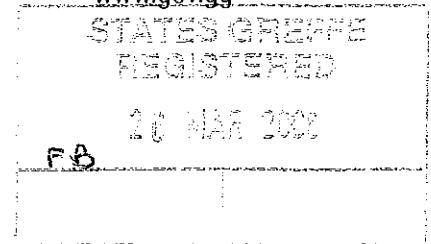


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Your Ref: 515/4(4)

Deputy G Southern
Chairman
Economic Affairs Scrutiny Panel
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Morier House
Jersey
JE1 1DD



16 March 2006

Dear Deputy Southern

ECONOMIC AFFAIRS SCRUTINY PANEL – FULFILMENT INDUSTRY

Thank you for your letter of 10th March in connection with your Panel's review into the Jersey fulfilment industry. I am replying to your letter in the absence of Deputy Falla, the Minister, who is away from the Island.

I am indeed aware of Senator Ozouf's policy announcement, because the Economic Development Department and the Commerce and Employment Department have been in dialogue on this issue and we agreed to issue similar – but not identical – policy statements.

You will find attached the Guernsey version of this policy statement. In it you will find that in direct accord with Jersey, Guernsey has clearly stated that while it supports "Whole Chain Companies", particularly those that have grown from an indigenous base, it has set its face against third party fulfilment operations. Where the statements differ, is in the remedies available to the two Islands.

As I am sure you know, Guernsey does not have a Regulation of Undertakings Law or its direct equivalent, nor are these particular operations required to be licensed in any way. What we do have is Housing Control legislation – administered by our Housing Department.

Under these arrangements, a third party fulfilment operator, or indeed any fulfilment company, seeking to bring in key staff without residential qualifications will require a housing licence, e.g. for a Managing Director or specialist IT people. The Housing Department will consult with Commerce and Employment prior to determining a licence application. As the policy makes clear, we are unlikely to give support to such licences and although, ultimately, this is a matter for the Housing Department, which is not bound to take our advice, in all likelihood, if an application does not enjoy this Department's support then the Housing Department will be unlikely to grant it.

A further limiting factor in Guernsey is the availability of commercial accommodation with an appropriate use class to enable fulfilment to take place.

Against this background, I am sure that while some companies currently trading through Jersey may indeed explore Guernsey as an alternative, I do not share your view about a real shift of business from your Island to ours, given our stand on the housing licence situation and, in particular, the lack of available space.

I note your request for economic impact information and our views about the potential effect of any action that might be taken by HM Government, together with an invitation to meet with you and to provide a written submission to the Panel or to act as a witness for your review. However, I would ask your Panel to regard this response and the accompanying policy as the limit of the Commerce and Employment Department's contribution to your review and I must decline to explore this further or to become engaged in any formal submissions to, or appearance before, your Panel.

While clearly there are matters of mutual interest here for both Islands and indeed they have been explored through discussions between Economic Development and Commerce and Employment, it is our view that the work of your Scrutiny Panel is essentially a political process internal to Jersey and it would be entirely inappropriate for Guernsey politicians to become engaged more directly in this or other reviews.

On the assumption that this is the first such request to emanate from one of the new Jersey Scrutiny Panels to a Guernsey Department, I have copied this letter to our Chief Minister with a recommendation that the Policy Council should consider how Guernsey Departments might best respond to any such requests in future.

Yours sincerely



Carla McNulty Bauer
Deputy Minister

Enc.

Copy to: The Chief Minister, Policy Council, States of Guernsey



POLICY FOR THE FULFILMENT INDUSTRY

Introduction

1. Previous research on the nature of the fulfilment industry in the Island has thrown some light on the activity at a time when it is attracting some negative publicity which is in danger of undermining the Island's good international reputation and integrity. The negative publicity is focusing on existing UK companies that are switching the distribution of their DVDs/CD's through the Channel Islands to take advantage of the Low Value Consignment Relief (LVCR – the EU approved mechanism for VAT exemption).
2. This paper sets out a policy that can maximise the benefit of the fulfilment industry while at the same time not damage the Island's international reputation or integrity.

The economic benefits

3. There are basically two types of activity within the fulfilment sector, although a number of companies operate as a hybrid of the two activities.
 - Whole Chain Companies (WCC) physically buy in and own the stock and sell the goods to the final customers. WCC receive revenues based on the total value of sales.
 - Third Party Service Providers (3PS) on the other hand provide logistics or distribution services to other retailers. 3PS only receive revenues based on the service they provide, with the sales revenue going to the retail company.
4. The Department's Building Confidence and Economic Statement (BC and ES) contains the key objectives of creating the conditions that:

The optimum direct and indirect economic benefits are derived from business activities on the Island to benefit the community as a whole; so that

The working population has increased opportunities to migrate into jobs with higher earnings potential.

On purely economic growth grounds the dichotomy within the fulfilment sector means that the appropriateness of the two types of activity for the Island is significantly different. Generally the high value added per employee and significant tax contribution of WCC activity means that it is fully complementary to the BC and ES and therefore should be supported by the States wherever possible.

5. 3PS activity contributes less significantly and the States should therefore be much more cautious about this type of activity. Significant growth in employment in this sector poses two questions:
 - Where will this labour be drawn from – the unemployed/new labour market entrants or other industries/firms?
 - Could the labour be put to more productive uses?
6. The answer to the first question is that while some of the existing employees might have come from the unemployed or new labour market entrants there are greater concerns that further jobs growth will start to bid up wages in this area and therefore undermine activity of all firms in the sector and possibly other sectors such as tourism.
7. The very low value added per employee of 3PS activity also suggests that the labour could be put to better use in other areas such as tourism and retail.
8. On pure BC and ES grounds the conclusion should be to support WCC activity but actively discourage further growth in 3PS activity, where it requires significantly more labour.
9. The impact of the fulfilment industry does not however, stop here. BC and ES issues also have to be balanced with those surrounding the Island's international reputation and compliance with good practise in Fair Trading terms.

The policy

10. The appropriate policy (for further details see notes below) that meets both the BC and ES and protects the Island's international reputation and integrity is:
 - (i) Established WCC should be supported, particularly those that are or have been majority beneficially owned by Guernsey principals.
 - (ii) New WCC which are beneficially owned by Guernsey principals and in conformity with the principles of BC will generally be supported.
 - (iii) With the exception of those companies trading in DVD/CD's into the UK market, high value hybrid companies should be supported, where they do not involve UK companies diverting current business through the Island.
 - (iv) New UK companies will not be encouraged to operate through 3PS in the DVD/CD market. (It is recognised that whilst the Island may be seen as an attractive location for this market, the reality is that the limited land and labour resource that is available has to date ensured that this market has not developed locally).

Notes

11. WCC are as previously defined – companies that physically buy and sell goods to final customers and receive revenues based on the total value of sales and are generally owned by locally qualified principals.
12. 3PS are as previously defined - they provide logistics or distribution services to other retailers and only receive revenues based on the service they provide, with the sales revenue going to the retail company.
13. Hybrids are fulfilment related companies that do not fit easily into either category but have a permanent establishment with some or all of their core activities in the Island such as a head office, finance, purchasing, marketing or customer service. Hybrids employ locally qualified people in high value jobs, make a significant local tax contribution and stock is owned and possibly held by the local business. Their pick and pack operations are likely to be carried out by a 3PS but could be done by the company itself. There could also be companies that operate as both WCC and 3PS.

Implementation

14. For the policy to work:

- The Policy Council will undertake any international relations work.
- The Commerce and Employment Department will take note of the above in considering requests for support for both Housing licence applications and permissions for change of use etc forwarded from the Housing Department and Environment Department respectively.
- The States of Guernsey will explore the potential to curtail or vary the service offered by Guernsey Post within the constraint of the legal and regulatory framework.
- The States of Guernsey will encourage Guernsey Post to take such steps as it is able in order to curtail any business of Guernsey based 3PS carrying out fulfilment activity in the DVD/CD market in accordance with 10 (iv) above.
- Commerce and Employment Department will continue to monitor the fulfilment industry and will consider amendments to this policy in the light of significant developments elsewhere.