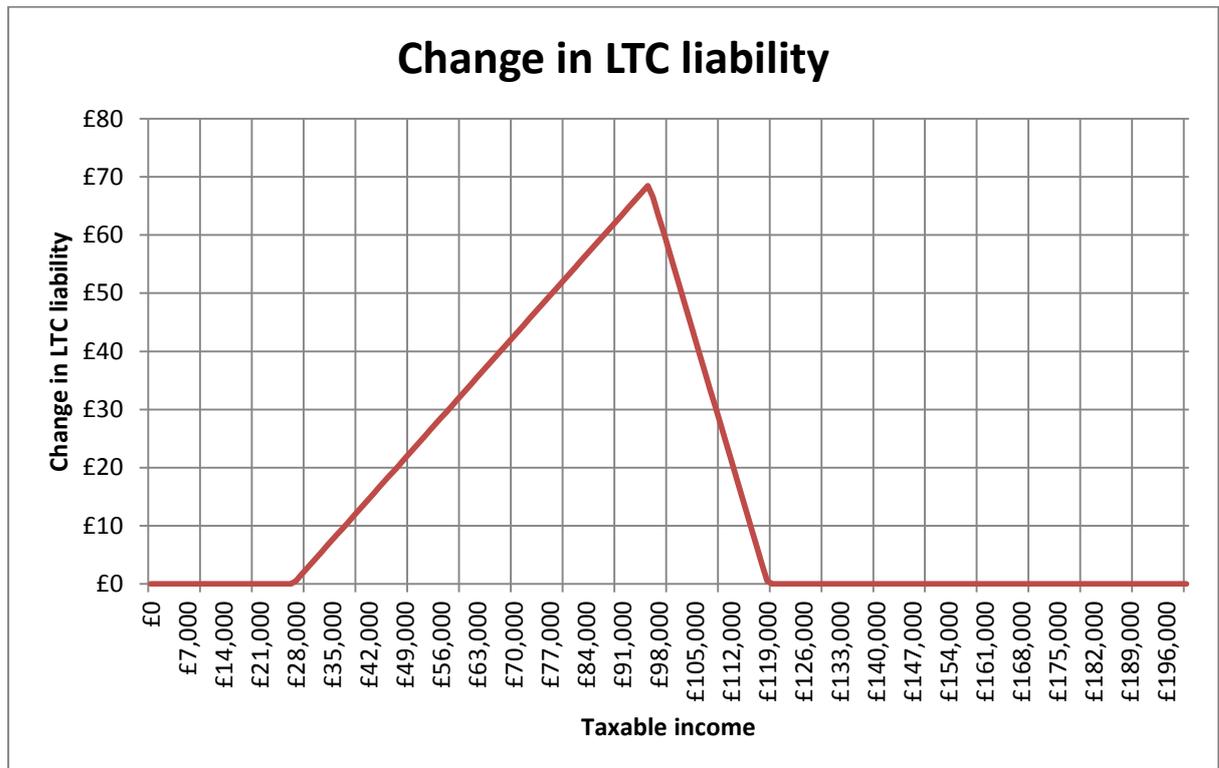
Option: Increase MR of income tax by 2%: married couple/working age – Income tax



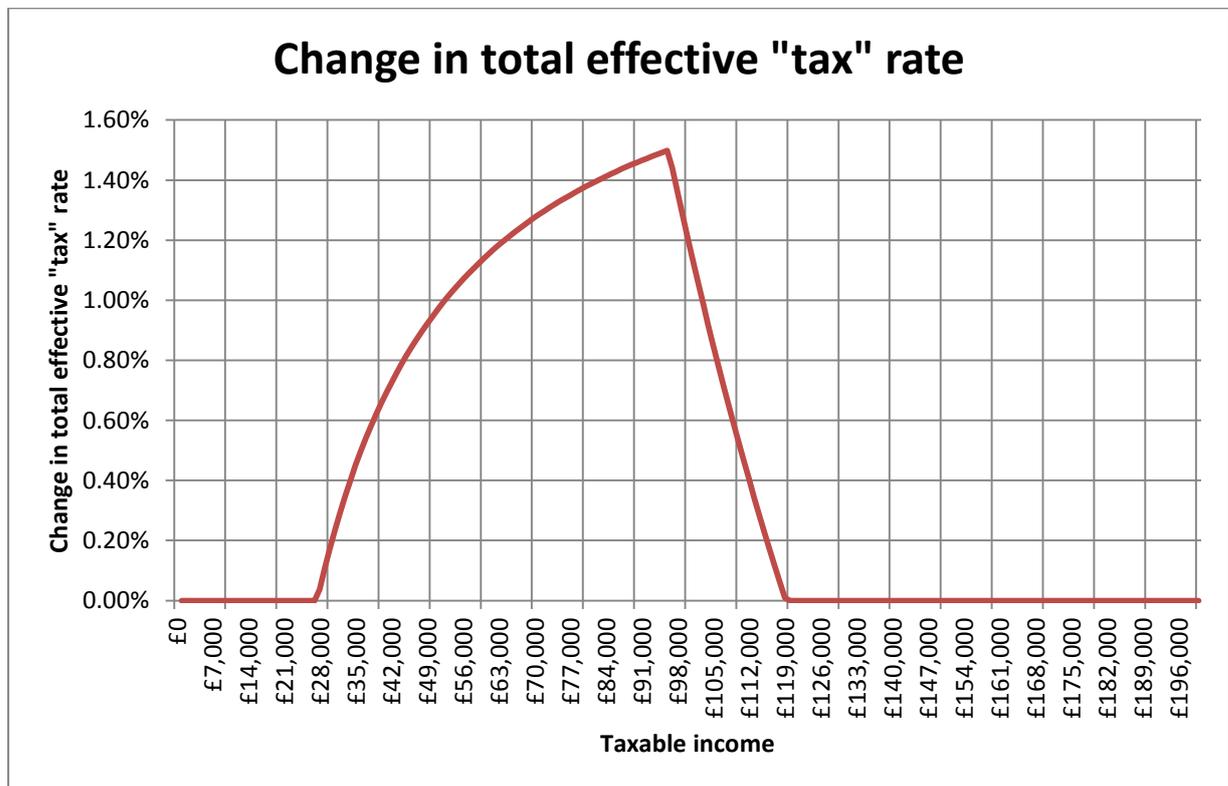
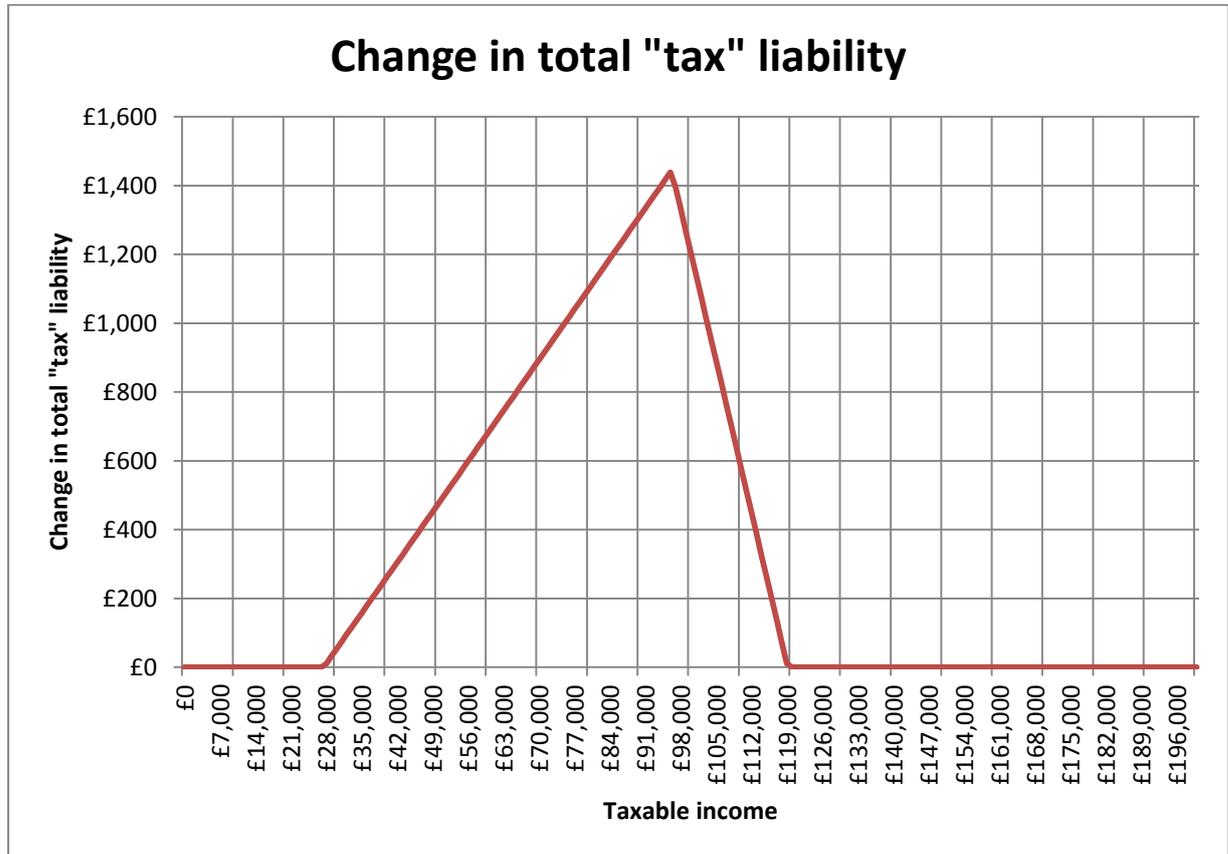
<sup>23</sup> Increasing the marginal rate of income tax to 28% will necessitate increasing the marginal rate of long term care contributions to 1.4%. The two marginal rates are interlinked.



Option: Increase MR of income tax by 2%: married couple/working age – Long term care contributions



Option: Increase MR of income tax by 2%: married couple/working age – Overall tax position

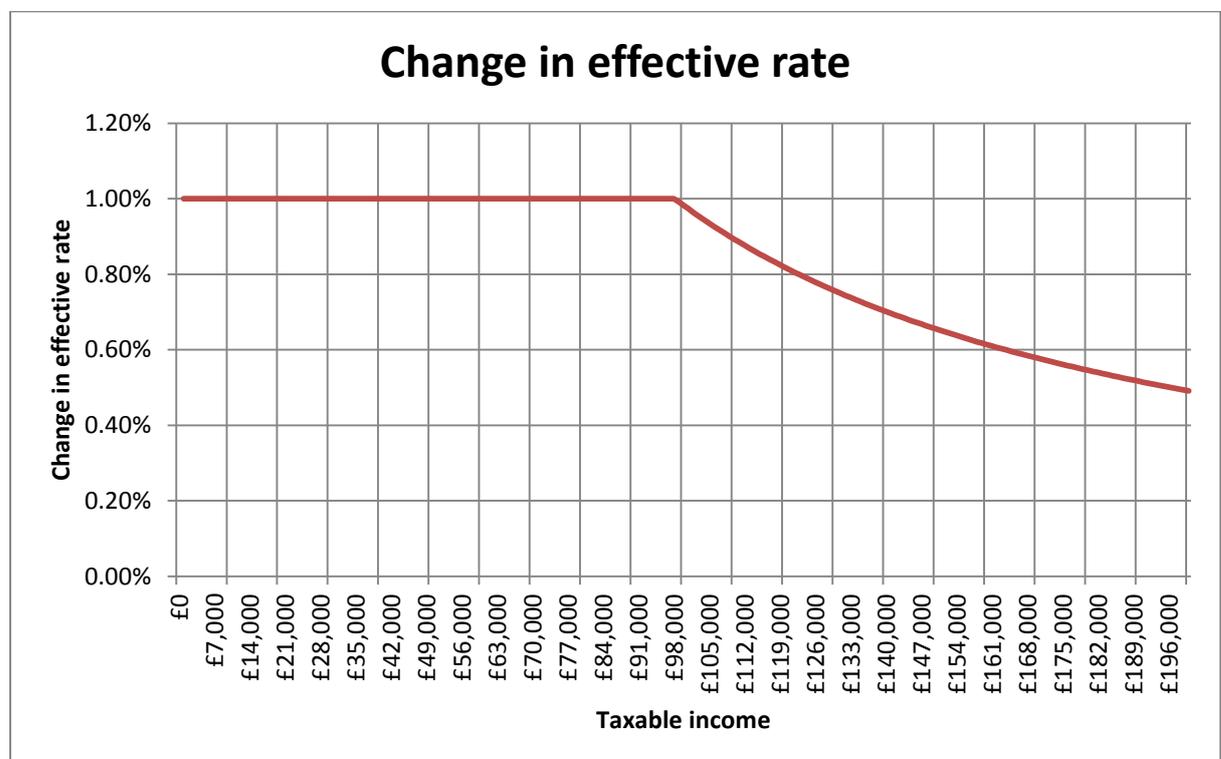
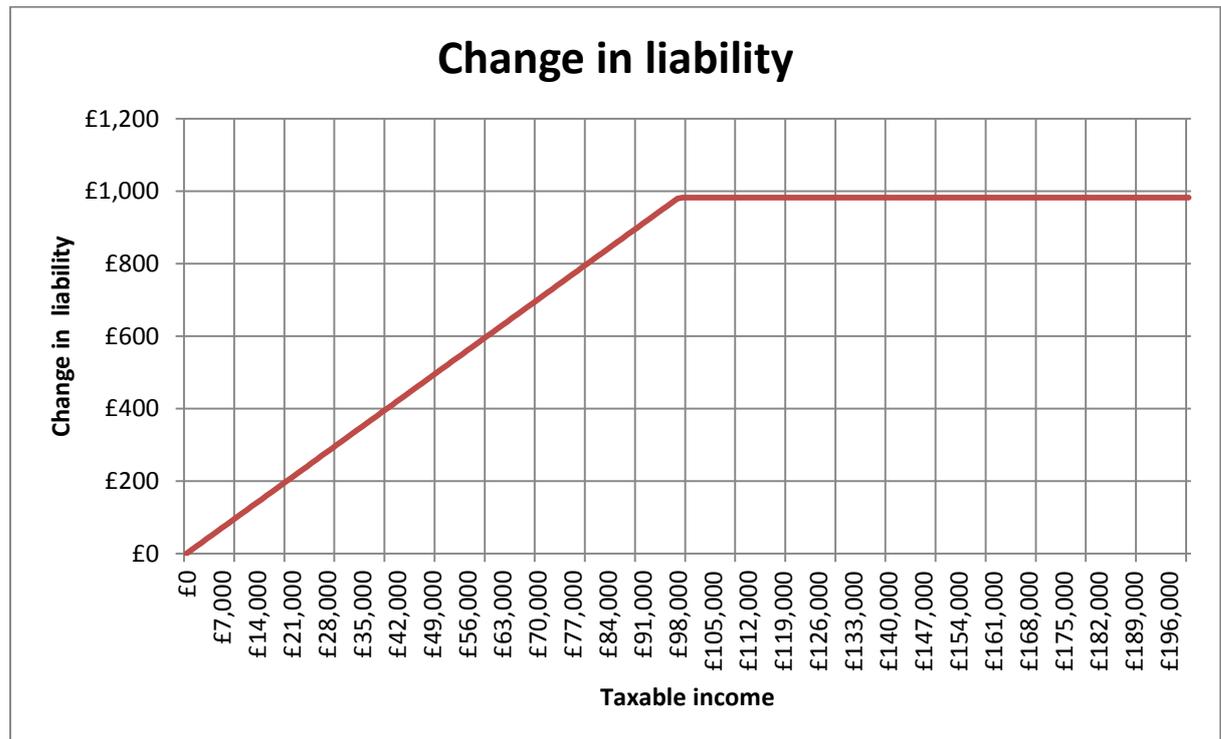


Household 3: married couple –working  
age (assumed income split equally  
between spouses)

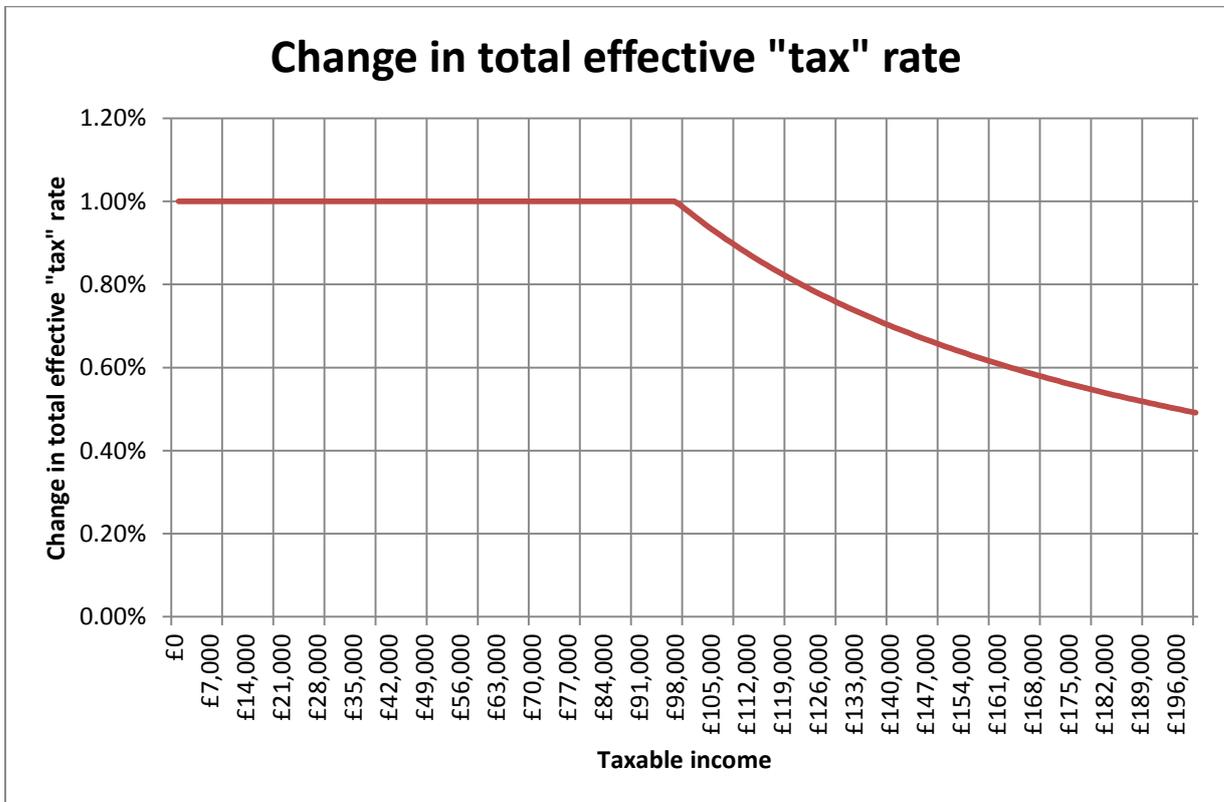
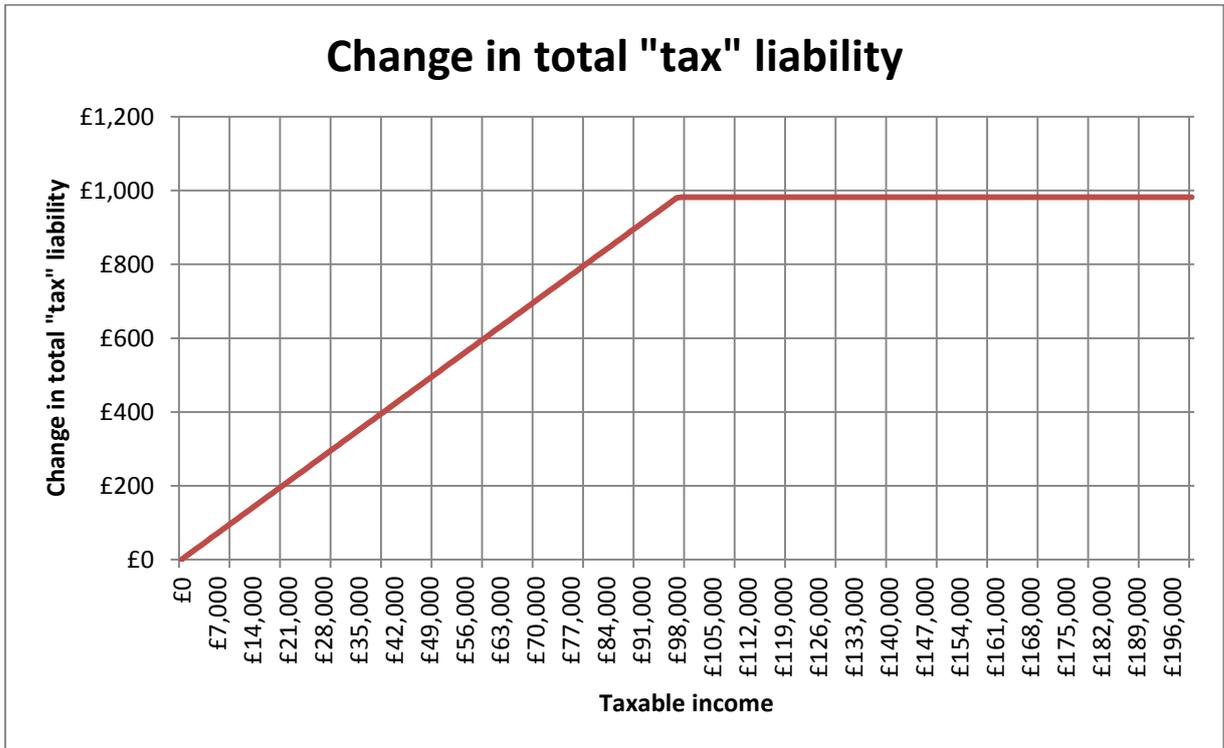
Option – introduce Social Security type  
charge below the standard earnings limit

Option: introduce Social Security type charge below the standard earnings limit

*Option: Introduce SS type charge below SEL of 1%: married couple/working age*



Option: Introduce SS type charge below SEL of 1%: married couple/working age –  
Overall tax position

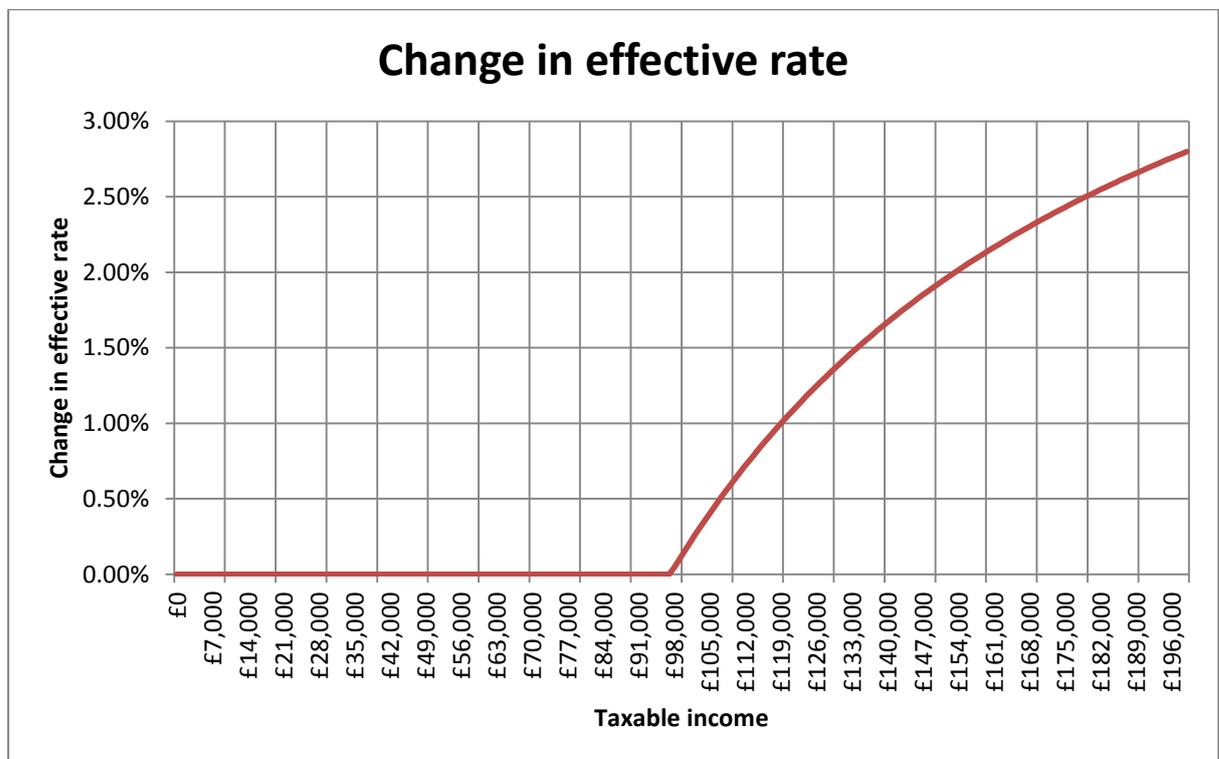
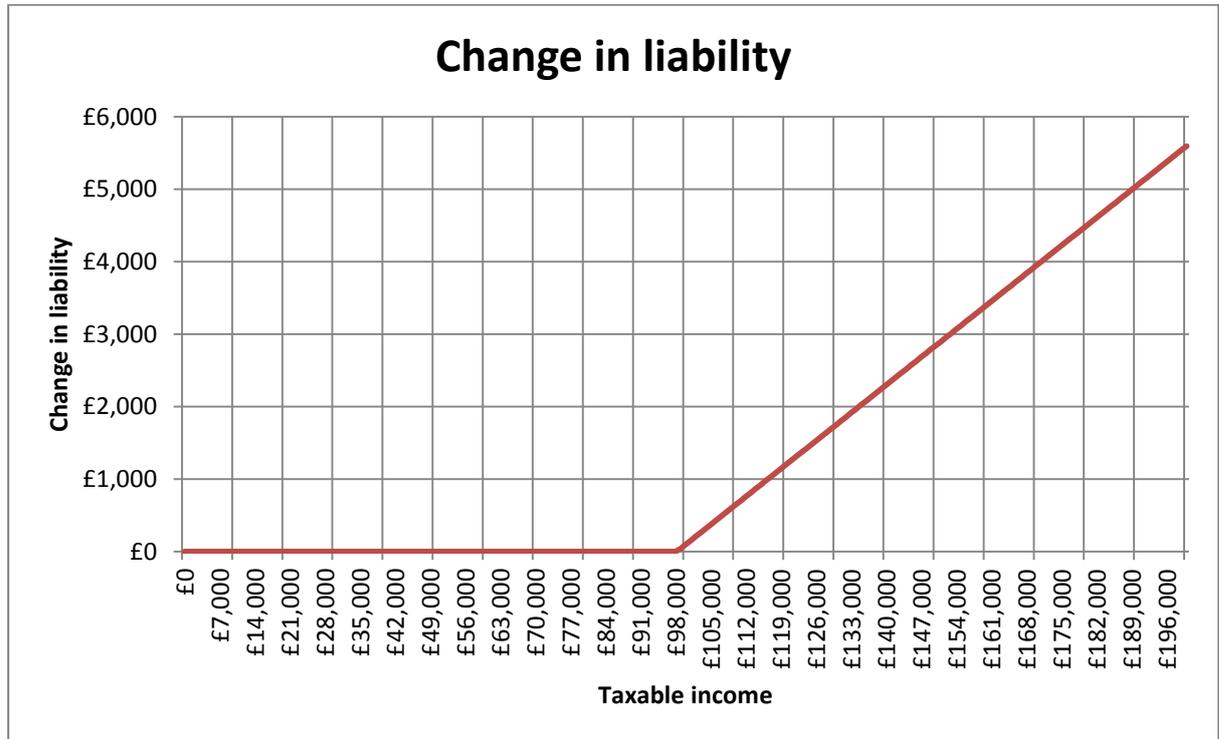


Household 3: married couple –working  
age (assumed income split equally  
between spouses)

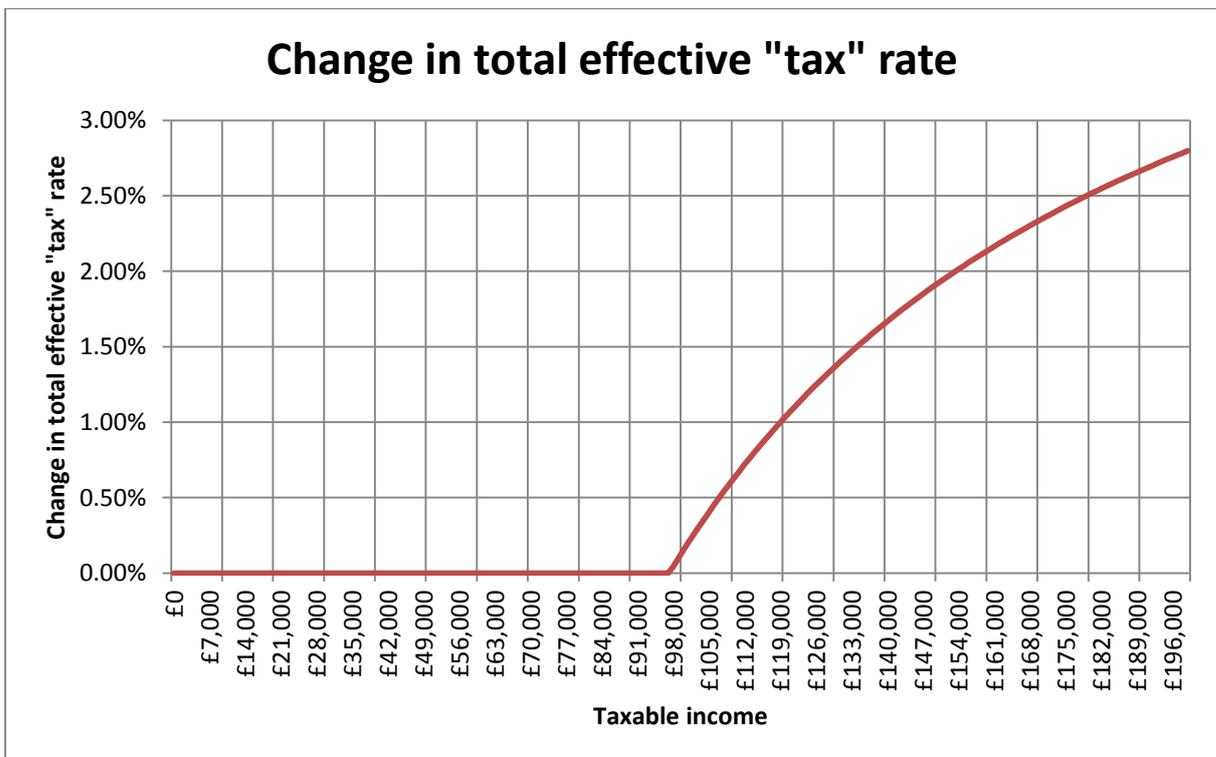
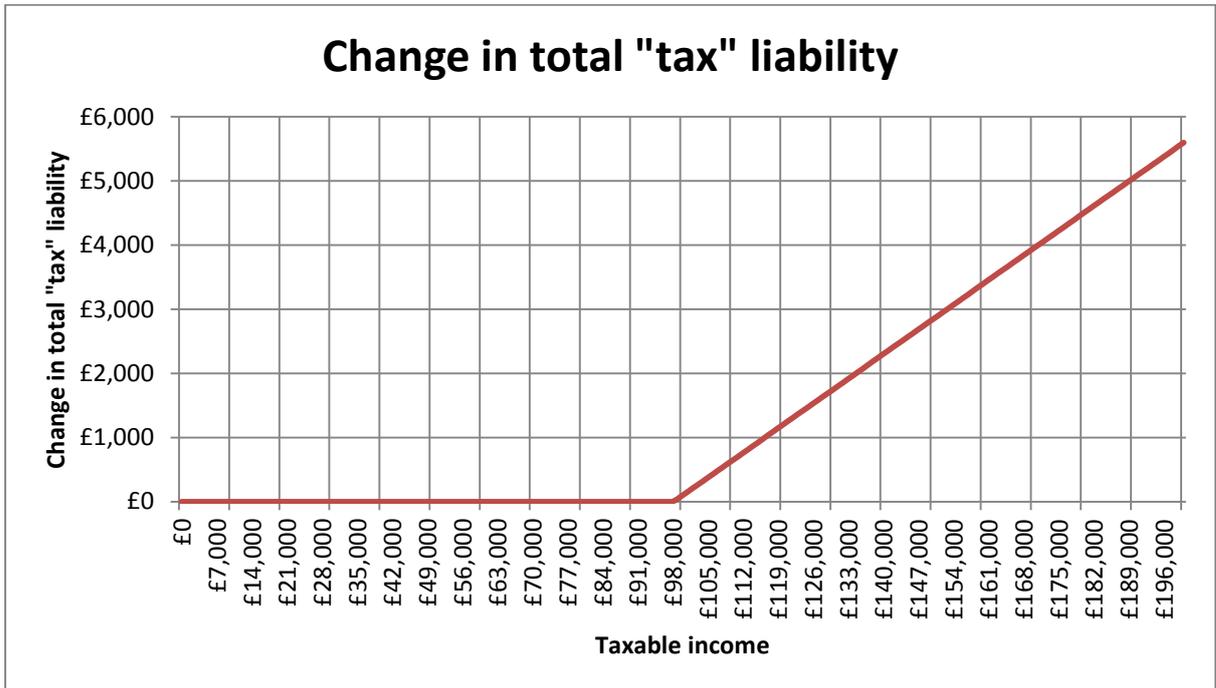
Option – introduce Social Security type  
charge above the standard earnings limit

Option: introduce Social Security type charge above the standard earnings limit

*Option: Introduce SS type charge above SEL of 5.5%: married couple/working age*



Option: Introduce SS type charge above SEL of 5.5%: married couple/working age –  
Overall tax position

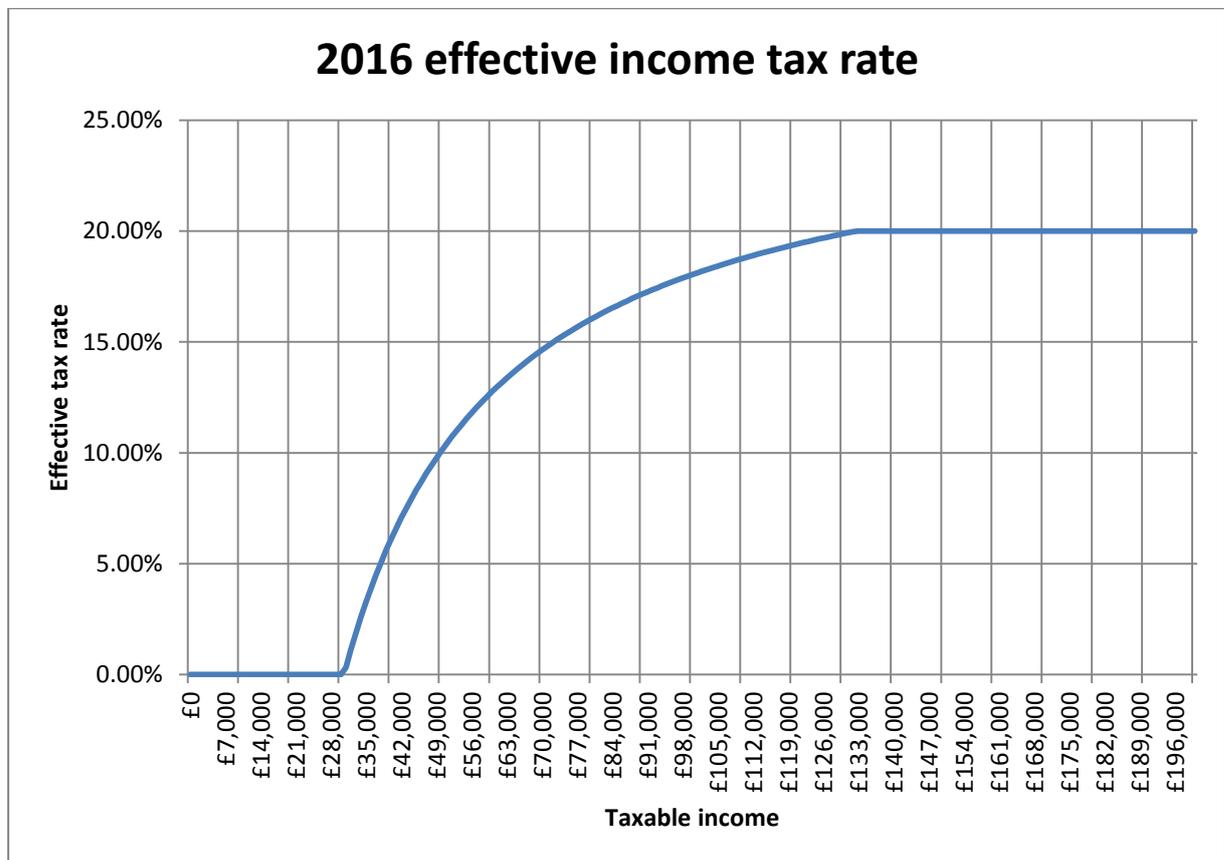
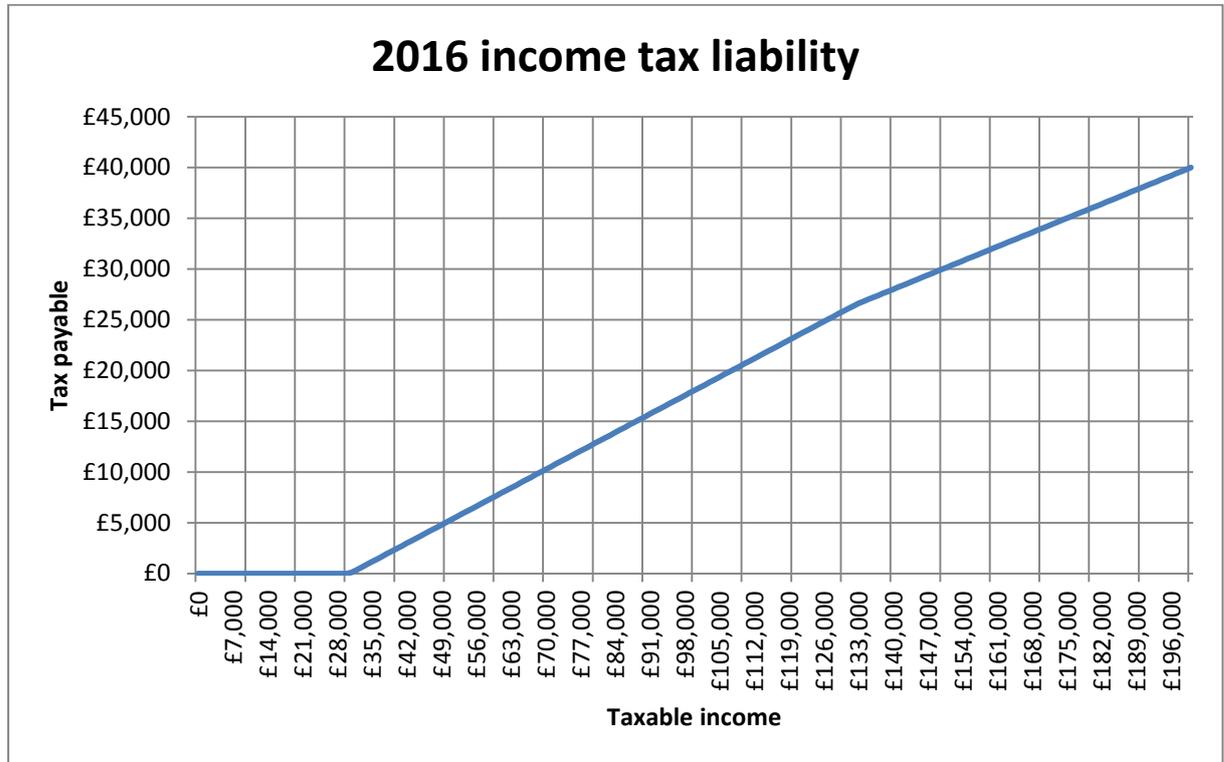


Household 4: married couple – 65+  
(assumed income split equally between  
spouses)

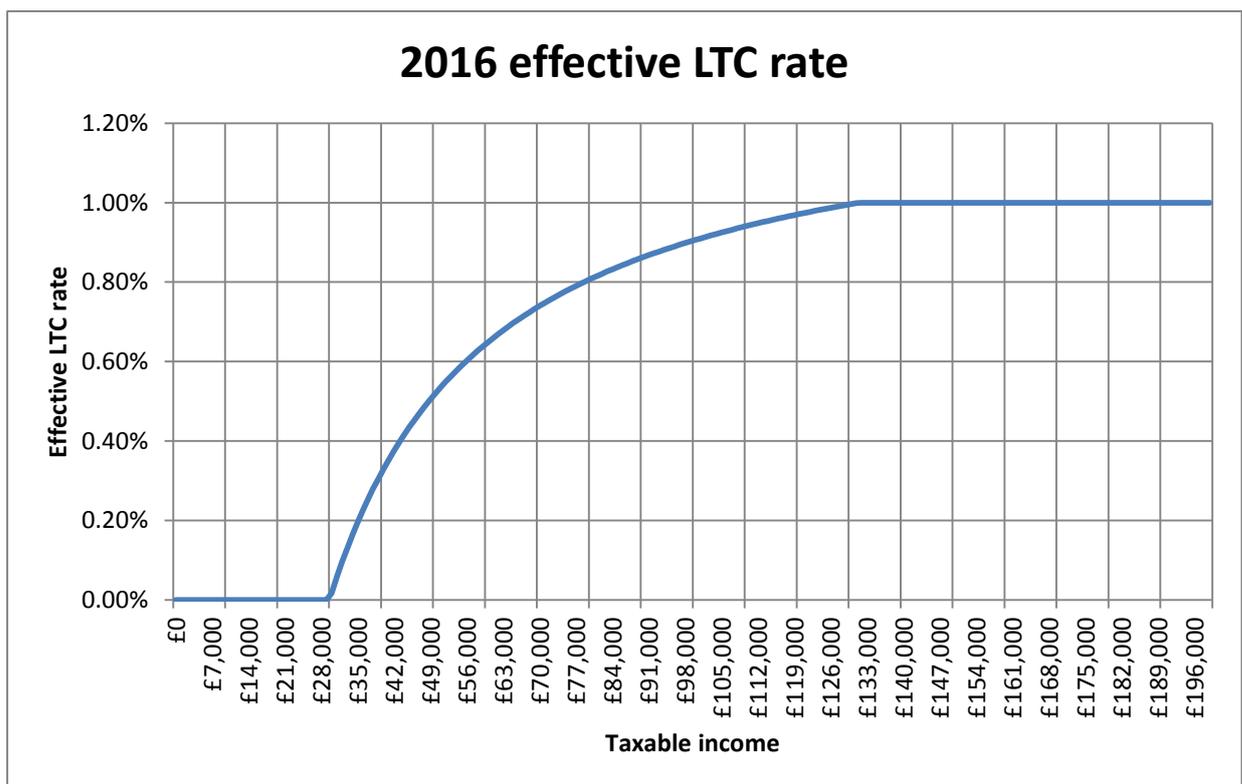
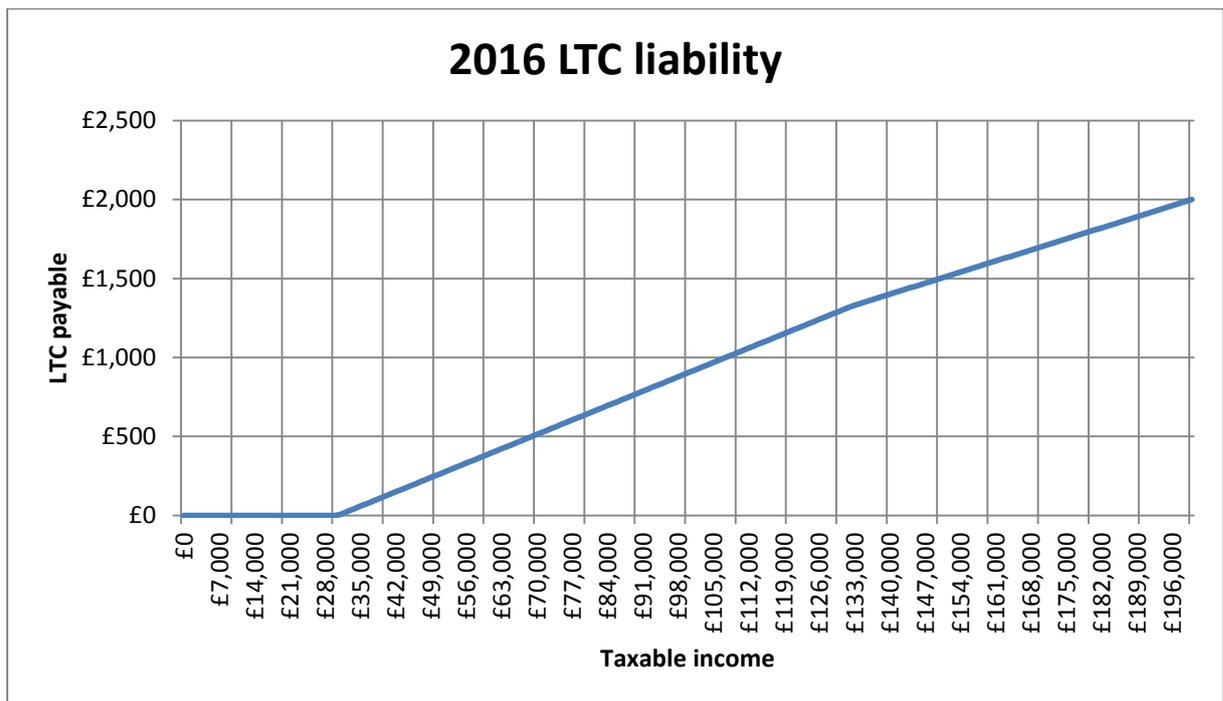
## 2016 Baseline Analysis

**Baseline for 2016 year of assessment**

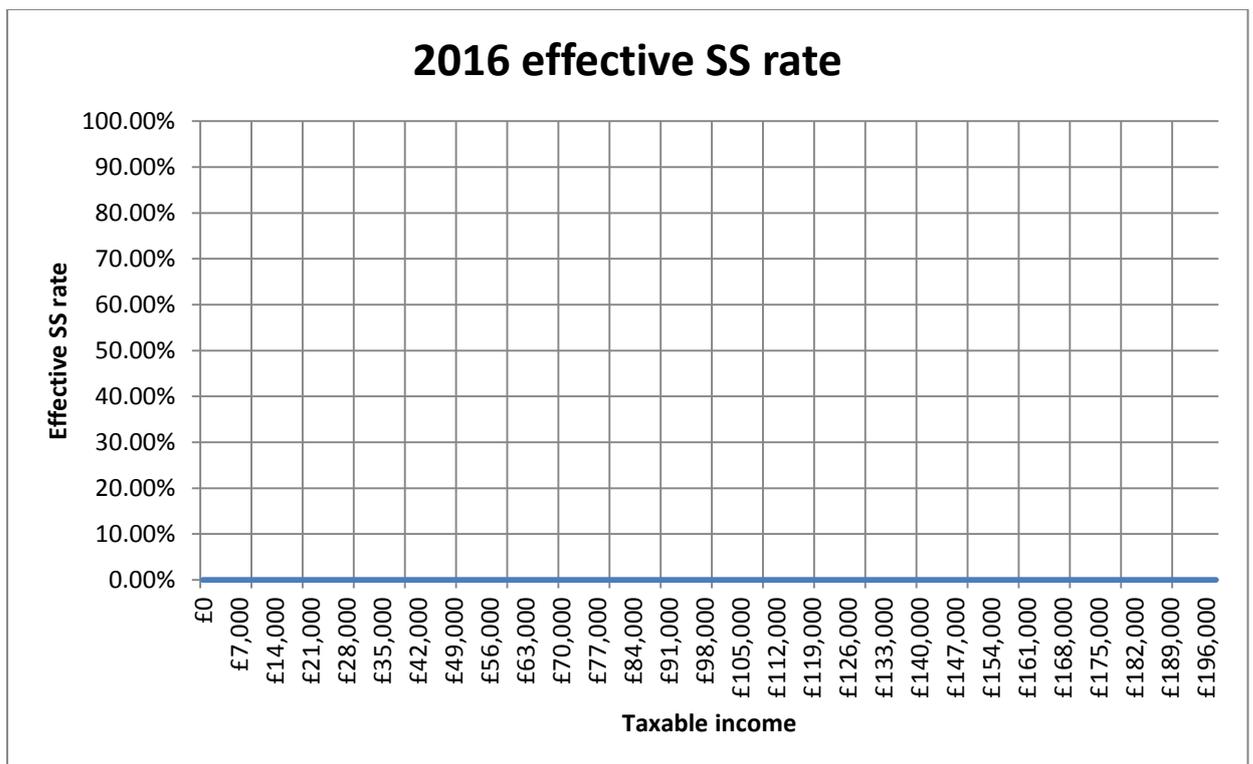
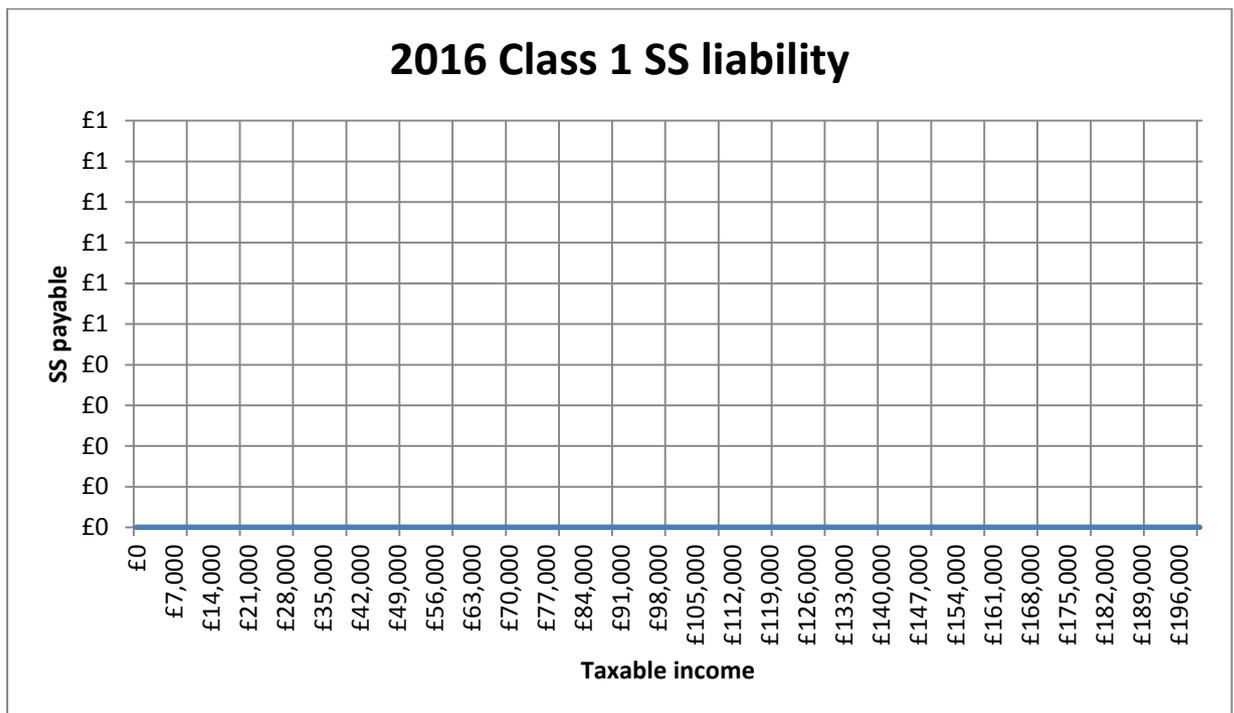
*2016 Baseline: married couple/65+ – Income tax*



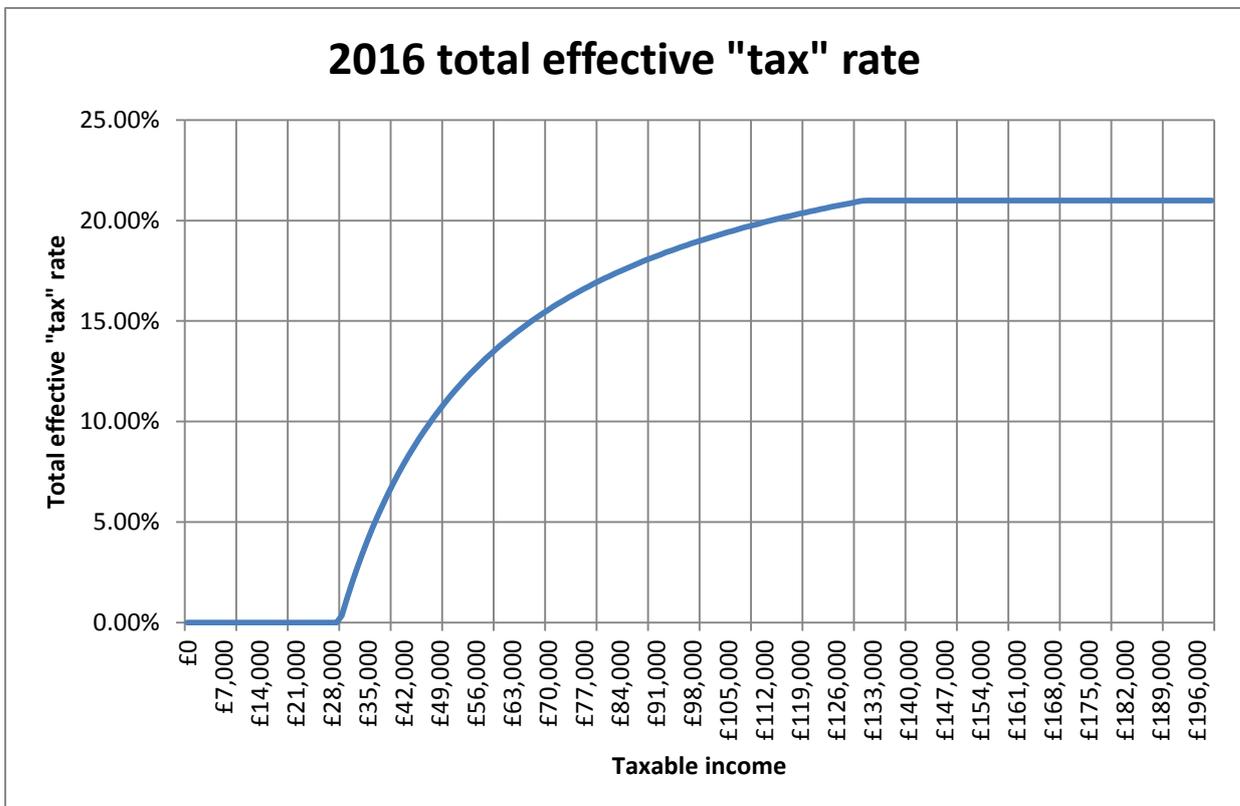
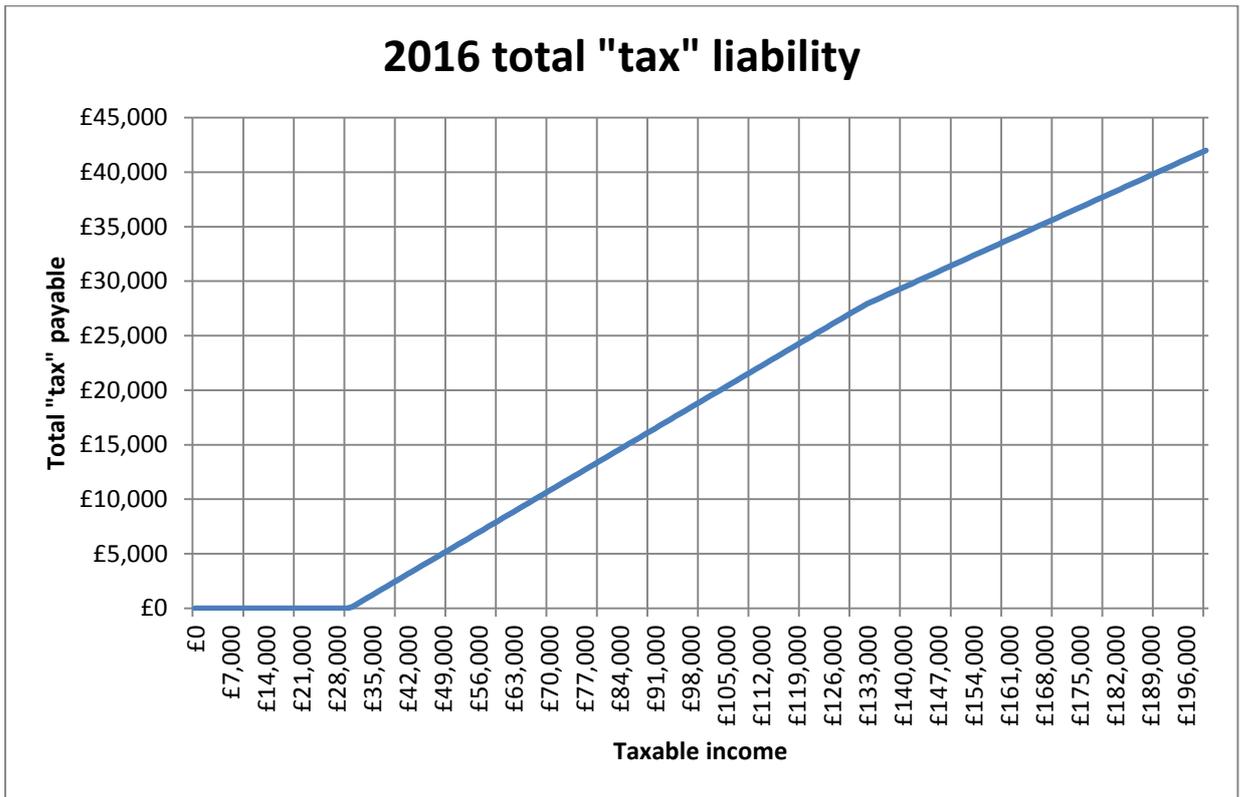
2016 Baseline: married couple/65+– Long term care contribution



2016 Baseline: married couple/65+ Social Security contributions



2016 Baseline: married couple/65+ Overall tax position

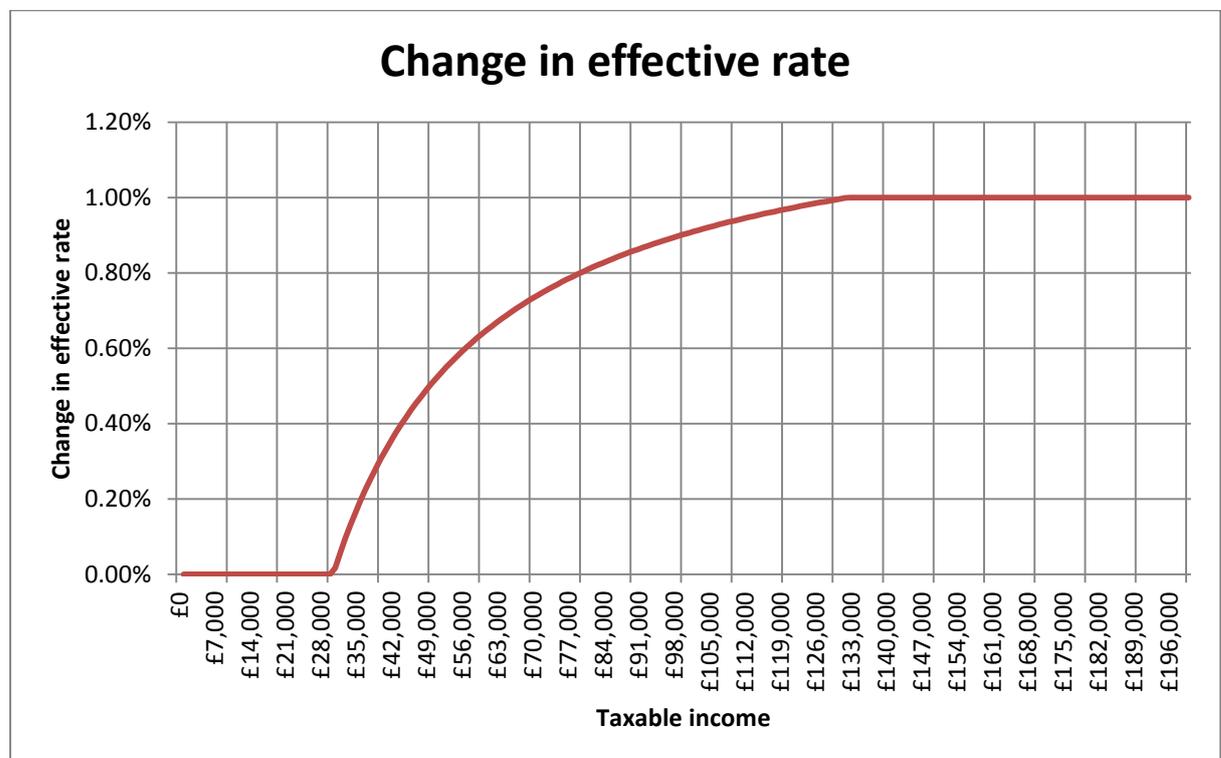
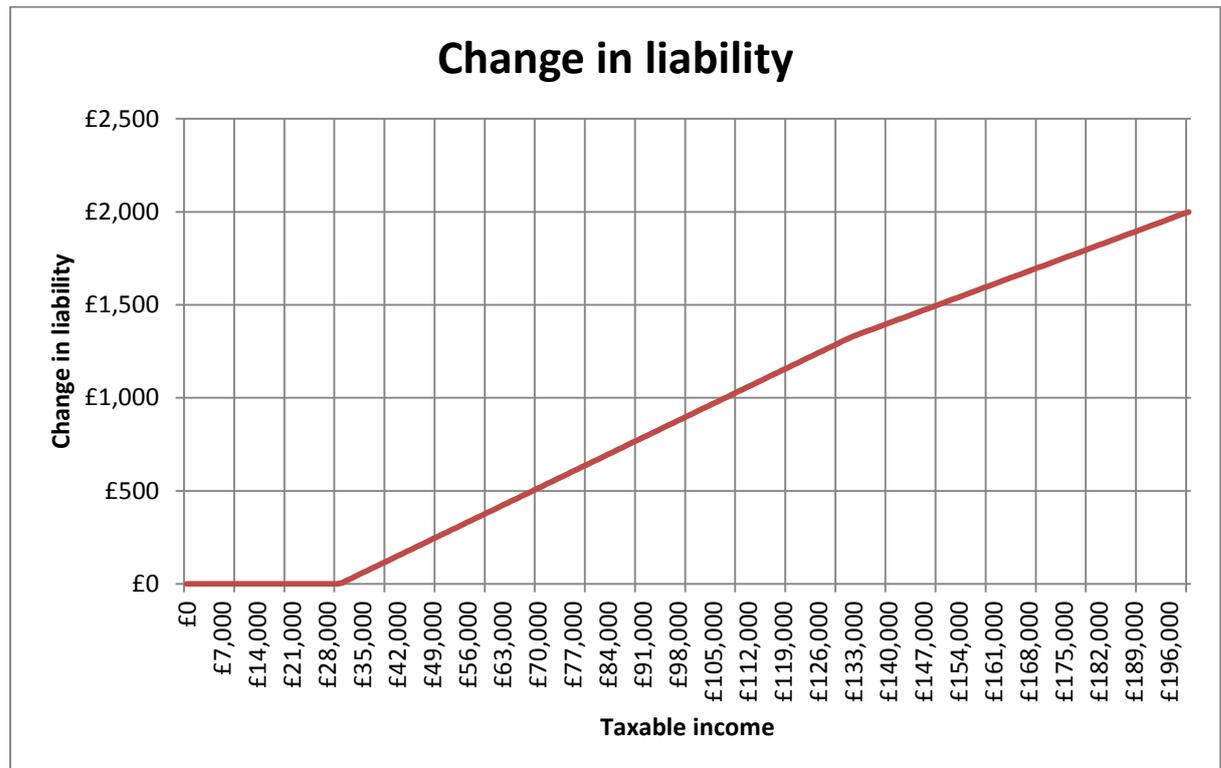


Household 4: married couple – 65+  
(assumed income split equally between  
spouses)

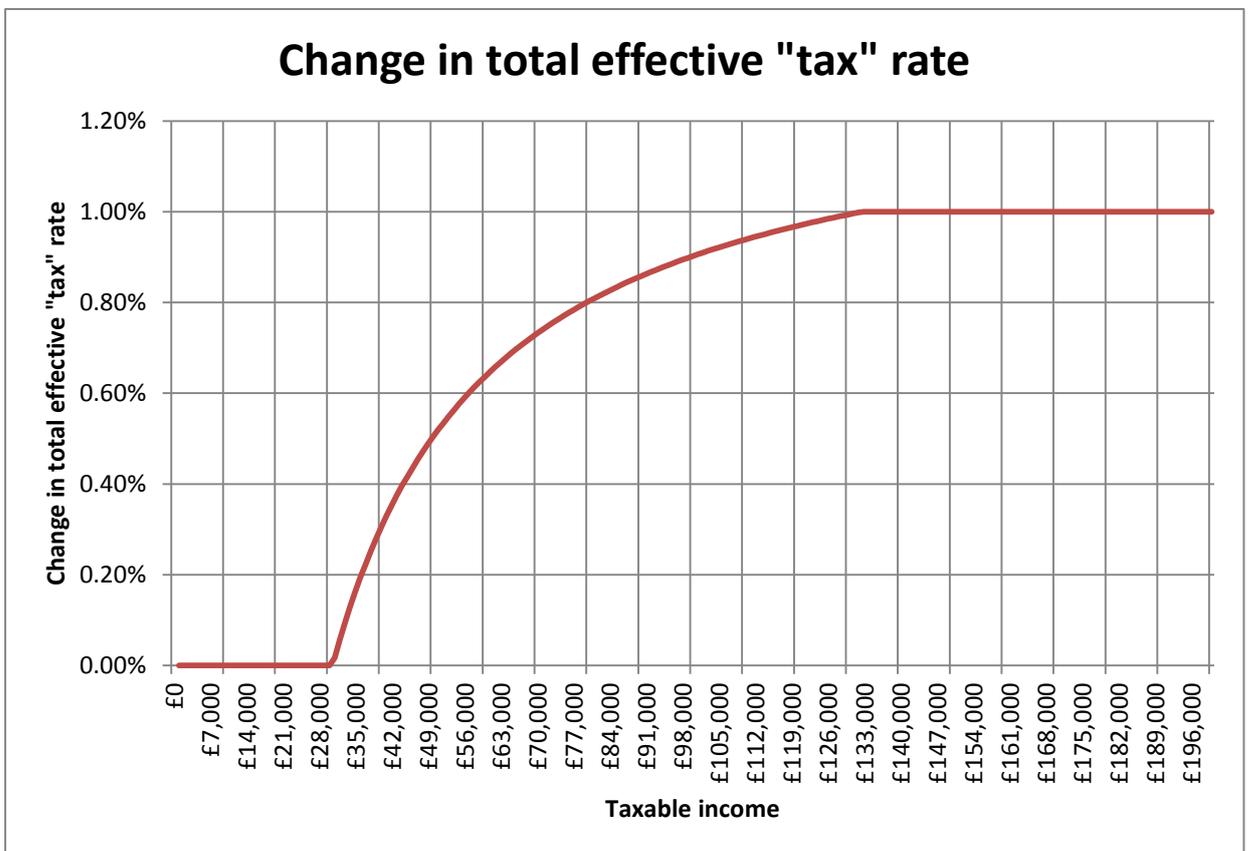
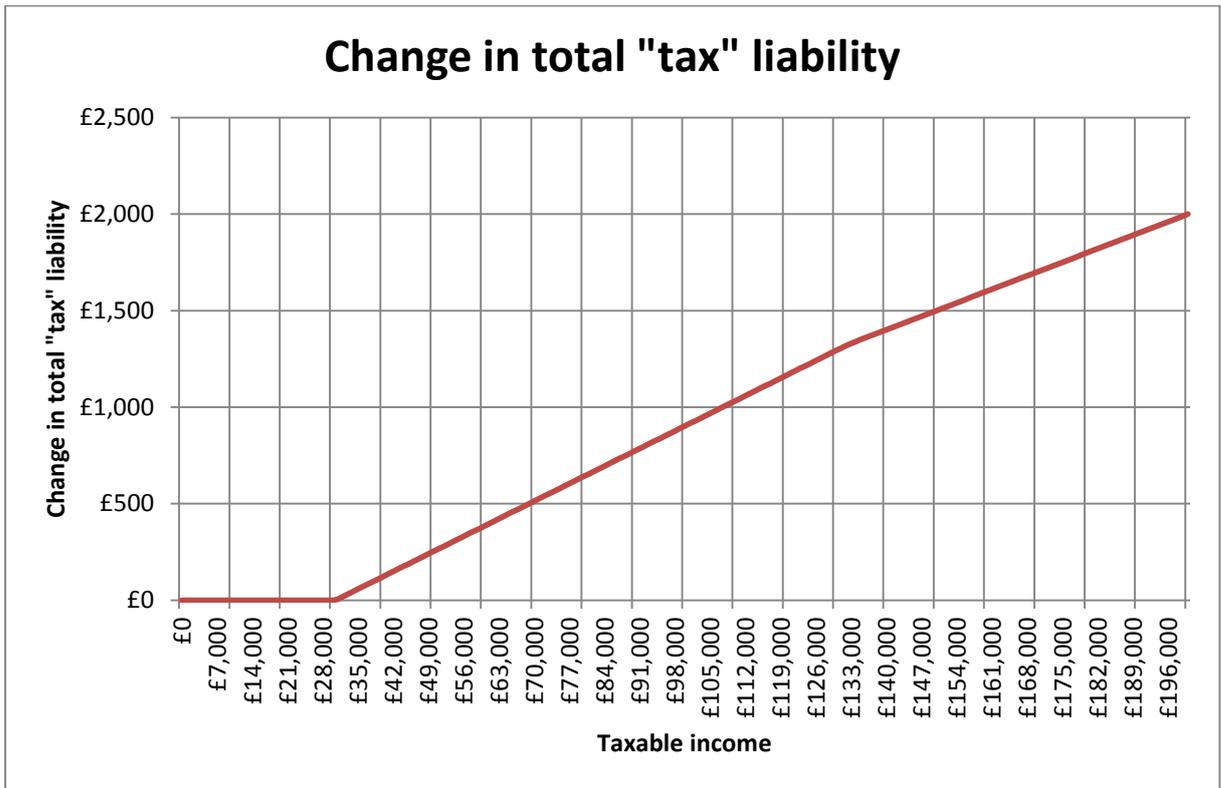
Option – introduce new LTC type charge

Option: introduce new LTC type charge

*Option: Introduce new LTC type charge of 1%: married couple/65+*



Option: Introduce new LTC type charge of 1%: married couple/65+ – Overall tax position

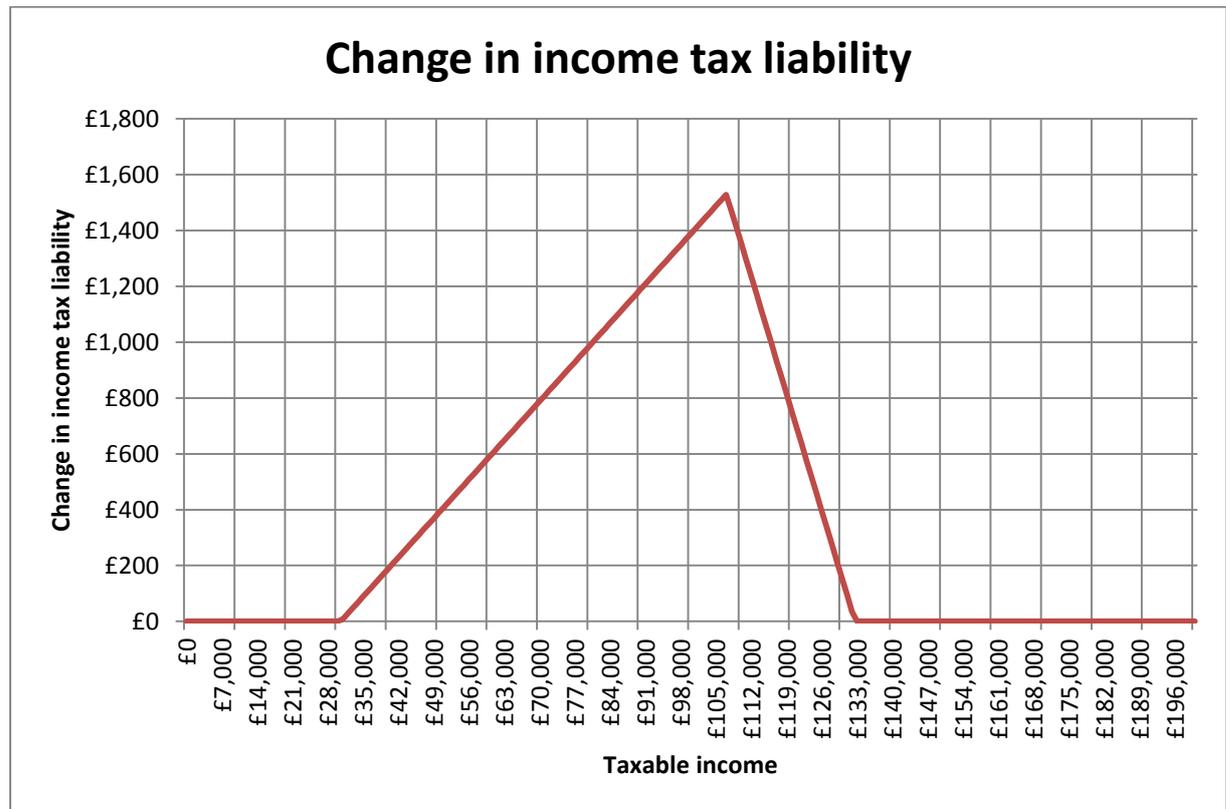


Household 4: married couple – 65+  
(assumed income split equally between  
spouses)

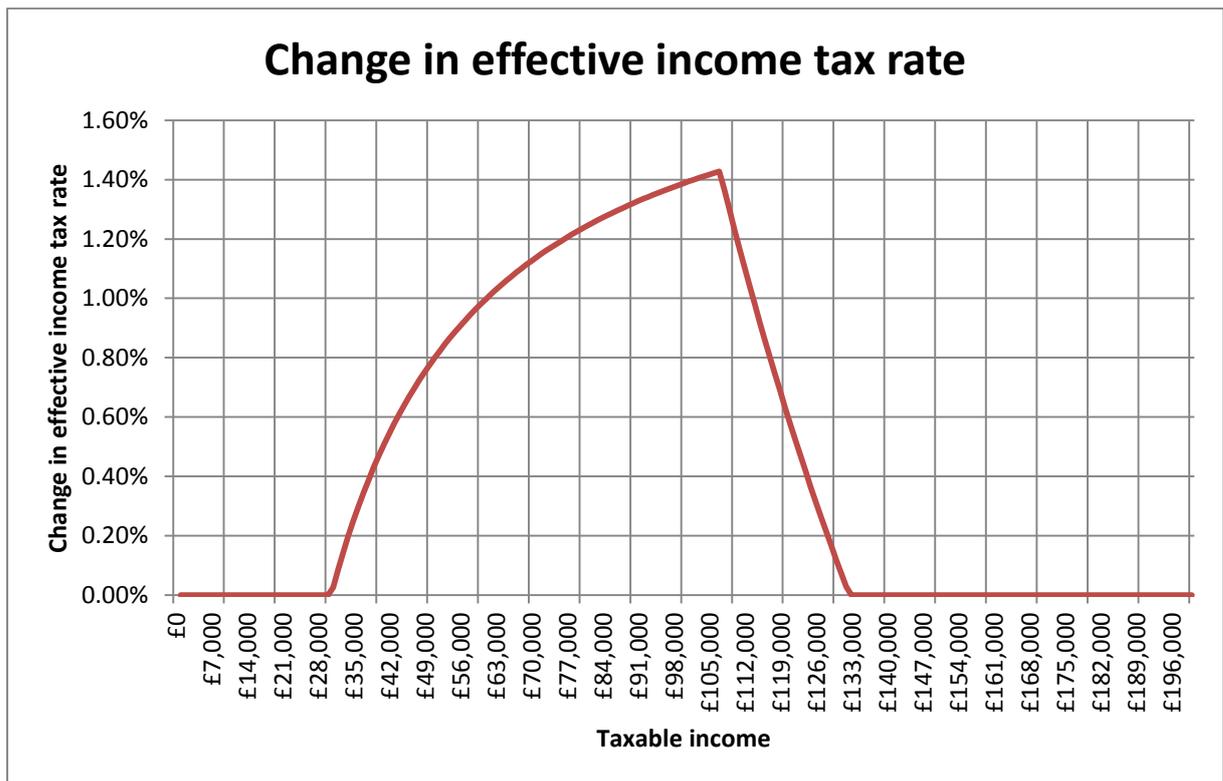
Option – increase marginal rate of income  
tax from 26% to 28%

Option: increase marginal rate of income tax from 26% to 28%<sup>24</sup>

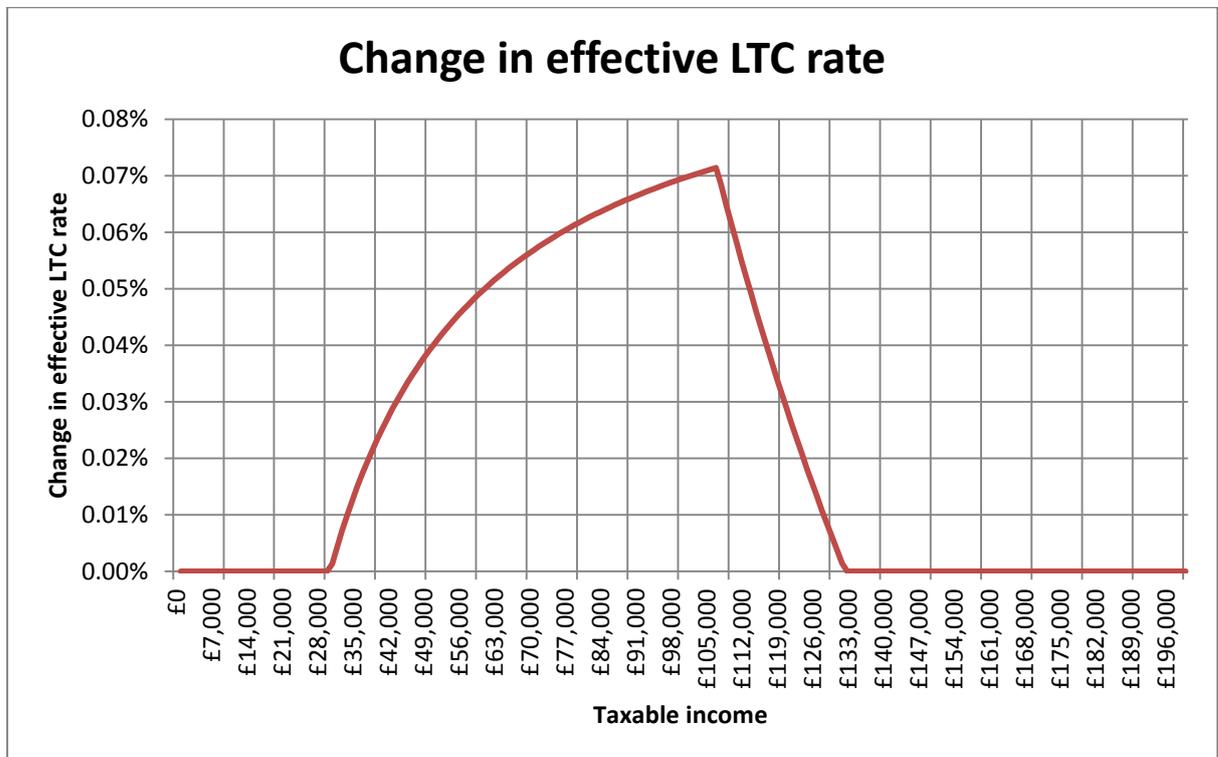
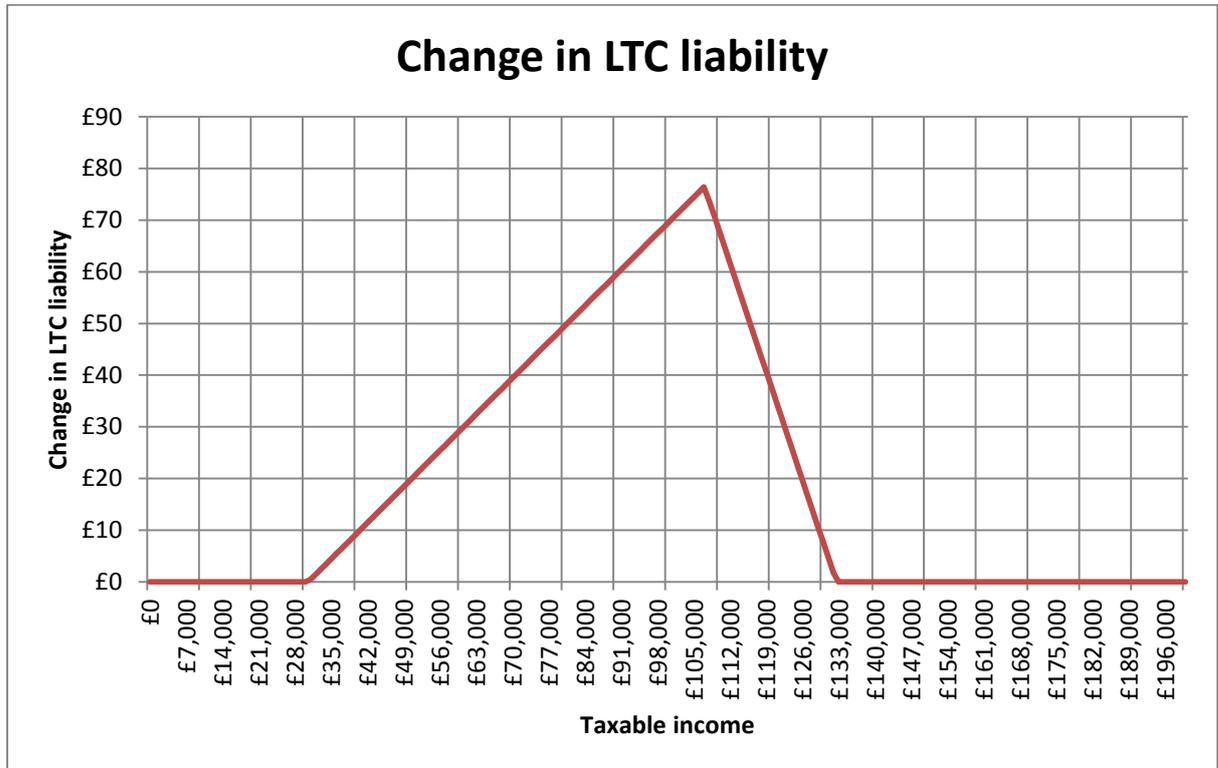
*Option: Increase MR of income tax by 2%: married couple/65+– Income tax*



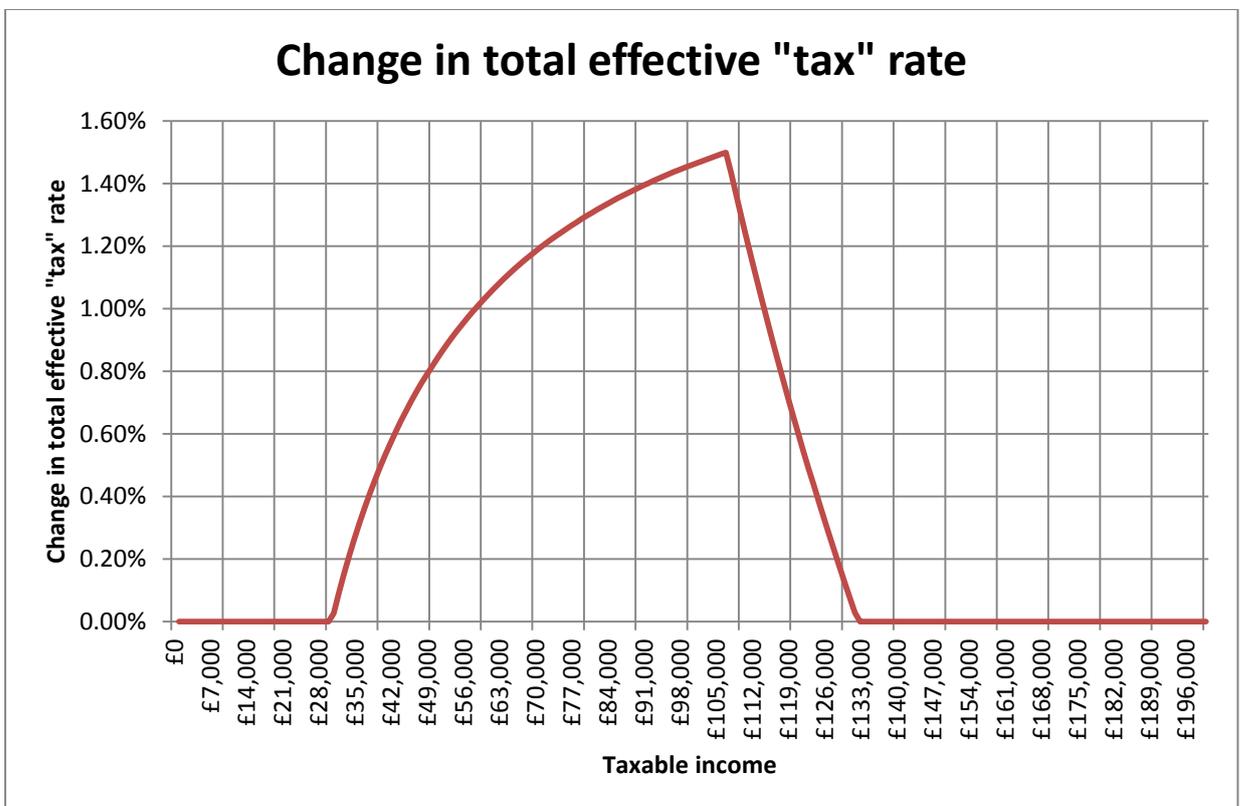
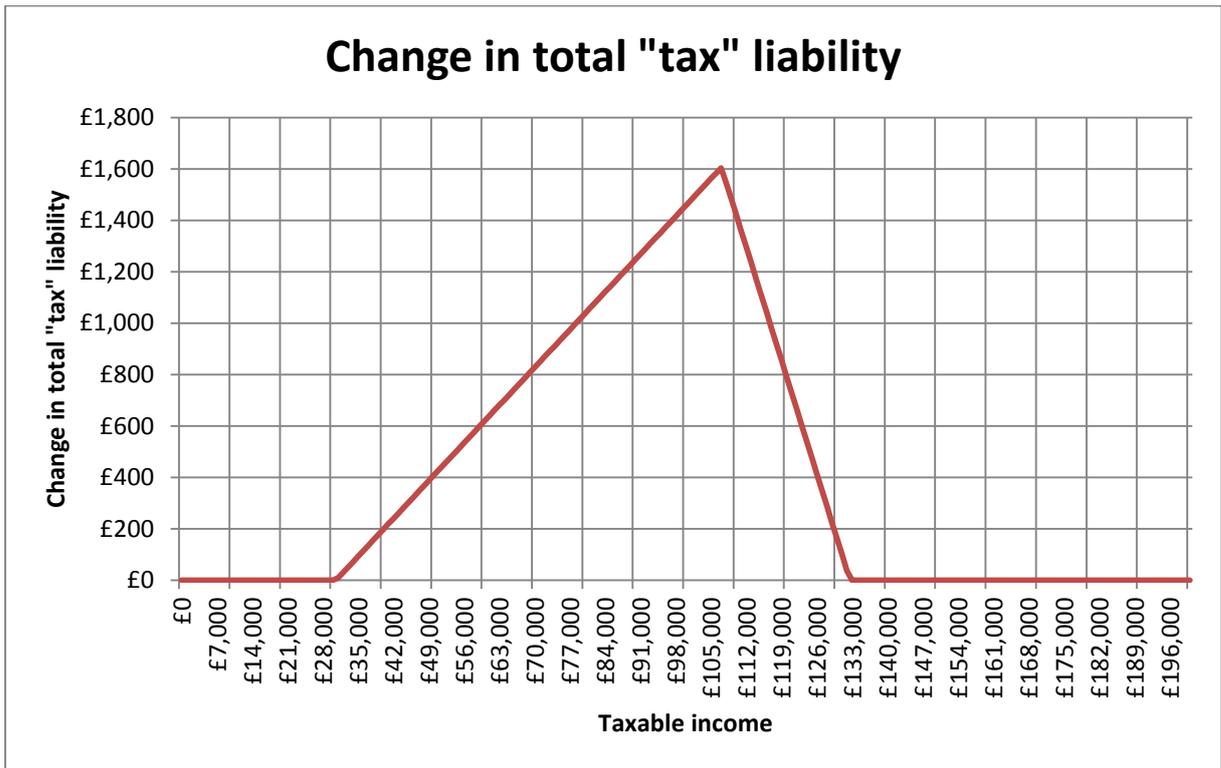
<sup>24</sup> Increasing the marginal rate of income tax to 28% will necessitate increasing the marginal rate of long term care contributions to 1.4%. The two marginal rates are interlinked.



Option: Increase MR of income tax by 2%: married couple/65+— Long term care contributions



Option: Increase MR of income tax by 2%: married couple/65+ Overall tax position

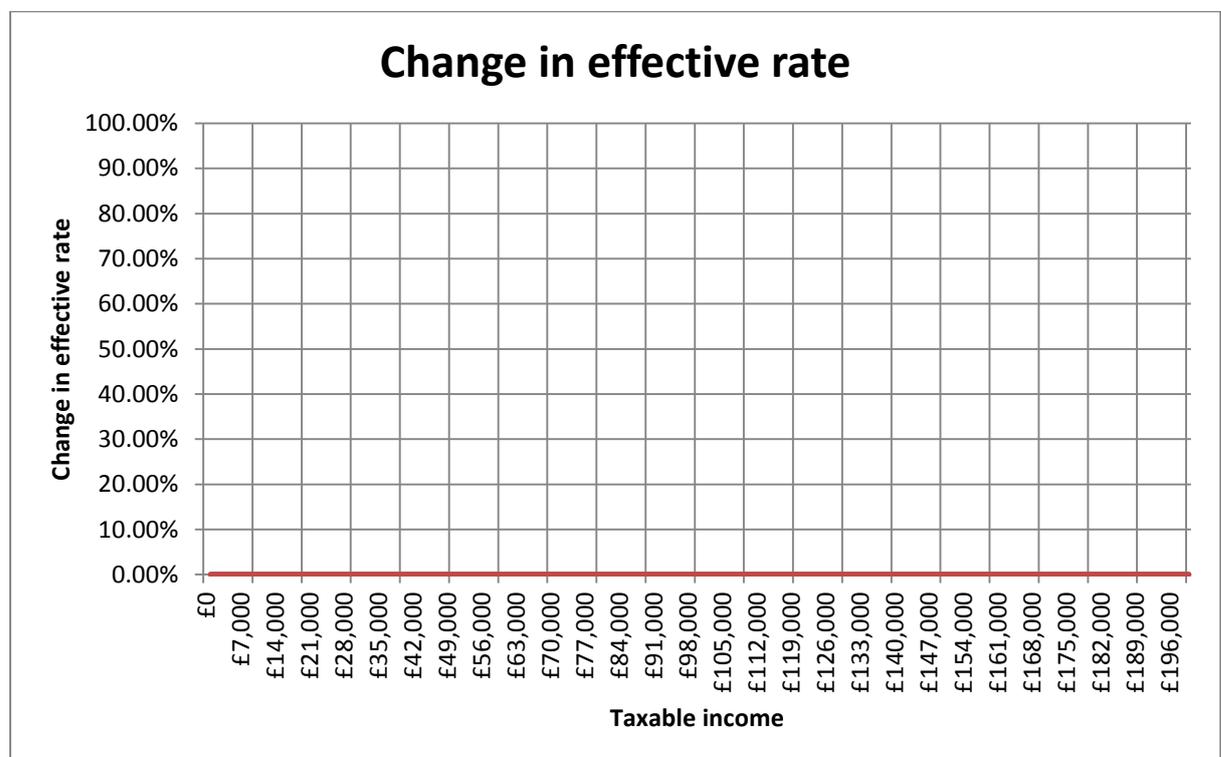
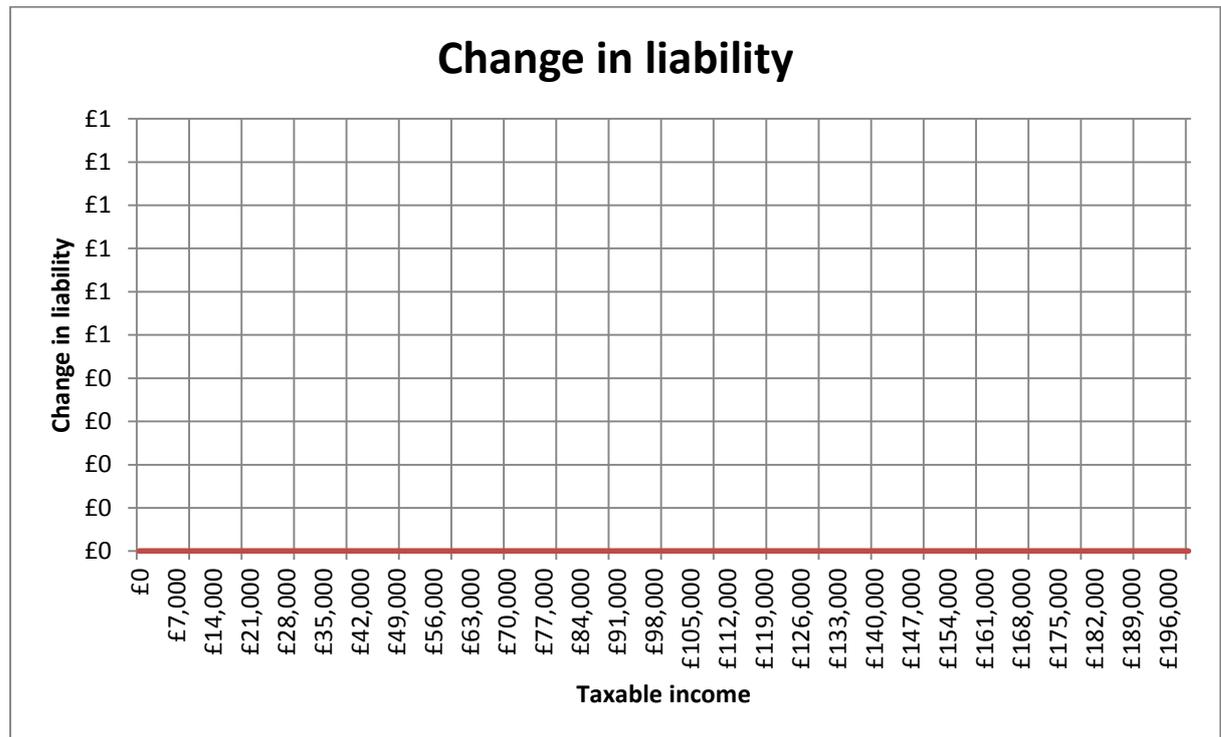


Household 4: married couple – 65+  
(assumed income split equally between  
spouses)

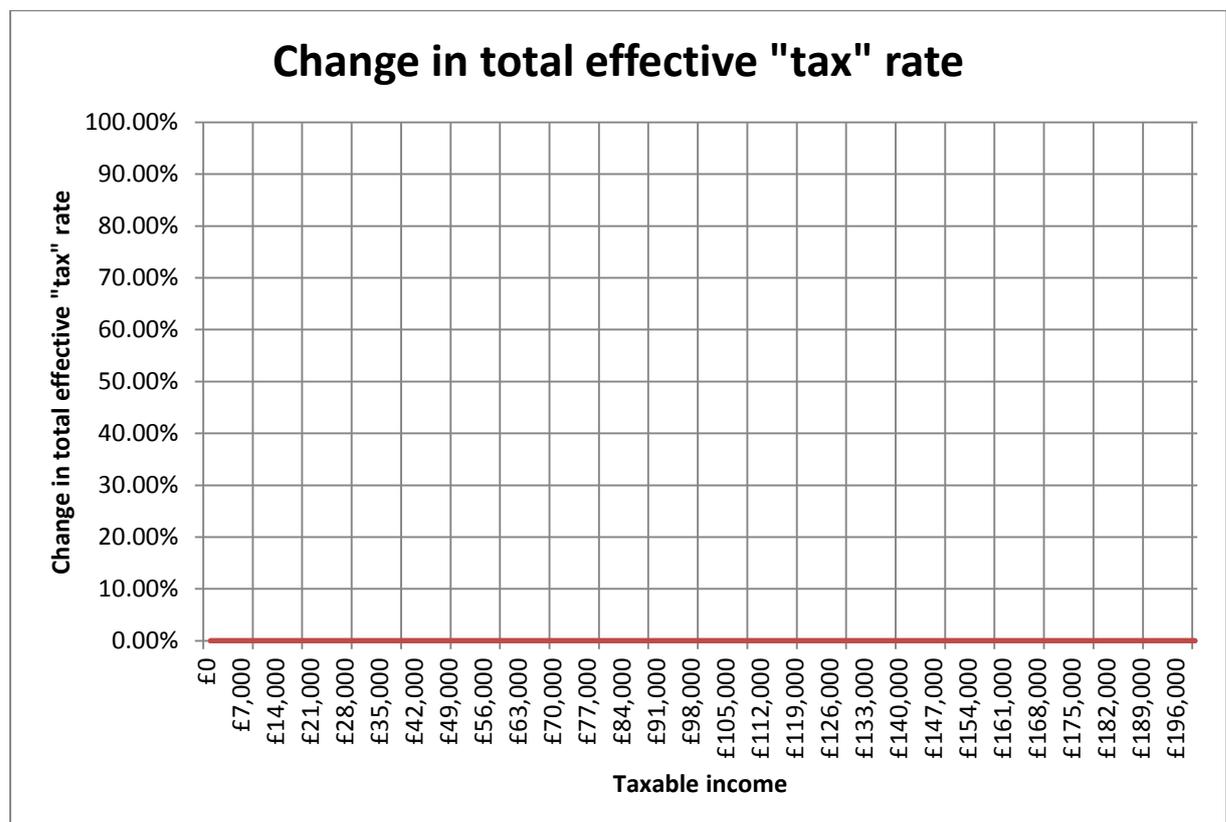
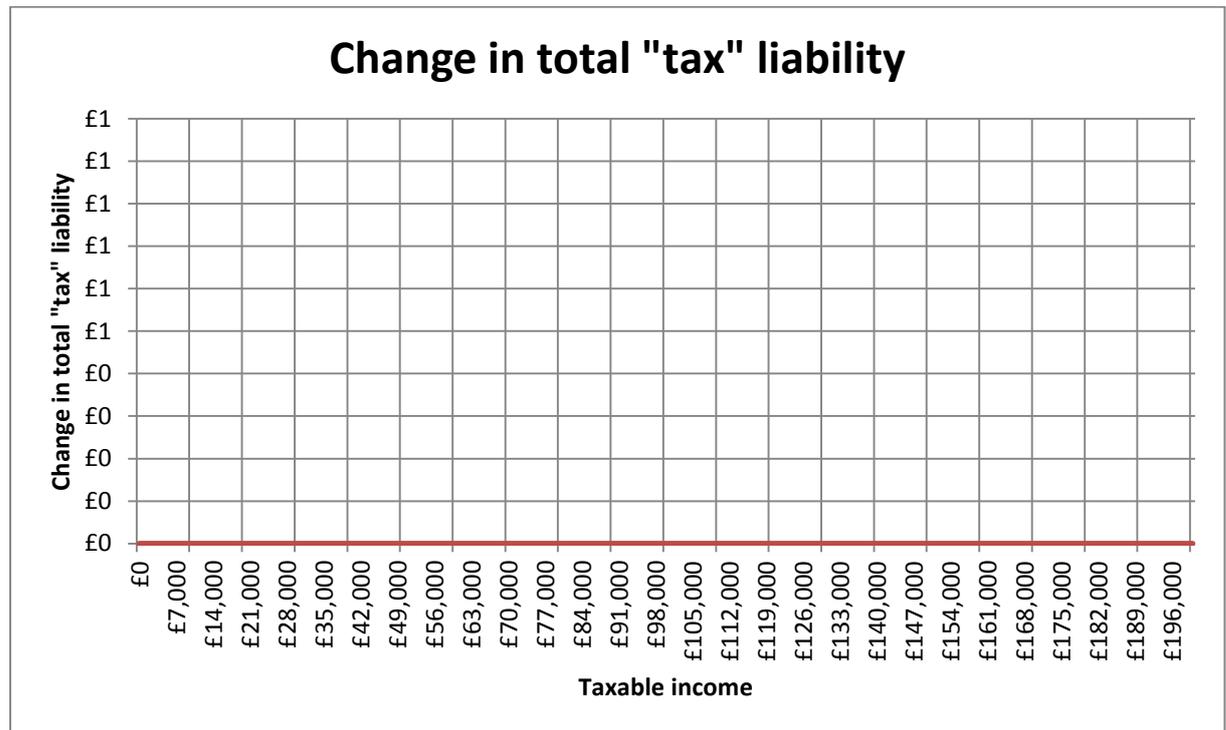
Option – introduce Social Security type  
charge below the standard earnings limit

Option: introduce Social Security type charge below the standard earnings limit

*Option: Introduce SS type charge below SEL of 1%: married couple/65+*



Option: Introduce SS type charge below SEL of 1%: married couple/65+ Overall tax position

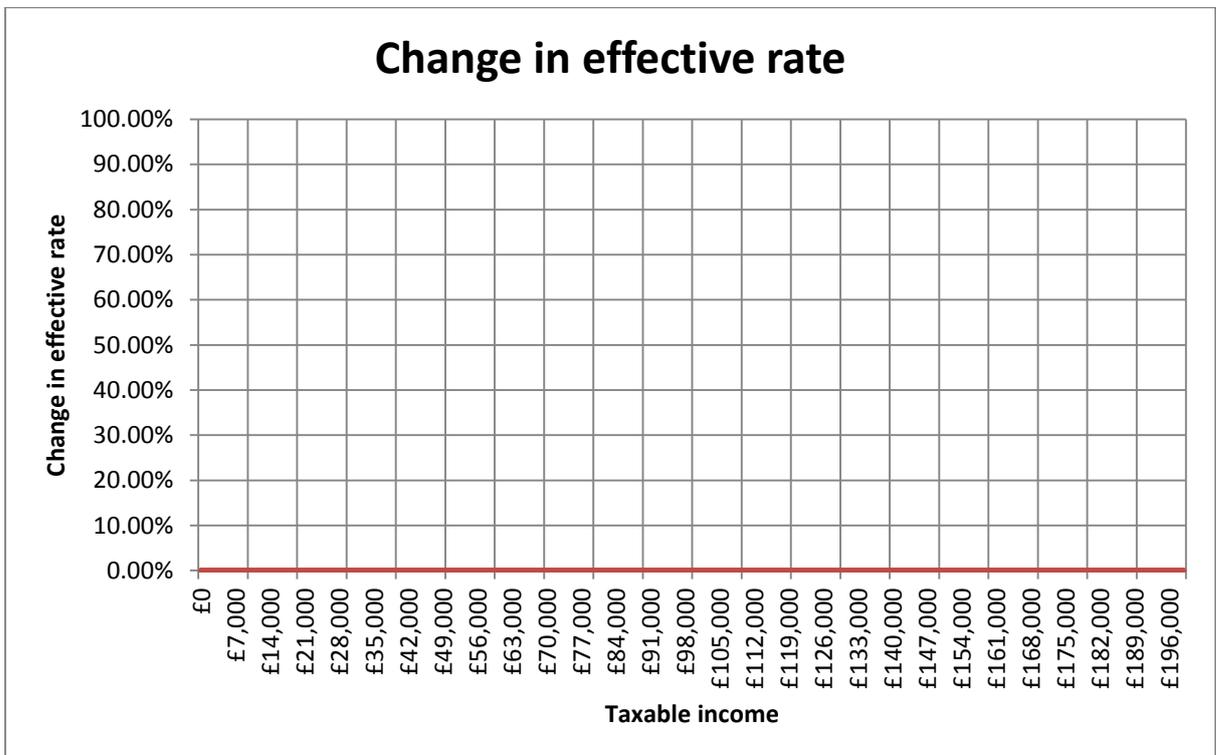
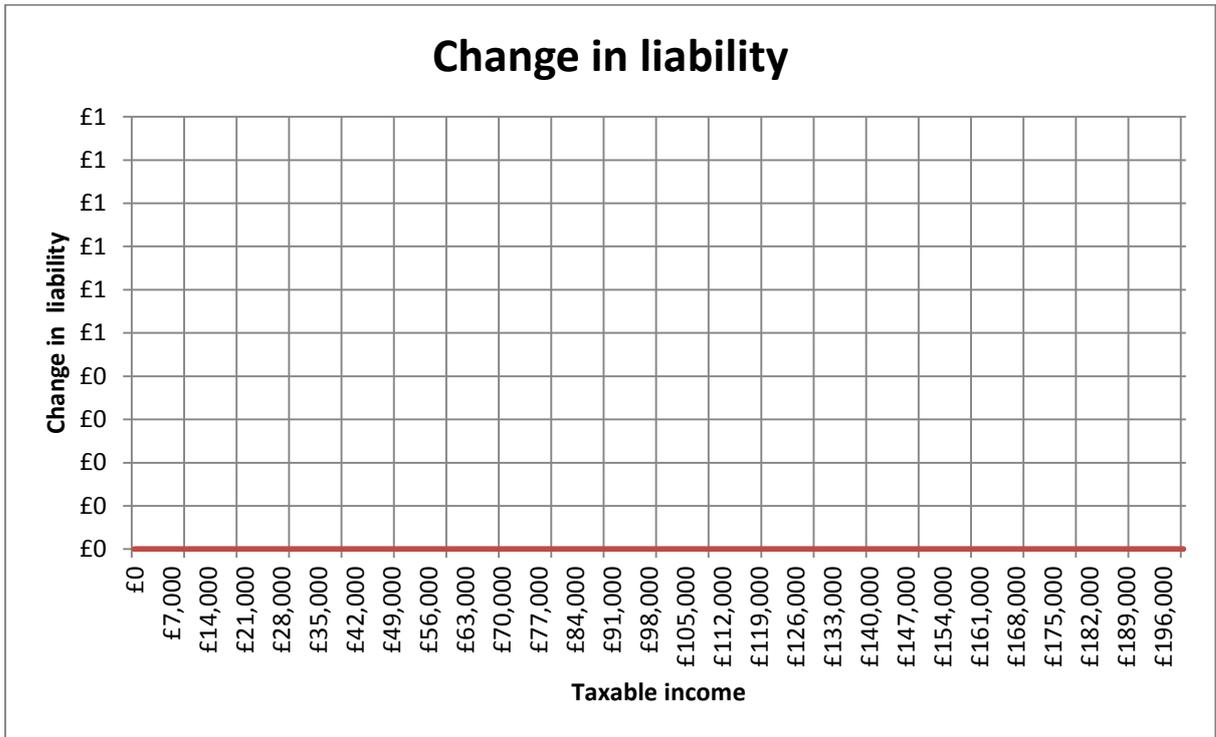


Household 4: married couple – 65+  
(assumed income split equally between  
spouses)

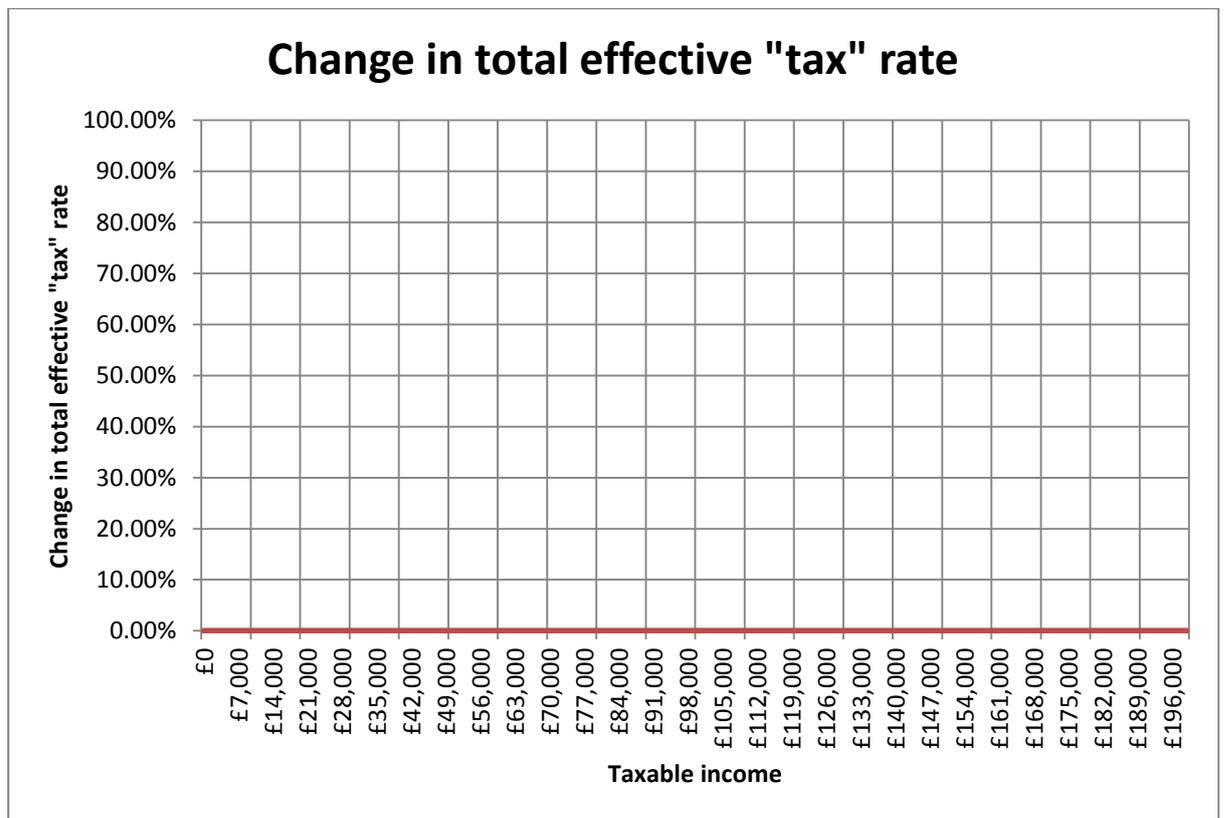
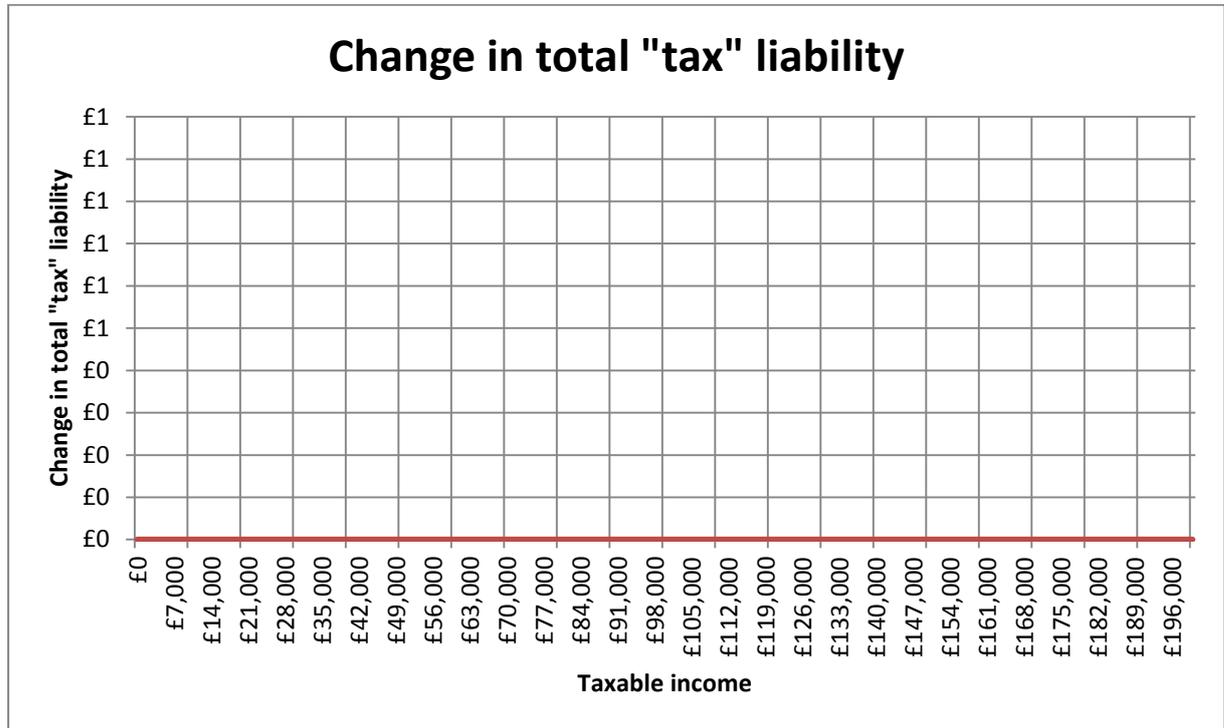
Option – introduce Social Security type  
charge above the standard earnings limit

Option: introduce Social Security type charge above the standard earnings limit

*Option: Introduce SS type charge above SEL of 5.5%: married couple/65+*



Option: Introduce SS type charge above SEL of 5.5%: married couple/65+ Overall tax position



#### 4.4 GST Distributional Analysis

There are several different ways to analyse the distributional consequences of GST. In particular, one can look at two different approaches:

- the proportion of **gross income** taken in GST
- the proportion of **expenditure taken** in GST

Using data from the Household Expenditure Survey (HES) it is possible to calculate how much households spend on GST by the level of their income.

However, looking at GST as a proportion of gross income is not be the only way of considering this. Other taxes may already reduce household income, and these may affect households differently. For example, one way to reduce the proportion of income taken from the lowest quintile in GST would be to raise the rate of other taxes on this quintile. This would reduce the money that these household have to spend, and thus reduce the amount of the GST as a proportion of income (although not necessarily disposable income).

Looking purely as a proportion of income, even disposable income, while important, does not necessarily tell the whole story. In particular, it shows a snapshot of spending and income patterns in the population at a particular moment in time, and may be misleading given the variability of income over a lifetime: those with low incomes now may be the young or elderly or temporarily out of work who will be, or have been, amongst higher income groups at other times. As the IFS notes, “given that households can smooth consumption over their lifetime, expenditure is a better proxy for lifetime resources than current income.”<sup>25</sup>

So under this measure, GST looks more regressive in part because those with high incomes tend to have high savings, and so appear to escape the tax. However, savings must be spent at some point, and they will be subject to the tax when they are. For example, people tend to spend more than their income when they are young and when they are old, while in-between they pay down debt and accumulate savings. Over the course of a lifetime, income will be broadly equal to expenditure (unless of course a large inheritance is left, but then the tax will be paid by the receiver when it is spent).

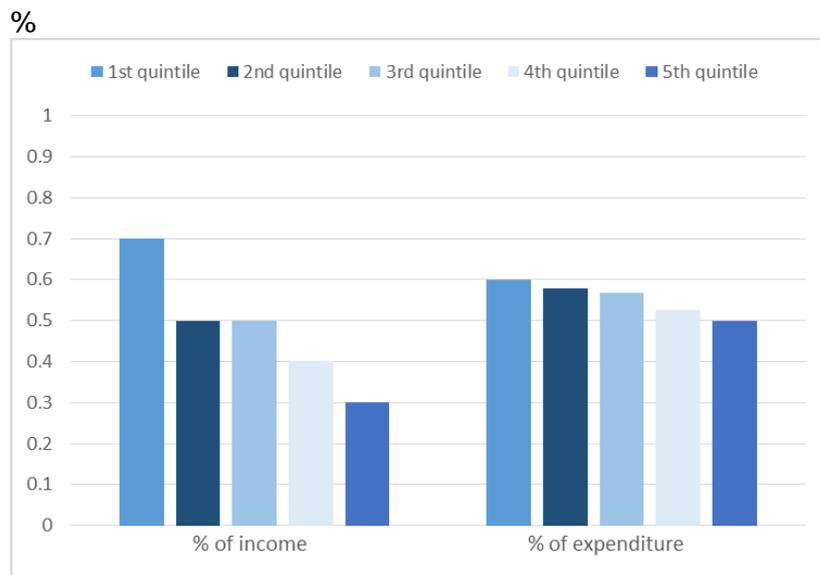
Looking at GST as a proportion of spending instead of income, addresses this concern to the extent that the latter is a better reflection of household’s perceptions of their own lifetime spending ability. As to be expected, this measure shows GST as less regressive than as a proportion of gross income.

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<sup>25</sup> Brewer, Browne & Phillips (2008) *The Distributional Effects of the 2008 Pre-Budget Report*.

Estimates of these two measures are shown below based on the 2014/15 household expenditure and income distribution surveys.

**Figure 40: Increase of 1% in GST as a share of income and expenditure across the income distribution**



Source: States of Jersey Statistics Unit/Economics Unit calculations

While the degree varies slightly by the measure chosen, GST is mildly regressive. This is mainly due to the effect on those households on the lowest incomes, which spend a larger proportion of their income on essential items such as food, domestic energy and so on.<sup>26</sup>

#### 4.5 Island-wide Rates Distributional Analysis

For residents there may be some relationship between the value of property and the income of the resident. If the rates payable are proportionate to the value of the property the impact may be largely neutral on average. However, this relationship is unlikely to be perfect and there will be circumstances of high tax liability, low ability to pay and vice versa.

According to the findings of 2014/15 Household Spending Survey the average amount of rates paid (Parish plus Island-wide rate) equates to about £300 per household per year. The split of this amount between Parish rate and Island-wide rate depends on the Parish however it is estimated that the split is approximately 60% Parish rate and 40% Island-wide rate equating to £180 of Parish rate and £120 of Island-wide rate.

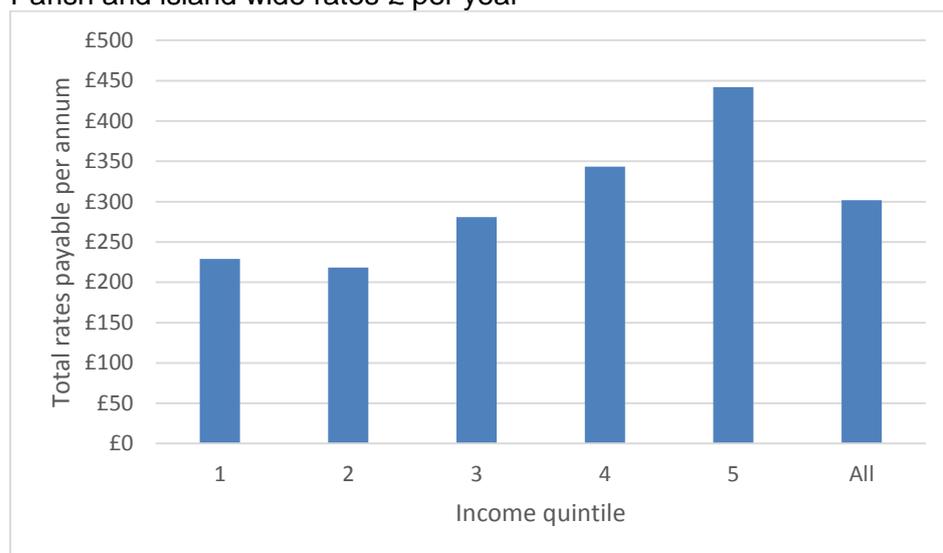
<sup>26</sup> For example, according to the HES, an average household in the lowest 20% of incomes spends 14% of their income on food, while an average household in the top 20% of incomes spends just 8%.

In 2015 approximately £6.6m was raised from the domestic Island-wide rate, therefore in order to raise the additional revenue target of £8m and £15m for the health charge the domestic Island-wide rate would need to be more than doubled in 2017 (to approximately £300 per household per year) and then doubled again in 2018 (to approximately £600 per household per year).

The figure below shows current expenditure on rates by equivalised income quintile:

**Figure 41: Expenditure on rates by income quintile**

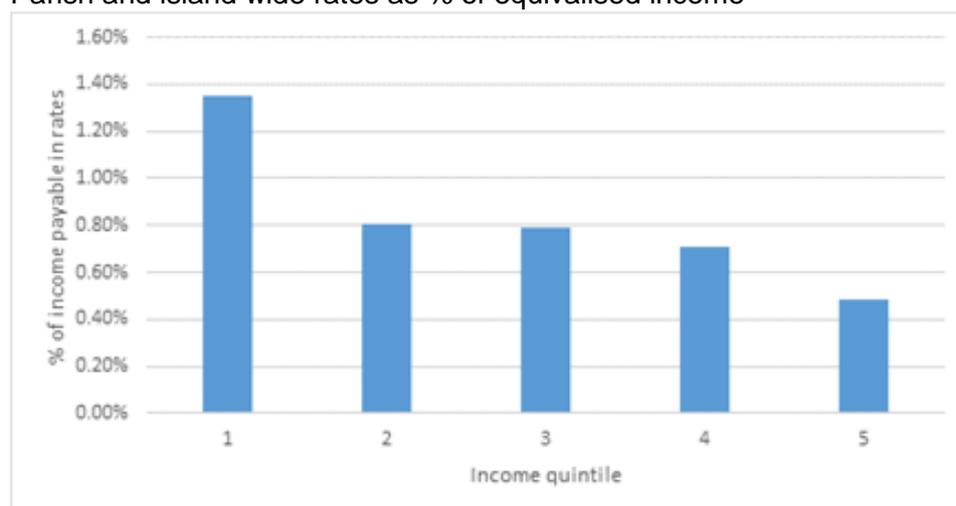
Parish and island wide rates £ per year



Source: Jersey Household Spending Survey 2014/15

**Figure 42: Expenditure on rates by income quintile**

Parish and island wide rates as % of equivalised income



Source: Jersey Household Spending Survey 2014/15

## Appendix 1: Terms of reference

In developing the approach set out in the MTFP 2016-19, the Council of Ministers has tried to balance twin economic objectives. Firstly, returning finances to structural balance, so that they remain on a sound and sustainable medium-term footing. Secondly, doing so in a manner that allows the economy to recover over the life of the MTFP. In doing this the advice of the independent Fiscal Policy Panel (FPP) has been critical and Council of Ministers has focused on following the Panel's recommendations set out in their reports in 2015. In particular, the FPP stated in their Pre-MTFP report that:

*“The States should develop a plan that will address any structural deficit by 2018 and 2019. Care should be taken to ensure that the range and timing of the measures minimises the risk to the economic recovery, which, in the early stages, may involve using the States’ reserves.”*

After seeing the proposals for MTFP 2016-19 the FPP stated in their September 2015 Annual Report that:

*“In general, the Council of Ministers has followed the Panel’s recommendations in its proposed approach in the draft MTFP.”*

*“In line with the Panel’s previous recommendations, the draft MTFP proposes to gradually withdraw fiscal stimulus from the economy as it recovers, and to use the States’ reserves to pay for this whilst the measures planned to bring the States’ finances back into balance are phased in.”*

The FPP’s advice in future reports will be critical in determining the overall approach in the MTFP and making sure that the economic impact is such that it allows the economy to recover and addresses any underlying structural imbalance in States finances at the right time. However, the fiscal measures – either changes in expenditure or revenue – will impact differently on different groups in the island community, as is the case with any fiscal adjustment.

The distributional analysis that will be undertaken on the measures set out in MTFP Addition 2016-19 will help the States to understand how the impacts may vary across households at different points in the income distribution. This will be informative for the States in understanding where the burden of the adjustment may lie and whether it is deemed to be fair. The measures that will be analysed and the type of analysis that will be undertaken is explained below:

## **1. Revenue Expenditure changes**

There are measures in the MTFP that see increased investment in key public services such as health and education and reduction in spending in other services through savings. It is generally much harder to determine the distributional impact of increases or investment in government expenditure than changes in taxation or cash benefits. However, the analysis will consider what evidence and research from elsewhere suggests about the distributional impact of changes in public expenditure (i.e. how it impacts on people at different points in the income distribution) in the service areas affected by changes in the MTFP and whether there are reasons to think the analysis is relevant for Jersey. In addition, it will look at what information is available about the nature of the changes in expenditure that are proposed as part the MTFP and whether there is any reason that the impact of the increases will be different to the overall distributional impact of general public spending in the service area.

## **2. Benefit Changes**

Considerable written information has already been provided during the MTFP process on the proposed benefit changes in respect of the legal changes that were required. Every individual change was subsequently challenged as part of MTFP debate and additional information was provided as part of the response. This analysis will therefore collate all information included in the public reports to show:

- Number of claimants affected by one or more changes
- Demographic info on these claimants
- Approximate weekly impact of changes in 2016 (i.e. at current prices)

The economic assumptions used for the MTFP Addition will be used to show the impact on typical benefit claimant households over 2017 – 2019. Consideration will also be given to any implications for changes in behaviour.

## **3. Capital Expenditure**

It may be even harder to determine the distributional impact of changes in public capital expenditure than current expenditure. However, the analysis will consider what evidence and research from elsewhere suggests about the distributional impact of public capital expenditure and whether it is relevant for Jersey. In addition, it will look at what information is available about the nature of the changes in capital expenditure that are proposed as part of the MTFP and whether there is any reason that the impact of the changes will be different to the overall distributional impact of public capital spending.

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## **4. Revenue raising measures**

### **i. General revenue raising measures**

For each proposed revenue raising measure which applies to the population of the island generally, the analysis will indicate the distributional impact of the measure on a range of different households. Wherever appropriate the analysis will be produced in graphical form to aid understanding and to highlight the resulting change in effective tax rates at differing income levels.

### **ii. Charges/User Pays**

The analysis will consider what evidence and research from elsewhere suggests about the distributional impact of user pays charges, including those in health for the different services or departments (i.e. how they impact on people at different points in the income distribution) and whether there is reason to think the analysis is applicable to the proposals for such charges in Jersey.

### **Timescales**

Some of the analysis of measures that have already been decided will be undertaken in March/April e.g. revenue expenditure investment in health/education and benefit changes. However, some of the analysis will not be able to start until there is a clearer direction in terms of the actual policy e.g. revenue raising measures/ revenue expenditure savings, although it is intended that this work will be done in April/May. This will enable the inclusion of the impact analysis in the MTFP Addition when it is lodged at the end of June 2016.

### **Recommendation**

The Council of Ministers are asked to approve the approach set out in this paper.

## **Treasury and Resources**

**February 2016**