Sent: 03 April 2005 22:15

To: Scrutiny

Subject: Tax reforms

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Dear sirs,

I have recently been in communication with a number of States Members on the subject of the proposed Tax reforms, and having spoken to Dep. Phil Rondel this week, have summarised my points here, and ask that you include these in your forthcoming scrutiny of the proposed tax changes.

The question I raise is essentially simple - " ***If Guernsey can manage to move to 0/10 tax without the introduction of a GST - then why can't we?"***

The starting point was the realisation that duty rates in Guernsey are substantially lower that here (petrol duty is 6 pence per litre in Guernsey, 36 pence here, diesel is the same here, but free in Guernsey, alcohol is also lower, etc). Having challenged Sen Walker of the issue, he explained that there are 2 fundamental differences between the 2 Islands - Guernsey Income Tax allowances are less generous than ours, and they account for capital expenditure in a different way than we do.

I have finally received a confirmation from Sen le Sueur that this is the case (attached). The difference is that we calculate the size of the tax deficit (or surplus) after deducting capital expenditure for the year, and Guernsey don't. This meant that whilst we are calculating a shortfall of £80m to £100m, Guernsey are only estimating their shortfall to be about £45m. However, if you deduct our current capital programme expenditure of about £43m, our "black hole" is suddenly exactly the same as theirs - coincidentally the same amount that is due to be raised by the GST.

This means that if we changed our accounting for capital expenditure to the 'Guernsey method', the argument for the introduction of a GST is immediately removed. The question is - are Guernsey burying their heads in the sand, being overly optimistic and assuming that economic growth will help to fill the void - or are we being overly cautious, or negative, and counting on a GST to fill the void? Dep Lyndon Trott's assertion rings true, that GST is a government's 'soft option', as they can increase it relatively easily once it is in place, without the need to seriously address public-sector spending.

If we end up with GST and Guernsey do not, we will be even move un-competitive than we already are, compared to our sister Isle. Moreover, despite the assurance that it will be only 3% for the next 3 years, there is every likelyhood that it will increase after this time. If my theory is valid, then our ability to generate a 2% economic growth will be seriously in doubt, as any new business will gravitate to a low-duty, no-GST jurisdiction - Guernsey!

It does seem to me that despite being in this position due to pressure from the EU, we are not looking beyond our shores when it comes to implementing a solution. Surely we cannot purposefully put ourselves in an anti-comptitive position with our nearest neighbour, and primary competitor in the Tourism and Finance sectors?

So far, I have not seen any aknowledgement in the public domain that the difference in our respective 'black holes' is due to the way that we account for capital expenditure. It is not my style to start a JEP ' war of letters' on the subject, so I would appreciate a reply confirming that you have received this email, and will investigate my points. I would be happy to supply the panel with copies of the relevant correspondance with Senators Walker and le Sueur, and be interviewed if necessary.

Yours faithfully,

27/04/2005

Chris Parlett

States of Jersey

Senator Terry Le Sueur
President,
Finance and Economics Committee.
Cyril Le Marquand House,
St. Helier,
Jersey, JE4 8UL.

21st March 2005

Our Ref: TLES/D/JM

Dear Mr Parlett,

In response to your email of 13th March 2005, please find below information regarding the differences in accounting for capital expenditure between Jersey and Guernsey.

In presentational terms, the Jersey budget shows gross income, deducts funds allocated for revenue expenditure and capital expenditure for that year, leaving a surplus or deficit which is added to, or deducted from, the capital fund.

The Finance Law actually deducts funds allocated for revenue ('cash limits') from gross income, places the balance into the capital fund and the States vote out an agreed sum for capital expenditure. For example:

Income	£500m
Revenue Expenditure	£460m
Transfer to Capital Fund	£ 40m
Sums Voted for Capital Projects	£ 45m
'Deficit' in year	£ 5m

The sum voted for capital is the amount required to meet the anticipated outturn cost of the capital project - **not** the amount of cash expected to be spent in the year covered by the budget. For example, a school costing £20m and built over 2 years would require the whole £20m to be voted in year 1, rather than £10m each year.

Furthermore, the Public Finances Law does not permit there to be an overall deficit in the Capital Fund. Thus, the above scenario would not be permitted unless there was at least £5 million previously available to be brought forward.

This approach is prudent and results in a balance of voted but unspent funds - the States invests these funds and the interest received is credited to general revenues.

Guernsey

The difference between income and revenue funding requirements is Guernsey's 'headline' surplus and is appropriated to reserves including the capital reserve (which is why Guernsey appear to have a higher declared surplus than Jersey). For example:

Telephone: 01534 603215 Facsimile: 01534 789901 E-mail: t.lesueur1@gov.je

Income	£300m
Revenue Requirement	£250m
Declared Surplus	£ 50m

Appropriation to Capital Reserve £ 50m (may not be all of the surplus - could be appropriated to Guernsey's equivalent of the Strategic Reserve etc.)

Capital funding is provided both from capital allocations from General Revenues and capital funds allocated from the capital reserve.

The funds allocated to a capital project from the Capital Reserve are recorded as a movement in the Capital Reserve balance, e.g.:

Sum voted from capital (say) £60m

Movement in Capital Reserve -£10m (i.e. the difference between the £50m appropriated and the £60m withdrawn).

The key difference is that Guernsey only 'votes' an estimate of the funds required in the year and retain an unspent balance in the capital reserve.

Arguably, this is a less transparent way of budgeting for the full cost of a committed capital scheme.

If Jersey shifted to the Guernsey basis in 2005, the headline deficit would improve by the sum allocated for capital (£43m in 2005).

Funding would need to be voted to cover the estimated capital expenditure in year, so the 'net' budget deficit would reduce by the difference between the estimated outturn cost of the capital projects and the estimate of the cash required for expenditure in 2005.

However, to ensure that sufficient funds were available to meet the future capital commitment, the 'surplus' shown would need to be appropriated to the Capital Fund and would not be available to spend as revenue funding.

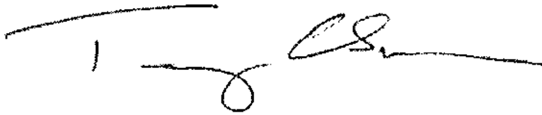
The key point, therefore, is that a difference in presentation does not provide more revenue on an on-going basis.

With regards to Guernsey's policy on how to address EU and competition issues relating to its corporate tax structure, it is currently unclear as to their future intentions. Whilst Guernsey has indicated for some time that it will move to a 0/10% corporate tax structure, it has not yet formally agreed to do so. Furthermore, it is unclear how Guernsey will resolve the resulting fiscal deficit following such a move to a 0/10% regime. Whilst Guernsey has indicated that it will not introduce VAT, it has not ruled out introducing a form of GST in the future.

I hope the above explanation has addressed the issues you have raised.

May I take the opportunity in thanking you for your thoughtful contribution to the debate.

Yours sincerely



Senator Terry Le Sueur
President, Finance and Economics Committee