STATES OF JERSEY

FISCAL STRATEGY

Lodged au Greffe on 8th March 2005
by the Finance and Economics Committee

STATES GREFFE

PROPOSITION

THE STATES are asked to decide whether they are of opinion −

to refer to their Act dated 29th June 2004 in which they approved the States Strategic Plan 2005 to 2010 and agreed that the States would take steps to maintain a strong and competitive economy and to provide high quality public services, and to their Act dated 7th July 2004 in which they approved the Fiscal Strategy and charged the Finance and Economics Committee to research measures to mitigate the loss of taxation revenues as a result of the agreed changes to the corporate taxation structure, and –

(a) to agree that a progressive package of tax and benefits, capable of generating additional net annual tax revenue of £55 million, should be implemented, and that–

(i) a broad-based Goods and Services Tax (GST) will be introduced in 2008 at a rate of 3%, fixed for at least 3 years, as set out in the summary of proposals, page 40, of Section 2 (the accompanying Report of the Finance and Economics Committee;

(ii) the proposals being brought forward for approval by the Employment and Social Security Committee, in liaison with the Finance and Economics Committee, will include provision to ensure that the effects of GST on those on low incomes will be mitigated through enhancements to benefits implemented prior to, or simultaneously with, the introduction of GST;

(iii) tax allowances for taxpayers on higher disposable incomes will be phased out over a period of 5 years in the manner set out in the summary of proposals, page 43, of Section of the said report;

(b) to approve the introduction of imputation provisions requiring Jersey residents to pay personal tax based upon the profits of the Jersey companies in which they have a beneficial interest, (known as ‘look-through’ arrangements), by 1st January 2009 as outlined in the summary of proposals, page 47 of Section 2 of the said report;

(c) to agree that enhanced anti-avoidance measures and new information powers as outlined in the summary of proposals, page 50, of Section 2 of the said report should be introduced no later tha 1st January 2009;

(d) to charge the Finance and Economics Committee, working with the Environment and Public Services Committee, to undertake further research, and bring forward for consideration proposals relating to the introduction of environmental taxes, primarily aimed at meeting the environmental objectives of the States Strategic Plan 2005 to 2010, including –

(i) additional taxes on the ownership and use of motor vehicles, on the production and disposal of waste, and on the consumption of energy;

(ii) a development gains tax to be considered in conjunction with the development of a planning gain policy.

FINANCE AND ECONOMICS COMMITTEE

CONTENTS

	Page
Executive Summary	**5**
Introduction	**10**
Section 1: The need to reform Jersey's taxation structure	**11**
◡ Why change to 0/10%?	11
◡ Options for filling the £80-£100 million deficit	20
◡ Problems with Jersey's current tax structure	22
• Excessive dependence on direct taxation	22
• Over-reliance on corporate taxes	24
• Jersey's low taxes	25
• Widening the tax base	26
◡ Tax options for raising £55 million	29
◡ Principles applied in assessing the main tax options	30
◡ Comparison of the main tax-raising options against the criteria	32
• Fairness	32
• Efficiency, simplicity, flexibility	33
• Economy and employment	33
• Diversifying the tax base	35
◡ The Finance and Economics Committee's overall conclusion	37
Section 2: The Finance and Economics Committee's proposals	**38**
◡ Goods and Services Tax (GST)	38
◡ Income Support System	41
◡ 20% means 20%	42
◡ 'Look-through' arrangements and selective taxes	44
◡ Anti-avoidance measures	50
◡ Environmental taxes	51
◡ Development levies	56
Section 3: Alternative tax options	**62**
◡ Payroll Tax	62
◡ Income Tax changes	65
◡ Capital Gains Tax	68
◡ Wealth tax	69
◡ Taxes and Inflation	71
◡ The next steps	71
◡ Financial and manpower implications	72

- **Appendix 1: Examples of the impact on households of 20% means 20% proposals** **74**
- **Appendix 2: Examples of the impact of the Income Tax Option on typical households** **85**

EXECUTIVE SUMMARY

WHY JERSEY NEEDS TO CHANGE ITS TAXES

Jersey is changing the way it raises taxes in order to safeguard the economy. This means that we can maintain our current way of life; our standard of living, our high quality public services, our pleasant environment and full employment for local people.

The States has agreed that in 2008 it will introduce a 0% rate of tax on the profits of most companies, but a 10% rate of tax on the profits of companies in areas such as the financial services sector. These measures safeguard our economy but, as a result, Jersey's tax take is expected to fall by up to £80-£100 million a year by 2010.

Six years of research and analysis by successive Finance and Economics Committees shows that if Jersey does not reform the way it taxes companies, the international financial services industry will, over time, move away from the Island. The result would be a huge fall in Jersey's tax take – in the region of £200-£250 million a year The stark prospect is that without changing taxes, the Island's economy could enter a downward spiral. Moving to 0/10% is the better option by far.

The move to 0/10% is not designed to 'feather-bed' the financial services industry, nor is it being 'soft' on business. The primary motive is to safeguard Jersey's economy, its quality of life and public services, now and for future generations, and to provide continuing and rewarding employment opportunities for Islanders.

There is no magic way of recouping the tax Jersey will lose by moving to 0/10%, but in July 2004 the States agreed (P.106/2004) to implement 4 measures –

- growing the economy (generates £20 million);
- cutting waste and increasing efficiency in public services (saves £20 million);
- introducing the Income Tax Instalment System (ITIS) (raises £5 million);
- increasing taxes (raises the remaining £55 million).

The Economic Growth Plan proposes a framework in which the economy can produce the target growth of 2% a year.

The Public Sector Change Programme will reduce States spending. It will make the States work better and more efficiently by the introduction of simpler, shared processes. Improving the efficiency of the public sector will save £20 million a year.

The Income Tax Instalment System, a simplified form of Pay-As-You-Earn, was approved by the States in December 2004 and will be introduced in 2006.

However, maintaining Jersey's current levels of public services and benefits can only be achieved by also increasing the tax paid by Jersey residents.

GENERATING £55 MILLION – TWO PRINCIPAL MEASURES

Two main taxation instruments will make good the shortfall caused by moving to 0/10%. Taken together they will raise the revenue required and they will ensure that the tax burden is spread fairly across the community, so that everyone pays a little, but those who are better off pay more.

1. Goods and Services Tax (GST)

- A broad-based GST of 3% from 2008. The rate would be the lowest in the world and guaranteed to be held for at least 3 years
- Only a small number of exclusions: exports and export-related services; transport to and from the Island; construction and letting of residential properties; exported and domestic financial services; life assurance, and postal services.
- A threshold of £300,000 for businesses. Those with a turnover of less than £300,000 would not be required to register. Only 1,500 businesses (approximately a quarter) will need to register
- Special treatment for financial services, to ensure that a contribution of between £5 and £10 million per annum would come from this sector.
- Around £10 million of the total raised by GST would be paid by non-residents of Jersey.
- The income support system will protect those on lower incomes.

2. Phasing out allowances for higher earners (20% means 20%)

- Tax allowances for the better-off gradually phased out, affecting only the top 30% of the population with higher disposable incomes.
- Effect on individual higher earners will depend on 2 factors: income and tax allowances. Only the highest earners will lose all entitlement to tax allowances and reliefs.
- Nobody will pay more than 20% of their income in tax.
- A phased approach over 5 years, so the tax bills for even these highest earners will in most cases increase by less than 1% of their income each year. The full effect will not be felt until 2011.

HOW THE COMMITTEE REACHED ITS DECISIONS

There are only 3 types of tax capable of raising£55 million p.a. –

- employee/employer payroll tax;
- income tax, either by increasing rates of tax and/or reducing allowances;
- consumption tax such as GST.

Each of these choices would result in Jersey residents paying more tax, but there are important differences in terms of their potential effects on the Island.

Payroll tax

A payroll tax is a tax on wages levied on the employer, the employee, or a combination of both. Taxing the employer increases the cost of doing business, and makes exports (including those of the financial services industry) less competitive. The resulting effect could be fewer jobs in Jersey in the future. Taxing employees reduces take-home pay for workers, just like increasing their income tax. Any payroll tax (on employer or employee) would not be paid by Islanders who do not work (many of whom may be rich).

Raising the rate of income tax

To raise the revenue required from income tax, the following sort of changes would be necessary –

1. Increase the standard rate from 20% to 25% (to generate £20 million); and
2. Reduce tax allowances by 25% (to generate £35 million).

This would mean that comparatively less well-off residents would have to start paying income tax for the first time.

Introducing a higher rate of tax for those on higher incomes would not generate sufficient revenue. For example, 30% income tax for incomes over £80,000 would raise £11 million, perhaps less if some of these individuals chose to leave the Island.

Raising the rate of income tax could deter higher earners and wealthy people from settling in Jersey and may encourage others to leave. Island residents would then have to pay even more tax to make up for the lost revenue.

Goods and Services Tax (GST)

A GST on its own might be unacceptable, as it would hit those on low incomes, who could not afford to pay the tax, and would not result in those on higher incomes paying a greater proportion of their incomes in tax. However, a package of GST combined with low income support and the phasing out of allowances for those on higher incomes has the following advantages –

- GST widens the Island's tax base so that everyone will contribute, including temporary residents and visitors. A wider tax base gives Jersey a more secure economic foundation and makes it less vulnerable to volatility in tax revenue. (Almost all successful countries understand this and have introduced some form of consumption tax.)
- Jersey residents do not bear the full cost of the tax since over £10 million of the£45 million which GST would raise will be paid for by non-residents.
- A broad-based GST is simple to administer and hard to avoid.

- Although there will be an initial rise in the Retail Price Index, consumption should fall, which in turn should help drive down inflation – making Jersey more competitive and a less expensive place to live.

- Everyone in Jersey would contribute a small share, but those on low incomes would be protected by enhancements to the income support scheme.

- Phasing out allowances for those with higher disposable incomes means Jersey keeps its headline rate of income tax of 20%, but the wealthier members of our community actually pay the full 20% rate of tax on their income, ensuring that the tax package remains progressive overall.

Additional research

The States (P.106/2004) required the Committee to examine and report on other types of tax –

Environmental taxes

Analysis of the effect of these taxes shows that people change their behaviour to avoid paying the tax. As a result, the revenue raised by environment taxes will decline over time. For this reason, the Committee believes environmental taxes would not be a significant nor reliable source of revenue.

However, the Committee supports the use of environmental taxes to help deliver the environmental objectives of the States Strategic Plan, so is recommending that more research is carried out to identify appropriate environmental taxes which would bring benefit to the Island.

Development gains taxes

By rezoning land for building, the States increases the value of land and the subsequent profit available to its owner. Profits derived from construction projects are already subject to Income Tax, but additional revenue could come from taxing development gains.

Analysis of the effect of this tax shows –

- Revenue would not be reliable or easy to forecast.

- A high development tax may discourage land-owners from selling land needed for the construction of housing.

- A development gains tax would not raise significant revenue.

But, to meet environmental policy objectives outlined in the States Strategic Plan the Committee recommends that more research is carried out into a development gains tax.

In making its choice of tax measures the Committee was guided by the following principles –

- Fairness

- Efficiency, simplicity, flexibility

- Maintaining the Island’s economic prosperity and employment

- Broadening the tax base, stability, minimising avoidance.

The Committee’s chosen package of proposals scores well on all these principles.

Most importantly, the package will ensure that Jersey can look forward to a sound economic future which means that the way of life which we all hold dear – with a pleasant environment, a generous level of services and a good quality of life – can be continued for generations of Jersey men and women to come.

REPORT

The Reform of Jersey's Taxation Structure

Introduction

In July 2004 the States agreed to change corporate tax rates in order to maintain a strong and competitive economy. These new rates will be a 0% standard rate of corporate profits taxation, with a 10% rate of corporate profits taxation for companies in the financial services sector. The States agreed that these new rates should be introduced no later than 1st January 2008 (P.106/2004).

The States also charged the Finance and Economics Committee to undertake further research into a Goods and Services Tax (GST), a payroll tax, environmental taxes, development levies and further tax enforcement measures and to bring forward recommendations for the approval of the Assembly.

This Report is the result of that further research. In the first instance it is important to have a proper appreciation of why the Committee is proposing an increase in tax for Island residents. To do this, the background of Jersey's current fiscal and economic situation needs to be understood.

Section 1 of this Report explains the need to reform the Island's tax structure and assesses the main tax raising measures that could be used to meet the revenue deficit arising from the move to a 0/10% corporate tax structure. **Section 2** details the research undertaken by the Committee and sets out its tax raising proposals. **Section 3** looks at further issues the Committee has considered and explains why it is not proposing alternative measures.

In approving P.106/2004 the States has already agreed the move to a 0/10% corporate tax structure which will result in a budget deficit of between £80-£100 million per annum. The States has agreed that by 2009 £20 million of the shortfall should be met by reducing public sector spending, through efficiency savings and cutting waste and that a further £20 million should be generated each year from economic growth. The States has also agreed the principle of raising £10 million by phasing out tax allowances for higher earners. Furthermore, the States agreed that £5 million per annum should be raised from the introduction of an Income Tax Instalment System (ITIS). **This leaves a requirement for £45 million per annum to be found from additional tax raising measures.**

SECTION 1 – THE NEED TO REFORM JERSEY'S TAXATION STRUCTURE

WHY CHANGE TO 0/10%?

International financial services are by far the most profitable of the Island's industries. They also tend to pay the highest wages.

As a result of the high level of profitability per worker – in the order of £90,000 per worker a year – and high average salaries, the total tax contribution from this industry is considerable. (In the rest of the economy the average profitability per worker is very much lower – roughly £6,000 a year). It is mainly because of the very high profits in this sector of the economy that the States are able to deliver a level of public services broadly similar to that of the U.K. yet with very much lower tax rates – in particular lower personal tax rates.

It would be difficult to imagine an industry, other than financial services, which was better suited to a small Island economy such as Jersey. It is one of the most profitable industries in the world and it uses relatively little land. Any alternative international industry that might be tempted to locate in Jersey would be very unlikely to be able to contribute so much to the economy and tax revenues. Therefore, losing the international financial services sector would reduce average wages and significantly reduce the average profitability per worker on the Island. To continue to deliver the same standard of public services the average person earning significantly less would have to pay a much higher proportion of their income in tax.

There are 2 key elements which influence the competitiveness of Jersey's financial services industry in the current international environment in which the industry must work. These elements have arisen independently of each other but do interact in terms of the solution to be proposed to the different challenges they pose. These 2 elements are–

- tax competition generally by rival jurisdictions competing for the establishment and/or retention of large financial services providers such as banks and fund managers; and
- changing European Union (E.U.) rules on harmful tax practices, applicable to corporate taxes only, which affect the corporate vehicles used by customers of financial services providers.

General tax competition

To meet recent and growing international competition, the States agreed in July 2004 that **the rate of corporate profits tax applied to the providers of international financial services needs to be at, or close to, a maximum of 10%**. This would bring it in line with what Jersey's competitors are doing (Singapore, Guernsey and the Isle of Man are moving to a rate of 10% and Dublin already has a rate of 12.5%). Above this level Jersey would rapidly become uncompetitive as a place to locate providers of international financial services. It should be stressed that this situation would have arisen irrespective of the E.U. tax rules which also lie at the heart of the fiscal strategy. In that respect, Jersey would in any event have been facing significant pressure on its revenues derived from the corporate taxes of large Jersey-based financial institutions because of the need to stay aligned with rates being offered by major competitors. The competition element is calculated to account for up to £50 million of the potential £80-£100 million shortfall identified as the consequence of a move to the new fiscal structure.

E.U. rules on harmful tax practices

In addition to a competitive rate of corporate profits tax, the providers of international financial services also require the legal mechanisms to be able to deliver the type of financial services their customers require. One very important service is the provision of a corporate legal entity, resident in Jersey, that does not have its profits taxed. Such legal vehicles are commonplace internationally and are currently available in Jersey through the Exempt Company structure. However, these exempt company structures are not available to Jersey residents. International pressure, particularly from the E.U. and the United Kingdom (U.K.) resulting from the initiative on harmful business taxation (known as the Code of Conduct on Business Taxation), means that Jersey can no longer maintain this discrimination. Failure to address this issue could well result in action by the U.K. or the E.U. which

would very seriously undermine the ability of international financial institutions to continue to operate from Jersey. The consequences for the Jersey economy would be serious.

In order to ensure that the providers of financial services can provide the products they need for their international customers, the facilities of the existing Exempt Company structure will need to be made available to residents as well as non-residents of the Island. This will be achieved by introducing a general rate of corporate profits tax in Jersey of 0%. This removes the discrimination between companies with resident and non-resident shareholders, and hence removes the threat of unilateral action by the U.K. and E.U.

However, in July 2004 the States agreed that in order to safeguard as much as possible of the tax revenue generated from corporate profits tax, those entities regulated by the Jersey Financial Services Commission would be excluded from the 0% rate and a higher rate of 10% applied to them.

It is a feature of the way the E.U. interprets its approach on harmful tax practices that assessing one sector at a higher rate of corporate tax (10%) than is the general rate in the economy (0%) is acceptable. It is nevertheless important to consider 2 further points in this respect, one of which legitimises the higher rate, and the other which limits the wider application of a 10% rate in the Jersey economy –

- It is considered acceptable to have a higher rate in the economy than is the norm on the basis that the sector chosen is effectively being 'discriminated against' compared to the general rate of corporation tax applied

- In order to justify that the general rate is indeed 0%, it may be unwise to seek to add any additional sectors to that defined for financial services and subject to the higher 10% rate. This would call into question the viability of the general 0% structure which, as can be seen, is vital for the separate purpose of maintaining the benefits of Exempt Companies by another method. However, it has been clear from negotiations with both HM Treasury and, through them, with the E.U. Code of Conduct Group on Business Taxation, that the possibility of adding local utility suppliers to the 10% higher rate band should not jeopardise the position pertaining to the general rate (see below).

The States have therefore concluded that in order to keep the financial services sector competitive, the zero profits tax legal entity must, in general, be made available to all companies, irrespective of the place of residency of the beneficial owners. This involves setting the general rate of corporate tax at 0%.

These 2 measures will, inevitably, lead to a substantial loss of tax revenue from the current economy. However the alternative of leaving the current tax structure unchanged would result in a considerably worse outcome. The financial services sector of the economy would become uncompetitive in its international markets, and companies would move to more competitive jurisdictions. This process of moving both jobs and business to more competitive jurisdictions is not just a theoretical threat, but can already be seen to be happening worldwide as mobile business, such as financial services, seeks to maximise its advantages in terms of differential costs, of which labour costs and total tax burden are two key determinants in location decisions.

Some attention has been given to the durability of a 0/10% corporation tax structure in a fast-changing world. The E.U. agreement specific to the Committee's proposals is contained in the record of the meeting of the combined E.U. Finance Ministers, known as ECOFIN, on 3rd June 2003. These ECOFIN Council Conclusions recognise the acceptability and timescale for implementation of the 0/10% proposals to the European Union, which throughout the negotiation process had also gained the full support of the United Kingdom government.

It must be acknowledged that future developments within the E.U. or in other international bodies, or even matters involving individual countries, could evolve over time to bring the 0/10% structure back for further debate. However, Jersey has received specific assurances from the U.K. Government that the issue at the heart of these reforms is one of perceived harmful tax practices, i.e. discrimination in tax treatment between different types of company and differing residence of shareholder, and that in the move to a 0/10% corporate tax structure Jersey has addressed these issues. In addition, Jersey has been assured by the U.K., the E.U. and the OECD in different discussions that the various international initiatives on taxation with which the Island is involved do not

have the harmonisation of tax rates as their objective. Secondly, the U.K. Government, together with other like-minded nations such as the United States, Australia, Canada, Ireland and some others, are clearly working to an agenda which recognises and espouses tax competition internationally as the acceptable norm. Given that the 0/10% structure is inherently about tax competition then alignment with those countries on the acceptability of the tax competition approach should provide some comfort as to the potential durability of the proposed 0/10% solution.

Some attention has been given to the prospects for defying the E.U. rules – since Jersey is not within the E.U.'s fiscal territory – and therefore avoiding the need for the general 0% corporate tax rate. The Committee strongly believes that this would be contrary to the interests of the Island and regard the following as the principal reasons for this stance –

- The E.U. element of the proposed changes only accounts for some £30 million of the identified £80-£100 million shortfall identified as the monetary consequence of the proposed change in the Island's fiscal system. The remaining part is derived from downward pressure on corporate taxes generally from increasing international competition. A policy of refusal to consider aligning ourselves with E.U. rules which, even on the best possible outcome, might result in addressing less than 50% of the Island's actual problem would not seem to represent an acceptable balance between risk and reward.

- Jersey is positioned on the periphery of the European Union and conducts much trade with it and derives significant opportunities from such positioning to develop financial services and other business with E.U. nationals. A policy which contemplates not just isolationism in this respect, but also one which would have the effect of undermining the E.U. Code of Conduct exercise, with attendant damage to the U.K. relationship with its E.U. partners, would seem again to represent a very high-risk approach.

- The United Kingdom is determined to ensure compliance by its Dependent Territories with the E.U. Code of Conduct with similar pressures faced both by Guernsey and Isle of Man in this respect. Although there are constitutional arguments to invoke to resist this, Jersey has already seen the U.K. prepared to contemplate a highly pressurised approach to forcing this compliance with threats of unilateral action by them against the Island to achieve such an outcome should the Island ignore the Code of Conduct requests. One such measure would be the revocation of the exemptions permitted to Island-based businesses within the U.K.'s Controlled Foreign Companies legislation. Such revocation would have a rapid and detrimental tax impact on all U.K.-owned businesses in the Island and probably force them to re-evaluate their options for representation on the Island over time. Where this would create most immediate concern would be in the banking sector with a handful of large U.K.-owned banks accounting for a very high share of the Island's direct tax revenues and nearly 50% of the Island's financial services workforce. There are other areas where the U.K. could take unilateral economic actions with severe consequences for Jersey, such as in withdrawing existing double tax exemptions, and the possible implementation of withholding taxes on inter-bank deposits by Jersey-based institutions into the U.K. All such measures are potentially serious for any large U.K.-owned business, particularly in financial services, in the Island. Therefore, they do not in the eyes of the Committee represent an acceptable balance of risk if these policies were to invite their implementation or even threat, recognising that business cannot function well in the face of uncertainty and that threat alone may be sufficient to create such uncertainty and attendant adverse economic decision making.

The taxation of Jersey utilities at 10%

As stated above, within the EU Code of Conduct on Business Taxation process there is an option open to the Island to include utility providers, both public and private sector, within the 10% higher rate band which has primarily been designated for financial services companies. This results from a particular feature within the policy approach of the EU Code Group in its determination of what constitutes 'harmful business tax practices' in that local utility providers are not deemed to be influenced by international competitiveness on tax rates in terms of their location decisions. They are generally not mobile businesses and their market is essentially confined to the local population where the utility is located. Thus, the EU approach is that it is indifferent as to whether such utilities are taxed within either the general rate arrangements for corporate tax or at the higher 'special' rate.

Jersey can therefore take either of these options.

Although the amount of corporate profits tax which will arise from taxing Jersey utilities at the 10% rate is currently rather modest at around a maximum in aggregate of £1 million per annum, and arguably represents nc more than a transfer of receipts where such utilities are in any event owned by the States, it is considered useful to take the option of taxing utilities at the higher rate for future policy flexibility. It is possible that in future, particularly where any privatised utility may be concerned, that the profit levels and taxes involved may be significantly higher than they are today and the option of being able to tax these at the special rate would therefore be of some value. This is all the more so given that the option incurs no current political nor economic cost for the Island.

The precise definition of utilities to be effected has yet to be finalised but for indicative purposes is expected to include Jersey Post, Jersey Gas, Jersey Electricity, Jersey Telecom, and Jersey Water.

Consequences of delaying decisions

A final, but vital, component of the need for change is the requirement to act quickly and decisively. Whilst the Island was successful in winning a longer period to enact tax reform than had originally been likely, there is no doubt that competition for financial services business worldwide is accelerating, based in no small part on the attraction of low rates for providers in key competitor jurisdictions and the absolute minimum requirement of being able to continue to provide tax neutral vehicles to global investors by finding a solution to replace the Exempt Company structures on which so much of the business flow of Jersey's financial services industry depends.

Business in the Island will not welcome any drawn-out period of uncertainty regarding the Island's recognition of these challenges and the willingness to address them quickly. Customer business can be lost unless certainty of applicable tax treatment can be given on any given structure for the whole of its intended life span – sometimes up to 20 years. Separately, large multi-national financial services providers, who are represented in Jersey and in many of the Island's competitor jurisdictions at the same time, have many options for switching business, capital and jobs at a rapid rate away from the Jersey to such competitor jurisdictions with relative ease. It should also be borne in mind that once such economic activity is lost by Jersey to competitor places then it is unlikely to return in the future without a very compelling reason to do so.

Mitigating the loss of corporate tax revenues

The estimated loss of some £80 – £100 million in tax revenues arising from the move to 0/10% is likely to be a worst case scenario which can be broadly categorised as follows –

International Business Companies – up to 10%. Many of the international business companies who pay substantial tax revenues are already close to an effective rate of tax of 10%, so the majority of that business should stay once the proposed 10% rate is introduced, but a few may well go.

Exempt Companies – up to 10%. This relates to the loss of the exempt company fee of some £10 million as they will all be categorised as zero rate. However, it should be possible, subject to international competitive pressures, to recoup this loss through, for example, increasing the annual filing fee.

Non-finance business. In broad terms, some 40% of the potential loss relates to non-finance business. Some 20% to 25% relates to non-finance business trading locally whose shareholder base is outside the Island.[1] There is a similar amount of non-finance business trading locally which is also owned locally. Although these businesses will no longer pay corporate tax on their profits, the majority of any loss of tax revenues will be made up by increasing the personal tax liability of Jersey resident shareholders (see the comments on 'look-through' arrangements in Section 2).

Finance industry companies. The majority of the loss, perhaps up to 60%, is estimated to come from income tax levied on companies involved in the finance industry currently paying at an effective rate of tax close to the

standard rate of 20% which will fall to be taxed at 10% under the proposals.

The above represents an analysis of a constantly changing picture, and although carried out many months ago on the basis of the tax information available at that time, the Committee is confident that it does remain a realistic estimate of the size and nature of the potential problem.

The potential impact of not adopting 0/10%: Jersey without an international financial services industry

In considering its options, the Committee has looked at how the Island's economy might look in the absence of the international financial services industry at its present level. This might be the outcome if the States failed to introduce measures to reform the corporate structure in response to the changes which are taking place in competitor jurisdictions. It looked particularly closely at that part of the financial services industry that provides services to the international markets including those serving non-resident clients. This industry is highly mobile and it would probably be that the most profitable parts that would leave first if the Island's corporate tax structure became uncompetitive. There could be a substantial change in the structure of the financial services industry in the Island within a relatively short period.

There would be a major shock to the Island's economy during the first few years after companies had gone, though they would be unlikely to leave the Island at the same time. The loss of some companies could have a bigger effect on the overall economy than others. The following effects would be likely to be felt in the Island during the first few years after the shock of the emigration of these key companies –

- employment in financial services would fall from today's level of 12,000 jobs to 1200-1500 jobs;
- a large fall in demand for goods and services (for example in the shops) since employees in the financial services industry have the highest disposable incomes and spending power;
- employment outside the financial services sector would also fall. Significant unemployment outside the financial services sector would be likely;
- property prices would fall and the age structure would alter as younger people would be likely to dominate those leaving the Island in search of employment;
- total population would fall, and the fall could be considerable – possibly by 20-22,000 (with the working population falling by 14-16,000);
- under the current tax structure, States' revenue could decline by £250-£300 million per annum compared to the present total of £450 million;
- if current levels of services were maintained, States' spending could fall by much less (perhaps only by £100 million or less) because it would tend to be older residents who would remain in the Island. The immediate liability for States' pensions would hardly fall at all;
- the potential deficit in the States Budget could amount to £200 million in each and every year;
- the potential tax base on which to make up this shortfall would be much smaller than it is now;
- to meet any shortfall by tax increases or service level reductions would require much higher tax rates, or deeper cuts, than meeting a similar shortfall from the current tax base.

The Island would probably begin to recover after this initial shock, but the economy would look very different from the way it does now. Exactly how the economy would look would depend on what, if anything, replaced financial services. In the absence of a replacement the following chain of events would be likely to unfold after the first few years following the shock –

- wages in the Island would fall as firms would be able to offer lower wages with the rise in unemployment and in response to the decline in overall profitability;

- to maintain anything like the current population, an alternative export industry would be required. This industry would need to be one where any additional costs arising from Jersey's physical location were at least off-set by some cost or quality advantage of operating from the Island;

- assuming such an industry could be found, output in the Island would start to recover, though almost certainly with much lower levels of profits and wages compared to now;

- population would stabilise, and might even start to grow again, though the new people coming into the Island would have a different set of skills;

- house prices would stabilise, but very likely at levels considerably lower than now. It is likely that many younger people would find that their mortgage debts were larger than the (now lower) value of their properties.

If the population had fallen significantly (which is likely), it might take a considerable time for property prices to recover. The problem of "negative equity" in property could last for a considerable time. The reduction in both property prices and wages would make tourism and, possibly, agriculture more competitive. In the absence of a significant new industry they would probably become the dominant industries again in Jersey and the main sources of employment for Jersey people.

Unless any new industry was capable of generating similar tax revenues for the States and wages for residents it would not be possible to maintain the current position of low tax rates with similar public spending per head as the U.K. Either tax rates would need to increase very significantly (i.e. up to the equivalent of U.K. rates) or public services would need to be cut drastically. If the former was adopted, high-income residents, particularly those with significant investment income, would be discouraged from remaining in Jersey because of the higher tax rates. To the extent that such residents left the Island this would lead to further downward pressure on tax revenues.

Exactly where the economy would end up is impossible to predict with any accuracy as there are too many unknowns. However, the typical pattern for small Island economies is that they tend to have lower average standards of living than their adjacent 'mainland'. Among other things, this reflects the additional transport costs of getting to and from the Island. The exceptions are where the Island has some clear and significant underlying economic advantage over the mainland. In the case of Jersey there is currently little evidence that the advantages of the Island for agriculture or tourism are that significant. The economic value of the Island's characteristics for these two industries may, therefore, be limited. As a result, levels of Gross National Income per head might fall from the 2003 level of £34,000 to around or below the average U.K. level – £18,000, once the economic adjustments had worked through the Island.

The delivery of the current level of public services combined with the current tax structure could result in a deficit in the States Budget of around £200 million every year. This is not sustainable, even in the short term, so some very large adjustments in either taxation or spending would be needed.

Conclusion

A flight of international financial services from Jersey would lead to an economy that could not sustain the current level of public services on the present tax structure.

The loss of tax revenue caused from international financial services leaving the Island would be far higher than the shortfall produced by altering the tax structure to a 0/10% corporate tax regime.

In addition, the total economic activity on the Island would be likely to be lower, but with a less than proportionate decrease in the demand for public expenditure (including States' pensions). Tax rates for future residents would therefore be likely to be significantly *higher* in the absence of the international financial services business.

OPTIONS FOR FILLING THE £80-£100 MILLION DEFICIT

The move to 0/10%, though essential to maintain the Island's prosperity, will create an £80-£100 million deficit in the States finances. There are essentially only 3 available options to meet this shortfall. These are–

- **reducing States spending** by improving the efficiency of the public sector and/or cutting public services;
- generating additional tax revenue through **economic growth;**
- additional **taxation.**

A clear message from the fiscal strategy consultation and also from the Imagine Jersey process is that whilst the public want the States to improve efficiency of the public sector there is little desire to save money through significant reductions in the range and quality of services provided. In particular, there appears to be little appetite to cut provision of core services such as education, health, social benefits and law and order which account for well over three-quarters of States spending.

Furthermore, as most of the services provided by the States have a positive redistributive impact – that is, tax revenue taken from the better-off is used to provide services for the not-so well-off – the effect of cutting services would, in general, harm the less well-off more than it would the better-off.

The Finance and Economics Committee has proposed, and it has been agreed by the States, that the annual increase in total States' net expenditure should be limited to one per cent less than the underlying increase in the Retail Prices Index (RPI(X)) for each of the years 2005 to 2009. This should ultimately cut States spending by up to £20 million each year. The Committee believes that these cutbacks in States spending are achievable and realistic targets. However, the Committee does not believe that further significant savings are possible without drastic cuts in the provision of public services such as education, health and social benefits.

The Committee has also proposed, and again it has been agreed by the States, that an economic growth target of 2% per annum in real terms should be set for the period 2005 to 2009. This measure should generate up to £20 million in additional tax revenue per annum. The recently published Economic Growth Plan provided by the Economic Development Committee lays out in detail the strategic approach for meeting these targets.

Economic growth with sustainable inflation is the first aim of the States Strategic Plan. Sustainable is the critical word, as it would be possible to rapidly deliver 2% economic growth which could damage the economic base in the Island, harm the economy's long term potential and have negative impacts on the natural environment. By ensuring that economic growth is well-managed and sustainable, the Economic Growth Plan means that these risks are kept to an absolute minimum.

Both the Finance and Economics and Economic Development Committees believe that a target of 2% economic growth is realistic and achievable and will generate up to £20 million per annum in additional taxation revenue. However, to generate further tax revenue from a more ambitious economic growth target would run the risk of fuelling unsustainable inflation and have consequences for inward migration. The 2 Committees believe, therefore, that the 2% growth target which should generate £20 million in tax revenue is an appropriate and measured objective.

Taking into account these 2 measures– cutting States spending and promoting economic growth – means that **additional taxation of up to £60 million is required** in order to meet the rest of the £80-£100 million deficit, of which £5 million will be delivered through ITIS, leaving a balance of £55 million to fund by other means.

PROBLEMS WITH JERSEY'S CURRENT TAX STRUCTURE

Successive Finance and Economics Committees have undertaken extensive analysis of Jersey's current tax structure and arrived at the following conclusions –

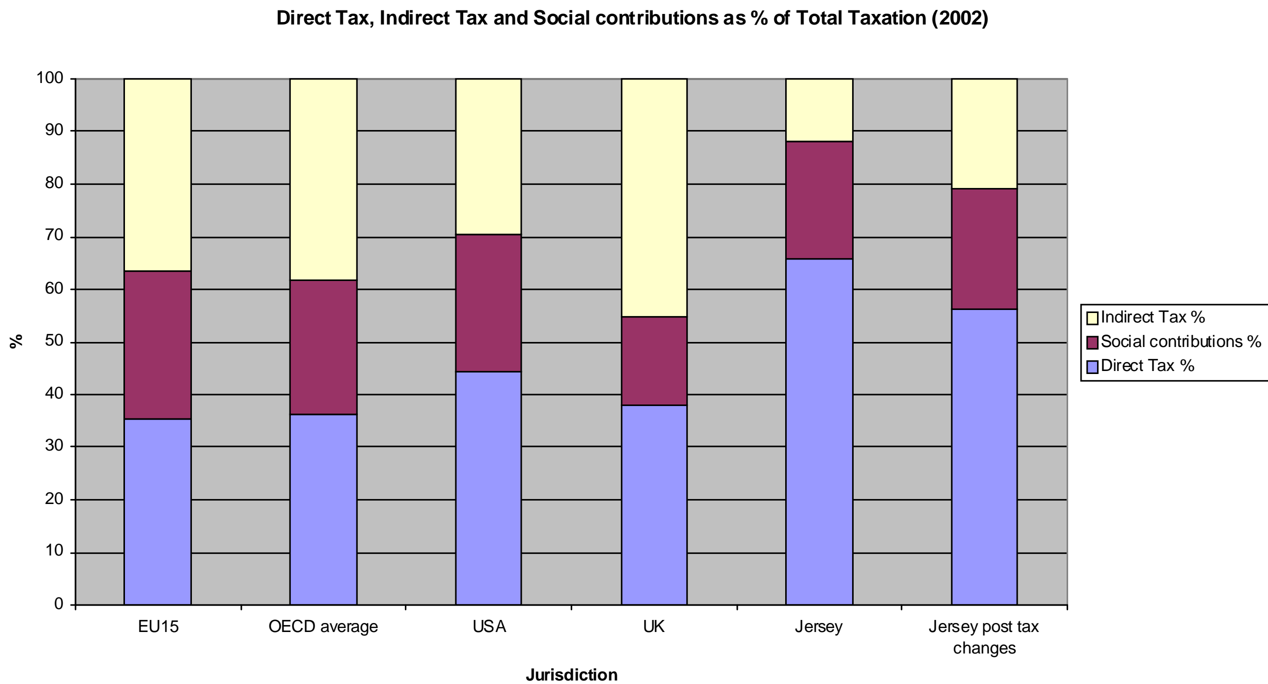
- the Island is too dependent on direct taxes;
- the Island is over-reliant on corporate taxes;
- taxes are too low to finance the level of public services, benefits and infrastructure the Island expects;
- the Island's tax base is too narrow and a wider proportion of the population need to contribute towards the services they enjoy.

Excessive dependence on direct taxes

As long ago as 1998, the Fiscal Review Working Group reported (R.C.41/98) that Jersey was too reliant on direct taxation and recommended that the Island should diversify its tax base. The Finance and Economics Committee of the day, and the current Committee, agrees with this conclusion. As Figure 1 indicates, Jersey still remains highly dependent on direct rather than indirect taxation. Some 12% of Jersey's tax revenue comes from indirect taxation, whereas in the U.K. indirect taxation accounts for some 45% of total taxation. The E.U. average is around 36%.

The Committee believes that this over-reliance on direct taxation leaves Jersey in a vulnerable and indeed dangerous position, especially in today's global economic environment. Few countries in the developed world rely so heavily upon direct taxation. This is not a desirable state of affairs and should be addressed without further delay.

Figure 1



Sources:

OECD, Revenue Statistics 1965-2003, 2004, tables 11, 13, 17, 19, 21, 23, 29, 31, States of Jersey, Report and Accounts, 2003, Annual report, Employment and Social Security Committee, 2003, States of Jersey, Review of the Relationship Between the Parishes and the Executive, 2003, page 9, Oxera calculations.

Notes: Jersey post tax changes assumes that there is a loss of £80 million from corporate income tax (direct tax) which is replaced by £45 million GST (indirect tax) and £15 million personal income tax (£5 million from ITIS and £10 million from 20 means 20– direct tax). Jersey taxes includes taxes paid to the Parishes.

Diversification of the Island's tax base would help to reduce volatility in future tax revenue, providing a more stable source of funds. It would also diminish incentives for tax avoidance and evasion. Following full implementation of the Committee's fiscal proposals future direct taxation would still account for approximately 56% of total taxation in Jersey, far higher than the E.U. average of 36%.

Over-reliance on corporate taxes

Not only is Jersey over-reliant on direct taxation, it also relies more on taxes from businesses rather than personal taxation compared to most other countries in the world. Personal taxation in Jersey accounts for some 49% of total taxation, with 51% coming from businesses (the corporate sector). As Figure 2 shows, most other countries generate the vast majority of their taxes from individuals rather than from business.

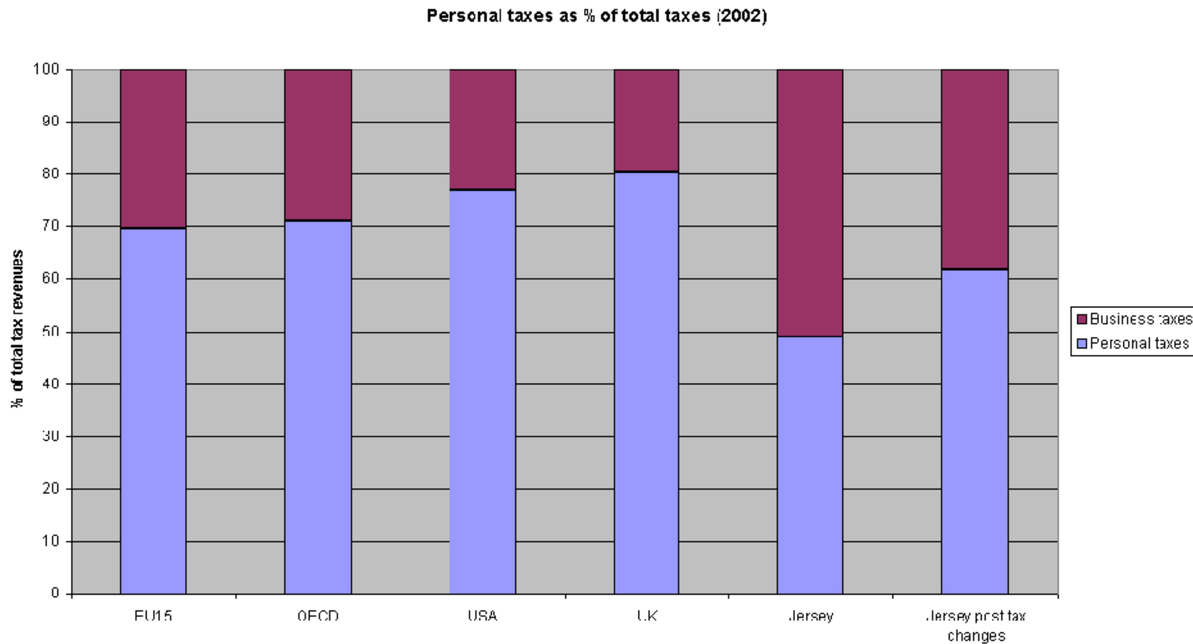


Figure 2
Sources:
OECD, Revenue Statistics 1965-2003, 2004, tables 11, 13, 15, 17, 19, 21, 23, 29, 31, States of Jersey, Report and Accounts, 2003, Annual report, Employment and Social Security Committee, 2003, States of Jersey, Review of the Relationship Between the Parishes and the Executive, 2003, page 9, Oxera calculations.

Notes: The definition of personal taxes is: personal income tax, employee social contributions, property tax, specific consumptions tax (e.g. Impôts) and general consumption tax (e.g. GST); business taxes are defined as corporate profits tax, employer social contributions, payroll taxes, and other taxes. Jersey post tax changes assumes that there is a loss of £80 million from corporate income tax (business tax), which is replaced by £45 million GST (personal tax) and £15 million personal income tax (£5 million from ITIS and £10 million from 20 means 20 – personal tax), Jersey taxes includes taxes paid to the Parishes.

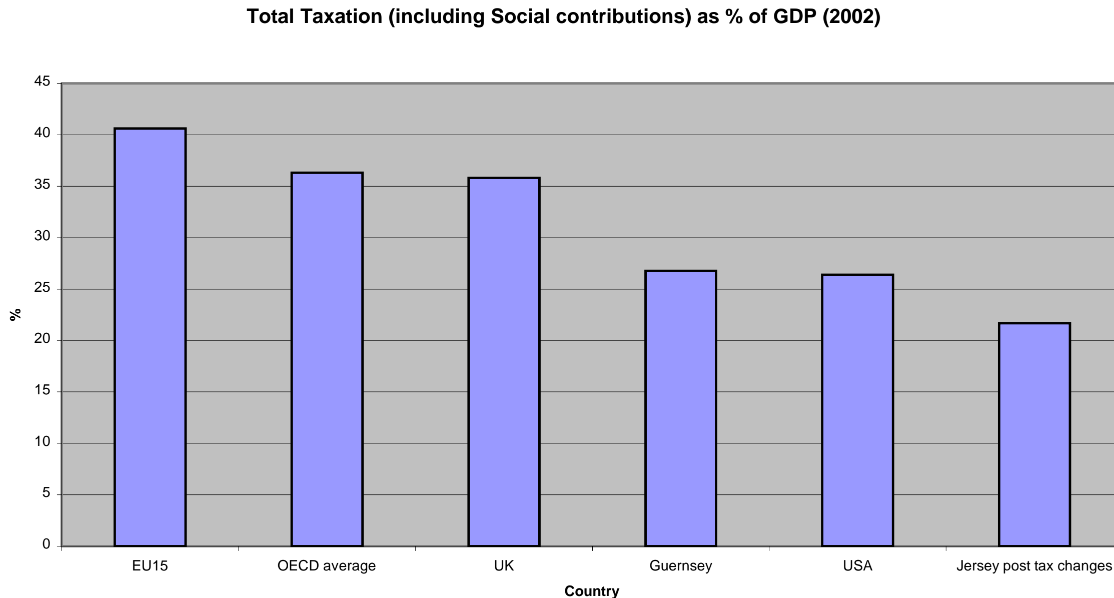
In the U.K. 80% of total taxation comes from taxes on people, with 20% being contributed by businesses. The average figure in the E.U. is 70% from personal taxation and 30% from businesses.

It is important to note that even after the full implementation of the Committee's fiscal proposals, Jersey businesses will still contribute nearly 40% of total taxation. This contribution to the total tax take from the corporate sector will still be one of the highest in the world.

Jersey's low taxes

By international standards taxes in Jersey are very low. The Island's international reputation as a low tax area is borne out by the statistics. As Figure 3 demonstrates below, total taxation (including Social Contributions) in Jersey (in 2002) as a percentage of Gross Domestic Product (GDP) is considerably below that of most other countries throughout the world. It is far lower than that of the United Kingdom (U.K.), European Union (E.U.) average, Guernsey and OECD average.

Figure 3



Sources:
OECD, Revenue Statistics 1965-2003, 2004, Table A:
http://www.gov.je/statistics/content/xls/GVA_GNI_data.xls,
States of Jersey, Financial Report and Accounts 2003, page ii; Annual Report, Employment and Social Security Committee, 2003, pages 5 and 10; States of Jersey, Review of the Relationship Between the Parishes and the Executive, 2003, page 9; 2004 Guernsey facts and figures, Table 3.2, Table 9.2; Oxera calculations.

Notes: the total Social Contributions in Guernsey has been estimated from their Social Contribution rates and structure. Jersey post tax changes has been calculated by reducing GDP by the £80 million tax loss, and changing tax revenues by a reduction of £80 million and an addition of £60 million (i.e. total tax revenues reduce by £20 million). Jersey taxes includes taxes paid to the Parishes.

Gross Domestic Product (GDP) is an internationally defined measure of the size of economy. It is derived from Gross Value Added (GVA), which measures the economic activity of each sector, by deducting the income that is generated by interest rate differentials (i.e. lending and borrowing money at different interest rates). Given Jersey's successful banking sector this adjustment is large; around £560 million in 2003 and is far more significant than in other countries included in Figure 3. However, income earned by the banking sector in this way does feed into profits and thus taxable income. As such, a better measure of Jersey's total taxation relative to its economic wealth is to use taxation as a percentage of GVA. On this measure, taxation accounts for around 14% of economic activity. Further information about measurement of the size of Jersey economy is available via the report on Jersey's GVA and GNI 1998 – 2003 on States of Jersey Statistics Unit website www.gov.je/statistics

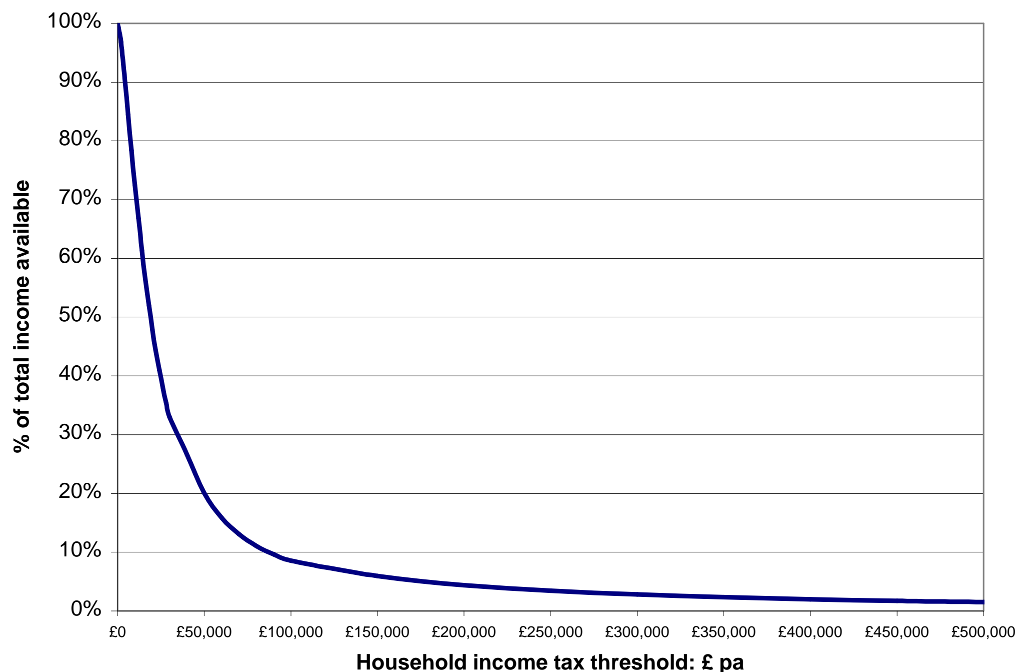
Even after taking into account the Committee's tax raising proposals outlined in this Report, Jersey will still have a rate of total taxation as a proportion of GDP which is much lower than in most other developed countries.

Widening the tax base

Jersey has an extraordinarily narrow tax base. The combination of an absence of GST and very high income tax allowances and exemptions mean that households can be on quite high incomes before they pay any tax other than impôts duties. For example, a married couple, both working with 2 children (one at university) and paying mortgage interest of £7,500 per annum will not pay tax until their income exceeds £37,180.

It is important to take account of the distribution of income when considering increased taxation measures. Figure 4 below shows household income distribution for Jersey (in 2001) in the form of the proportion of household income that is available to tax for any given level of tax threshold and indicates that only around 10% of household income is available to tax above a (gross) household income threshold of £80,000. **Tax measures that are exclusively aimed at households with high incomes do not yield particularly large amounts of tax revenue.** The Committee has taken this income distribution into account in formulating its preferred option and has come to the conclusion that it is necessary to broaden Jersey's tax base.

Figure 4: % of household income available to tax for any given (gross) income tax threshold



Source: Jersey tax records (2001), OXERA calculations.

At present over 13,000 potential taxpayers (some 25%) in Jersey do not pay any income tax, which contrasts sharply with other European jurisdictions – where the vast majority of households pay some income tax, and all of them pay Value Added Tax (VAT). Moreover, over 50% of potential taxpayers pay 6% or less of their income in tax. This situation is not sustainable as there are simply not enough households in Jersey on high incomes to shoulder the burden of funding the services enjoyed by the whole population.

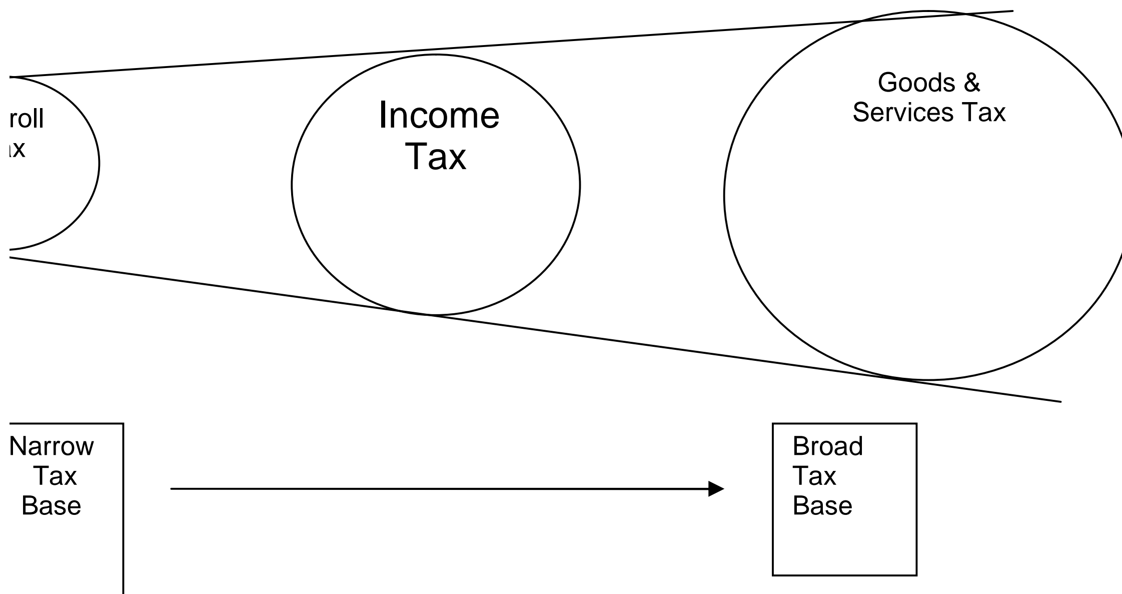
As Figure 5 demonstrates, a payroll tax has the narrowest tax base as it only captures earned income. Wealthy investors, and the retired, would not contribute to this tax base because unearned income is not taxed.

Income tax has a broader tax base as it captures all residents who accrue an income. However, it does not capture taxing the spending of non-residents nor visitors. Furthermore, due to the very generous income tax allowances and exemptions in Jersey a significant proportion of taxpayers do not contribute to this tax base.

Out of the 3 main tax-raising options, a GST has the characteristic of being the broadest tax base, ensuring that most of the population makes at least some contribution to the cost of the public services they enjoy. This leads to a more diversified, but inclusive, tax system. Consumption taxes are paid by everyone, whatever their source of income, including visitors to the Island.

The advantages of a diversified tax system are that the tax revenue tends to be more stable and predictable, and incentives for tax avoidance and evasion of tax are diminished.

5 Relative Positions of Main Tax Options in the Tax Base



Conclusions

The Committee has concluded that Jersey needs to –

- **become less reliant on direct taxation;**
- **become less dependent on raising taxation from businesses;**
- **ensure that the level of taxation is sufficient to fund the level of public services, social benefits and the infrastructure Islanders expect;**
- **widen the proportion of people who pay tax to ensure that, where able to do so, all those who benefit from these public services should make some contribution to their cost.**

TAX OPTIONS FOR RAISING £55 MILLION

There are realistically only 3 tax bases, or a combination of them, which are capable of raising the £55 millior which is required. These are taxes on wages (a payroll tax), income (income tax) and consumption (a goods and services tax). There are, however, an infinite number of permutations for raising £55 million from different forms of these 3 tax bases and various combinations of them.

However, for the purpose of arriving at a decision as to which taxes would be most appropriate to suit Jersey's needs, the Committee has assessed 4 main likely options.

The main tax raising measures the Committee has considered are –

- **Option 1:** A broad-based Goods and Services Tax at a rate of 3%, together with the phasing out of income tax allowances and exemptions for those on higher disposable incomes.

- **Option 2:** A payroll tax of 2.5-3% on employers and 2.5-3% on employees.[2]

- **Option 3:** Increasing the income tax standard rate from 20% to 25%, and reducing income tax personal allowances and exemptions by 25%.[3]

- **Option 4:** Introducing a package of proposals such as increasing the standard rate of income tax to 22%, introducing a higher rate of income tax of 25% on taxable income over £80,000, introducing a one per cent payroll tax on employers, and abolishing the cap on social security contributions.

Each of these tax measures would, in the first instance, raise about £55 million and will be considered further ir this Report.

PRINCIPLES APPLIED IN ASSESSING THE MAIN TAX OPTIONS

In order to identify which of the main tax options is best for Jersey the Committee has assessed them against the following criteria –

Fairness

What is 'fair' in relation to the payment of taxes is inherently a subjective concept. The Committee has, however, used the twin criteria of ***progressivity*** (i.e. the more you earn the more you pay) and ***inclusion*** (i.e. all except those on the lowest of incomes should make some contribution to the services that they enjoy). Clearly a balance has to be struck between progressivity and inclusion. Most countries achieve this through a mix of direct and indirect taxes.

– ***Progressivity:*** as far as possible taxes should be seen to be fair in terms of their relative impact on households, thus all should contribute as far as possible in accordance with their relative 'ability to pay'. Generally, those on higher incomes can afford to pay a greater proportion of their incomes than those on lower incomes. Progressivity can be supported by providing benefits to those on low incomes as benefits are essentially 'negative' taxes.

– ***Inclusion:*** a quarter of those liable to pay tax in Jersey do not pay any income tax at present due to the very high personal tax allowances and exemptions. The Committee believes that as many people as are able should contribute to the cost of running the Island. As far as possible the tax system should be inclusive – to avoid issues of moral hazard. Those people who benefit from the Island's public services and infrastructure, such as education, health services and social benefits, and who also have the right to vote in States elections, and thus have a say in the way those public services are provided, should contribute to some extent to the funding (i.e. taxation) of those public services where they are able. Those with no financial interest in paying for States services have little motivation to either contain States expenditure or to ensure that it provides value for money.

Efficiency, simplicity, flexibility: the cost of collecting taxes is a deadweight loss on the economy, and should be minimised as far as possible. Taxes should also aim to minimise the (unintended) distortion of economic choices. People should be able to easily understand the tax system, and it should be flexible so that it can easily be changed to suit the Island's needs.

Economy and employment: taxes should not adversely affect the Island's international competitiveness. Taxes should not have a potentially damaging effect on the level of local employment and should also be consistent with the aim of achieving real economic growth of at least 2% per annum.

Diversifying the tax base, stability, avoidance: Jersey is over-reliant on direct taxation, which leaves it unnecessarily vulnerable to changes in the global economy. The tax system should be more broad-based and diversified, so that the Island relies less on income tax and corporate tax as its main sources of income. A mix of mechanisms to raise taxation revenue would position Jersey better for the future. This will also create a more stable tax base, which means that the total tax revenues are less vulnerable to volatility in income streams. The tax system should also ensure that tax avoidance is kept to an absolute minimum.

In practice, not all of these criteria can be met simultaneously, indeed some are mutually exclusive, and compromises are necessary. However, in coming to its conclusions the Committee has sought to take into account all of these criteria in choosing between the different options that are possible.

COMPARISON OF THE MAIN TAX-RAISING OPTIONS AGAINST THE CRITERIA

In arriving at its conclusions the Committee assessed the main tax-raising options (detailed above) available to raise up to £55 million against the criteria outlined above.

The Committee's conclusions are given below –

Fairness

Progressivity

Option 1: A broad-based GST will tend to be marginally regressive. However, the 20% means 20% proposal increases the tax burden only for the better-off and the income support system will protect those on the lowest incomes from the effect of GST. The overall impact is that the tax changes are roughly proportional to income over the lower income ranges, with generally a slightly higher proportion of income taken in additional tax at higher incomes.

Option 2: The payroll tax option is proportional to earned income, as it taxes all earned income at the same rate. However, it does not include unearned income, so will not tax some households with high incomes.

Option 3: Using income tax measures is broadly progressive with those on higher incomes paying more in tax. However, it is not 'smoothly progressive' because income taxpayers would see their tax bills rise by an amount that will not vary smoothly with income, but would vary by household composition.[4] Some households on lower incomes would face a higher increase in taxes than exactly the same household with a higher income.

Option 4: The combination of measures produces the most progressive outcome as most of the measures will only apply to higher earning households. At high incomes employees would see a marginal rate of tax and social contributions of 31%, and employers would also see their employment costs rise for high earners.

Inclusion

Option 1: A GST would draw more people in to the tax bracket ensuring that those who benefit from the Island's public services and infrastructure, such as education, health services and social benefits, contribute to some extent to their funding.

Option 2: The payroll tax would draw more people into the tax base, as it would include those who currently do not earn sufficient income to pay income tax. However, payroll taxes do not include those with unearned (e.g. those with dividend income, pensioners) income in the tax base, no matter how high their income, so from this perspective is unfair.

Option 3: Reducing personal income tax allowances and exemptions would draw more people into the tax net, making it more inclusive. On the other hand, relying on higher rates of income tax would concentrate the tax burden even more on this form of direct taxation.

Option 4: The one per cent employers' payroll tax element could bring additional, low paid employees into the tax net on a marginal basis, to the extent it will impact on employees in the form of lower wages. The main elements of the package apply only to existing tax payers (the higher tax rates) and employees already in the tax net (the abolition of the ceiling on social contributions). Overall this is the least inclusive of the packages.

Efficiency, simplicity, flexibility

Option 1: A broad-based, low rate of 3% GST with a high level of thresholds, together with the extensive use of modern information technology, would be cost-effective to administer[5]. Although the introduction of any new

tax measure requires an extensive education exercise to explain its application, the proposed high level of thresholds will keep around three-quarters of Jersey businesses out of the scope of GST, thereby simplifying its application. The Island’s tax structure would also have greater flexibility in responding to volatility in flows of taxation revenue. The “20% means 20%” element simplifies the existing income tax structure.

Option 2: A payroll tax would be relatively efficient as it could ‘piggy-back’ on the current social security contributions system. It would also be relatively simple to understand and administer.

A payroll tax could be relatively flexible in as much as rates could be changed to reflect changing circumstances. However, with an ageing population, greater reliance on the proportionately diminishing size of the employed sector of the economy to fund future demands on public services may result in the rates of tax having to increase further to raise the same amount of money. Thus, the tax structure would be less flexible and adaptable for the Island’s future needs.

Option 3: Using income tax measures would be relatively efficient as an income tax system is already in place. I would also be relatively simple to understand and administer. Whilst income tax rates and the levels of personal allowances and exemptions could be relatively easily changed to account for changing circumstances, reliance on income tax measures would not give the Island’s tax structure the flexibility it needs to react to changes in the global economy and flows of taxation revenue.

Option 4: All the proposed changes would use the existing administration infrastructure, so would be relatively efficient to administer. The income tax rates and the payroll taxes (including the abolition of the social contributions ceiling) could be flexed in future if required. However, no new tax base is introduced, which would limit future flexibility.

Economy and employment

Option 1: GST does not damage the Island’s competitiveness as it does not increase the cost of exports, and taxes both imports and locally produced goods and services on a consistent basis. It thus keeps on-Island activity competitive in both export markets and, with domestic producers facing competition from imports, without the economy of the Island having to adjust by reducing wages and/or other input costs. Accordingly, GST would not damage local employment prospects and is the option most consistent with the economic growth objectives. As long as 20% means 20% does not induce increased wage demands from those impacted, this element of the package should have no effect on competitiveness or employment.

Option 2: An employer payroll tax would have damaging consequences for Jersey’s international competitiveness. It would increase the cost of exports and make imports relatively cheap compared to locally produced goods and services. It would effectively act as a tax on jobs by increasing business’s labour costs. Employers are likely to respond to the tax by cutting staff or moving jobs off-Island to cheaper locations.

Employer payroll taxes would directly impact on the cost of doing business in Jersey. It is therefore bound to be counter-productive in terms of encouraging economic growth, and would make it more difficult to ensure that Jersey remained an attractive place to conduct business. It would also act as a deterrent to job creation and retention, unless wage rates reduce to compensate employers for their increased employment costs.

Option 3: Using income tax measures would mean that Jersey would lose the advantage of maintaining the curren 20% headline rate of income tax. This advantage arises from maintaining Jersey’s international reputation as a low tax jurisdiction and its ability to attract workers with high incomes and therefore high contributions to the States tax revenues. Workers with the skills the Island needs, not only in the financial services sector, but also in others such as health and education, may be not be attracted to live in Jersey and may choose to move elsewhere, such as Guernsey or the Isle of Man. This would have an adverse effect on employment, tax revenues and the ability to promote economic growth.

Furthermore, wealthy residents, who are very mobile, may choose to leave the Island (or may not be attracted to move to Jersey in the future). This would result in a fall in tax revenue (which would need to be borne by remaining Jersey residents), with a knock-on effect in the rest of the economy because these people would no

longer spend their money in the Island.

Option 4: The removal of the ceiling on social contributions significantly increases the employment cost for jobs above the earnings ceiling. This will be counter-productive in that it will encourage high wage/high return businesses to leave the Island. The higher rates of income tax will impact on this same group, and Jersey will have lost the advantage of the 20% top rate of income tax (see above). As the international financial services business is both high paying, and the export engine of the economy, an adverse impact on the location decisions in this sector would have a significant detrimental effect on the economy as a whole. This option could cause the Island to enter a downward spiral of loss of high earning jobs and profitable businesses, particularly in the finance sector, leading to a fall in tax revenues so requiring a further increase in taxes leading to a further loss of high paid jobs. Economically it is by far the most damaging of the four options.

Diversifying the tax base, stability, avoidance

Option 1: A GST would diversify the Jersey tax system, leading to it being less reliant on direct taxation. It would, therefore, have greater stability and be less vulnerable to volatility in flows of taxation revenue. A GST would also help to reduce the incentive to engage in tax avoidance, as the tax liability of any individual is spread over a number of taxes.

Option 2: A payroll tax would do nothing to diversify the Island's tax base and would not introduce greater stability to the tax structure as the base is earned income which is part of the existing income tax base. It would increase the Island's dependence on direct taxes. In addition, a payroll tax would be open to tax avoidance for those who could move their earnings from pay to dividends. This is important for small businesses who could avoid payroll tax by paying themselves in dividends and not pay.

Option 3: Income tax measures would also do nothing to diversify the Island's tax base and would not introduce greater stability to the tax structure. In addition, reliance on income tax measures reduces the scope for the reduction in tax avoidance – introducing new taxes to the tax base makes it more difficult for taxpayers to avoid paying tax. The higher rate of tax at higher incomes also increases the incentives to try to avoid tax.

Option 4: All the tax measures use existing tax bases, this option does not diversify the tax base. The higher rate of income tax at high incomes, plus the additional social contributions on high incomes, increases the incentives to both avoid income tax and to pay dividends rather than pay.

Other issues

No matter which tax option or base is used, all (or nearly all) of these taxes are paid for by residents of Jersey in one way or another. GST will, however, be paid by some non-residents as well as the local population. Thus, if we need to raise, say, £55 million per year to balance the budget no matter whether GST, income tax or a payroll tax is used, it is (more or less) £55 million that will be taken out of the purchasing power of Jersey residents.

There are, however, differences in the way the reduced purchasing power is delivered, the impact on the distribution of taxes within the economy and the likely economic reaction to the tax changes.

How the tax makes itself felt

– **Goods and Services Tax (GST)** – this will come through in increased prices, with perhaps a small amount of the tax effectively paid by reducing the income of Jersey shareholders (including owners of small businesses, who may not be rich), and an even smaller amount effectively paid by non-Jersey based shareholders. Exported items will be generally excluded from the tax.

– **Income tax** – this comes through initially in the reduction of take home income, so reduces the ability to purchase (which is broadly equivalent to a general price rise).

– **Employee payroll tax** has the same effect as income tax, except that unearned income is excluded from the tax base.

- **Employer payroll tax** has a similar effect as a GST in the short run, so it appears as a price increase for goods and services – except that items produced outside Jersey are largely excluded from the tax, and excluding exports from the tax is difficult. This makes goods produced in Jersey less competitive internationally, and encourages more imports. If businesses cannot raise their prices because their competitors have not been subject to the tax – for example, because they are competing with imports or they are exporters – then they will try to reduce wages, or may exit the market. In the longer term, to maintain international competitiveness, employer payroll taxes tend to end up in the form of lower wages.

- **The Committee took the view that there was no overriding advantage, or disadvantage, in delivering the tax by way of increased prices or decreased disposable income. However, where the economy needs to adjust by reducing wages the Committee is of the view that this may be difficult to achieve in the short run. This could make Jersey businesses uncompetitive for some time, as the economy tries to adjust, and the Committee is of the view that this should be avoided if possible.**

Specific impact on the tourism sector of the economy

The impact of GST on the price visitors have to pay for goods and services consumed on the Island is straightforward – unless such expenditure is excluded from the tax net, there is a rise in the prices they have to pay. However, a similar rise in prices would also occur if an employer payroll tax was introduced (unless, again, employers in the tourism sector were excluded from the tax net). Which method of raising taxes would result in higher average prices for visitors is extremely hard to quantify, but the difference between the two will be quite small.

If the tax was an income tax, or an employee payroll tax, visitors would be better off. As long as these 2 changes in tax do not trigger higher wage demands then the price of goods and services to visitors does not change. However, the down side of these 2 approaches is that for every£1 of tax that is not paid by visitors, an additional £1 of tax is paid by Jersey residents.

The option of a GST is likely to raise up to £5 million from the spending of visitors. If such spending was to be excluded from the tax base, or if income tax or employee payroll tax was used instead, that £5 million would need to be recovered from Jersey residents. This translates to an average of about £170 extra tax per resident household per year (based on approximately 35,000 households on Jersey).

Thus, in relation to the tourist sector of the economy, the Island actually faces a choice: should it try to include the spending of tourists in the tax base – in which case GST or employer payroll tax can achieve this objective – or should it be excluded and, therefore, the residents of Jersey would need to pay more tax themselves. In the latter case personal income tax or employee payroll tax could be used – or a GST with tourists being able to claim back tax they have paid on the Island.

The Finance and Economics Committee has concluded that it is not minded to exclude visitor expenditure from the tax net.

THE FINANCE AND ECONOMICS COMMITTEE'S OVERALL CONCLUSION

The Finance and Economics Committee has assessed each of the 4 tax-raising options against the general principles outlined above.

The Committee has firmly concluded that the tax-raising option which best suits Jersey's needs is the introduction of a broad-based Goods and Services Tax at a rate of 3%, together with the 20% means 20% proposals.

Together, these 2 measures have a number of advantages.

- GST widens the Island's tax base so that everyone will contribute, including temporary residents and visitors. A wider tax base gives Jersey a more secure economic foundation and makes it less vulnerable to volatility in tax revenue. (Almost all successful countries understand this and have introduced some form of consumption tax).

- Jersey residents do not bear the full cost of the tax since £10 million of the£45 million which GST would raise will be paid for by non-residents (i.e. tourists and overseas customers of the financial services industry).

- A broad-based GST is simple to administer and hard to avoid.

- Although there will be an initial rise in the Retail Price Index (this may apply to each of the tax-raising options), consumption should fall, which in turn should help drive down prices – making Jersey more competitive and a less expensive place to live.

- Everyone in Jersey would contribute a small share, but those on low incomes would be protected by enhancements to the income support scheme.

- Phasing out allowances for those with higher disposable incomes means Jersey keeps its headline rate of income tax of 20%, but the wealthier members of our community will actually pay the full 20% rate of tax on their income ensuring that the tax package remains progressive overall.

- The package would be broadly progressive.

Most importantly, the package will ensure that Jersey can look forward to a sound economic future which means that the way of life which Island residents all hold dear – with a pleasant environment, a generous level of services and a good quality of life – can be continued for generations of Jerseymen and women to come.

SECTION 2 – THE FINANCE AND ECONOMICS COMMITTEE'S TAX REFORM PROPOSALS

GOODS AND SERVICES TAX (GST)

Following the States decision in P.106/2004 to undertake further research into a Goods and Services Tax the independent company Crown Agents for Overseas Governments and Administrations Ltd. (Crown Agents) was formally contracted to produce a comprehensive report[6] containing a prototype design of a GST, including a general guide to such a tax.[7]

Their brief was to produce a design that would –

- raise circa £45 million, net of collection costs, with an initial rate no higher than 5%;
- meet recognised best practice for such taxes;
- not breach the Island's obligations with the E.U.;
- minimise the cost of collection;
- not create an inordinate administrative burden for business;
- minimise economic distortions, for example, cascade problems;
- not create an uncompetitive environment for the Island's critical industries, in particular it must not harm the competitive position of the Island's finance industry. Indeed every effort was to be made to avoid affecting the competitive nature of all the Island's industries; where this was unavoidable the implications would need to be clearly identified;
- support the objective of the total fiscal strategy package being progressive.

During a three-and-a-half month period the Crown Agents team undertook the work to prepare the prototype design, which included extensive consultation and meetings with interested parties.

The main findings of the Crown Agents Report are –

- **A Goods and Services Tax (GST) for Jersey is feasible.**
- **A simple, broad-based, single rate tax will raise the required £40-45 million tax yield. (The key to success will be not to depart from this formula.)**
- **A turnover threshold of £300,000 for business registration would allow small traders not to be burdened with the tax.**
- **The opportunity exists to adopt a GST at one of the lowest rates and highest thresholds in the world.**
- **There would be a minimal impact on the cost of living and Jersey's key industries and international competitiveness would be protected.**
- **Administration would be cost-effective.**
- **Low-income groups could be protected.**

The Crown Agents have recommended a broad-based 3% rate of GST, capped at this rate by law for 3 years and with a registration threshold of £300,000. They conclude that a GST for Jersey should be broad-based, in other words be a simple tax and with minimal exclusions. In their calculations, the only exclusions they have allowed for are exports and export-related services; extra-Island transport of goods and persons; construction and letting of residential properties; exported and domestic financial services including life assurance and postal services. The broad-based approach is favoured because it minimises the cost of compliance for traders and suppliers and means that the cost of government administration is kept low. It also maximises the revenue yield with the lowest possible tax rate. In other countries exclusions are often made in such taxes in order to attempt to provide relief for lower income groups but Crown Agents believe that this is better done through an adequate income support system.

The registration threshold of £300,000 would mean that all entities with an annual turnover of less than that amount would not have to register for GST but could volunteer to do so if it suited their circumstances, e.g. firms that are net exporters. This threshold would be one of the highest applied anywhere in the world and would mean that only 1,500 or so businesses would need to account for GST, effectively relieving three-quarters of the business community from the administrative requirements.

The simplified treatment for the Financial Services Industry would involve providers of financial services being registered for GST but with a scheme devised to establish a GST burden by reference to the type of activity and the customer profile of individual firms. Tax borne on inputs would be offset to determine a balancing liability/repayment. Their supplies would not be subject to tax and they would not be involved in partial exemption calculations (to determine their deductible input tax). The various suppliers of financial services ("vehicles") that underpin much of the activity in the sector would be subject to special provisions that secure their existing tax neutral status.

Crown Agents estimate that government administration of the prototype GST would only require an extra 10 staff They also see the burden on business as light due to advances in computer systems. They emphasize that the ease of administration is highly dependent on the tax being simple with minimal exclusions, with a high registration threshold and with full use of modern technology. They recommend that the agency with prime responsibility for GST should be the Income Tax Department but with involvement of the Customs Department for the tax on imports.

The Committee has accepted all of the conclusions and recommendations in the Crown Agent's research which accompanies this Report. The Committee is, however, aware of the sensitivities of introducing a broad-based GST which includes, for instance, food and children's clothing. The public have, however, during the consultation period expressed a strong desire to minimise the cost of administration of GST and the Committee has noted that the cost of administration rises disproportionately with the number of exclusions from the tax.

Far more importantly, however, it has noted that excluding "essential items" from GST does not make the tax more progressive. If food, for instance, is excluded from GST the rate would have to rise from 3% to around 3.5%, but the overall effect of those on lower income households would be a saving of only £12 a year, whilst the administrative cost for businesses and the States would increase significantly.

In other words increasing the number of exclusions simply increases the rate of the tax and the cost of administration but does not make the tax any more progressive.

The Committee accepts the Crown Agents view that a far more effective means of mitigating the effect of the tax on lower incomes is through an increase in income support.

The Committee also believes that the public would prefer a simple broad-based 3% tax to a complicated, administratively costly U.K style VAT which would require a rate of over 4% to yield the same level of income.

Summary of proposals

- **introduce a GST with a rate of 3% and minimal exclusions;**
- **only exclusions allowed are for exports and export-related services, extra-Island transport of goods and services, construction and letting of residential properties, domestic financial services including life assurance, and postal services;**
- **introduce the tax in 2008;**
- **cap, by law, the rate at 3% for at least 3 years from its introduction in 2008;**
- **have a £300,000 registration threshold;**
- **implement a 'simplified treatment' of the Financial Services Industry to allow for individual treatment of specific firms/sectors but structured to raise £5-£10 million overall;**
- **give the Income Tax Department prime responsibility for GST.**

INCOME SUPPORT SYSTEM

The proposed new Income Support system will replace the existing Welfare, Housing, Educational Maintenance Grant and Non-Contributory Benefit systems and will, therefore, cover all low-income groups, both in and out of work, from low wage earners to low income pensioners.

The Income Support allowance for each household will be calculated by adding up different components relating to the individual and family circumstance such as for day-to-day living and housing costs and extras, as needed, towards disability, carers, health and childcare expenses. Income, after applying a modest disregard to provide some incentive to work and save, will then be deducted. The remaining balance would be paid as a weekly 'top up' allowance.

It is proposed that the components will be increased yearly in line with the cost of living index but the system will be capable of applying interim increases if necessary, (for example, where there may be an increase as the result of the introduction of a GST).

The consequences of introducing a broad-based GST at 3% has been considered in the light of the proposed new Income Support System. It is estimated that the impact in terms of additional cost to Income Support (not including housing rent) would be no more than £2 million. This is because one of the main components of tha system, or the allowance that covers day to day living costs, would need to rise in line with any cost of living increases occurring after the introduction of GST.

The Employment and Social Security Committee presented interim reports to the States last November on the 'Income Support System' (R.C.48/2004) and a 'Policy Review of the Social Insurance System in Jersey' (R.C.49/2004). Following further consultation on the proposed system and policy issues arising, the Employment and Social Security Committee will be finalising its proposals over the next month and aim to lodge a Report and Proposition in April 2005.

Summary of proposals

- **Employment and Social Security Committee to bring forward proposals for a revised income support system.**
- **Those on low incomes will be insulated from the effects of GST.**

20% MEANS 20%

In approving P.106/2004 the States agreed to introduce a broadly progressive package of new tax measures.

The form of GST proposed, together with additional low income support, will tend to be proportional (i.e. the amount of tax paid will increase proportionately with incomes). The addition of the "20 means 20" proposals is necessary to meet the States requirement for a package of tax measures which is progressive.

The Committee considered a range of options for increasing the progressivity of the tax system through income tax. Most of these required Jersey's headline 20% tax rate to be increased. The Committee took the view that this is not desirable, as Jersey's international reputation as a low tax jurisdiction is based primarily on the 20% income tax rate which has been in existence for 65 years, having been introduced in 1940.

At a time when many countries are reducing their top rates of tax, and the Isle of Man has already reduced its top rate of tax for individual taxpayers to 18%, (already having a standard rate as low as 10% on the first £10,300 of income for a single person and £20,600 of income for a married couple), the Committee believes that raising the top rate of tax would risk losing the Island's low tax reputation, and hence its prosperity. The Island also needs to limit its top rate of tax in order to attract wealthy individuals who will contribute significant amounts of tax.

The Committee's solution, indeed the only feasible solution for increasing the income tax contribution from those on higher incomes without increasing the 20% rate, is to phase out allowances for those on higher disposable incomes.

Originally, the Committee proposed phasing out allowances over a fixed income range of £80,000 to £150,000 for all married couples and £40,000 to £75,000 for single people. In the consultation which took place in early to mid-2004, it became clear that these proposals were unfair because they would have hit people who had mortgages and dependents far harder than those who did not.

Accordingly, the Committee amended its proposals, which were agreed in principle by the States in P.106/2004 in July 2004, to take into account individuals' personal circumstances. These proposals have the same yield as the original "20 means 20" proposals but phase out allowances over a more extended range of incomes so as not to impact too adversely on any particular individual, and to more closely link the additional income tax paid to an individual's personal circumstances and their ability to pay.

These revised proposals are that a person's tax will be calculated by 2 methods, both methods taking into account personal circumstances. Under the first method tax is calculated by reference to tax allowances and reliefs being reduced year by year until 2010 with the balance of income subject to tax at 20%. The second method computes tax by reference to the basic exemption thresholds and any additions to it, such as child allowance and mortgage interest tax relief that a person is entitled to, with the balance of income subject to tax at the marginal rate of 27%. The 2 calculations involved will be carried out by the Comptroller of Income Tax who will always send the taxpayer the lower of the 2 tax bills for each year without any need for action by the taxpayer.

For the vast majority of people in Jersey, (i.e. those who are below the tax thresholds, or who currently pay tax at the marginal rate,) this will mean that they will be totally unaffected by these proposals. In other words 37,000 taxpayers, over two-thirds of all taxpayers, will not pay any more tax under "20 means 20".

The 16,000 taxpayers on the highest disposable incomes, less than a third of taxpayers, will have their allowances phased out as their incomes increase. Furthermore, these changes will be brought in over a 5-year period, so very few, if any, taxpayers will see their tax bill rise by more than one per cent of their income per year, and in the majority of cases, the increase will be less than 0.5% a year. The percentage rise in their tax bill may be larger, but nevertheless their overall liability can never exceed 20% of their income.

There has been a great deal of scaremongering and misinformation about the phasing out of allowances, so the Finance and Economics Committee has published examples of the effect of the tax on the Income Tax web site and a selection of these are attached in Appendix 1. It has been stated by some during the consultation period that the proposals result in single households being discriminated against compared to married households. The

Committee wishes to make it clear that this is simply not the case. For example, a single person without children or a mortgage earning £26,000 a year will have a £4,000 tax bill for 2004. Under the '20 Means 20 proposals they would pay £4,045. If that same person were married and the household income doubled with the wife working, the total tax bill for the household for 2004 would be £7,780. Under '20 Means 20', it rises to £8,051. So, under '20 Means 20' the single person pays an extra **£45** in tax and the couple pay an extra **£271** in tax.

It is anticipated that these proposals will be included in Budget 2006 so as to take effect from the year of assessment 2006. However, having listened to the comments expressed, the Committee is proposing that these allowances be withdrawn over a 5-year period, rather than the 3 years originally indicated.

Summary of proposals

- **The 20% means 20% proposals take into account individual circumstances.**
- **Only those with the highest disposable incomes, as judged by individual personal circumstances, will lose their tax allowances and reliefs.**
- **The 20% means 20% proposals will only affect those paying at the standard rate of 20%.**
- **These people amount to roughly 30% of the taxpaying population.**
- **The proposals will not affect those who are exempt from tax or benefiting from the marginal rate.**
- **Those not affected amount to 70% of the taxpaying population.**
- **Those who do lose their tax allowances and reliefs will do so gradually over a 5-year period.**
- **No one will pay more than 20% of their income in tax.**
- **The full effect of 20% means 20% will not be felt until the tax payment year 2011.**

LOOK-THROUGH ARRANGEMENTS

In response to the E.U. initiative on so-called harmful taxation, it has been necessary for the States to agree a standard corporate tax rate of 0% in order to retain the equivalent of the Exempt Company structure on which the finance industry is largely based. To mitigate the loss of tax from locally-owned businesses it is proposed that the Jersey resident owners of companies (or 'corporates') are taxed on the proportion of Jersey corporate profits attributable to them. These are the so called 'look-through' arrangements.

In general terms, the proposed 'look-through' arrangements will ensure that a Jersey resident owner, or partial owner, of a Jersey corporate will have the profits arising to that corporate assessed on him in proportion to his ownership of that corporate. In many cases that will be a fairly simple matter to establish but, for more complex structures, involving ordinary share capital, preference shares, participating loan stock, etc, detailed rules governing the calculation of ownership will be drawn up. The critical issue, however, is that any Jersey resident with a beneficial interest in a corporate will have the profits of the corporate assessed on him in proportion to that beneficial interest.

The Jersey resident owner will have to declare on his Income Tax Return all of the corporates in which he has an interest, whether Jersey or foreign corporates, as well as declaring his profits in all these corporates in proportion to his interest in each one of them.

Any person who has an interest in a Jersey corporate will be assessed on the proportion of his profits in that corporate as personal income.

The corporate profits arising will be taxed on the Jersey resident on an actual basis rather than the preceding year basis of assessment as currently applies to trading corporates, e.g., the corporate profits arising for the year of assessment 2009 will be assessed on the Jersey resident for that year. Alternatively, the Jersey resident can be assessed on the profits applicable to his interest on the 'accounts year' basis, e.g., if the corporate accounts year end is 30th June 2009, he can be assessed on his 'look-through' profits in the year of assessment 2009. Averaging provisions will be introduced to prevent any tax leakage on the change from the previous to the current year basis of assessment. (It is proposed that such an actual basis of assessment is also introduced for all other corporates.)

Prior to the introduction of the new regime, and by virtue of new powers that will be introduced into the Income Tax Law, a return will be issued by the Comptroller of Income Tax to all Jersey resident taxpayers, asking for a declaration of all the Jersey resident corporates, as well as all the foreign corporates, in which he has an interest. The return will also ask for a declaration of all trusts, including offshore trusts, in which the Jersey resident taxpayer has an interest, whether as settlor or beneficiary, and whether he has, through that trust, an interest in any Jersey resident corporate or foreign corporate or similar structure. Penalties will be imposed, under revised Articles 136 and 137, on any taxpayer who makes a false declaration.

Where a Jersey resident has an interest in a non-resident corporate and his interest in that corporate and the corporate itself has been established for a bona fide commercial reason and not designed in any way for the avoidance of Jersey tax, the corporate profits will not be attributed to the Jersey resident but all dividends received by him from that non-resident corporate will be charged to tax under Case V of Schedule D. The Jersey resider individual will need to satisfy the Comptroller of Income Tax that his interest in that non-resident corporate and the corporate itself is for a bona fide commercial reason and not designed in any way for the avoidance of Jersey tax, so he will need pre-clearance of any and all such transactions from the Comptroller.

There will be an automatic '*de minimis*' limit in operation for public companies whose shares are traded on a recognised Stock Exchange. That limit has yet to be finally decided but is likely to be between 2% and 5% so that those Jersey residents with an interest of such a '*de minimis*' amount will not have the corporate profits in publicly quoted companies applicable to that holding assessed on them. This is to ensure that Jersey residents are not placed in the absurd position of having a proportion of the profits of multi-national companies, such as BP or Marks and Spencer, assessed on them as personal income.

The '*de minimis*' limit will not apply to private companies, so any person who, along with connected persons, such as a husband or wife, or partner, or a relative, or a husband or wife of a relative, attempts to manipulate the

'*de minimis*' limit, and professionals or investors who attempt to create an artificial arrangement to avoid such a '*de minimis*' limit, will be caught under anti-avoidance regulations.

Individuals who possess a shareholding below the '*de minimis*' limit will not avoid paying tax as they will be taxed on the dividends distributed rather than the proportion of profits attributable to them.

The corporate profits that will be assessed on the Jersey resident will be computed on current income tax principles. In other words, the accounting profits will not form the basis of assessment, but will have to be amended in accordance with Article 70 and other applicable Articles of the Income Tax (Jersey) Law 1961.

Directors' fees paid will serve to reduce the profits assessed on those with an interest in the company and these fees will be assessed, as now, on those who receive them. Dividends will not be paid under deduction of tax and will not be an allowable deduction in computing the profits assessed on the 'look-through' basis. As they will have been paid out of taxed income, albeit in the hands of the individual owner, they will be treated as being exempt from any further tax but no tax will be available for repayment.

The Jersey resident corporate will also be required to declare on the Income Tax Return issued to it, by virtue of new powers to be introduced into the Income Tax Law, the names and addresses of all Jersey residents with an interest in the corporate.

The corporate profits, as amended to give the taxable profits in accordance with the current provisions of the Income Tax Law, will be assessed on the Jersey residents with an interest in the corporate, so the corporate will be deemed to have distributed its profits to the Jersey residents in proportion to their interest in the corporate. The Jersey residents will not be assessed on the profits deemed to have been distributed to any non-resident partial owners of the company. This will ensure that most, if not all, the corporate profits currently taxed on the corporate will continue to be taxed, albeit on the Jersey resident with an interest in the corporate rather than the corporate itself, who will be able to set off against those 'look-through' corporate profits any tax allowances and reliefs to which he may be entitled.

Where a corporate, for whatever reason, does not actually distribute enough profits to enable the Jersey resident to meet the tax liability under these 'look-through' provisions, it is proposed that an undistributed profits charge, or a deemed distribution charge, be raised on the corporate – as agent – for the Jersey resident with an interest in it, at the rate of 20%.

A Jersey resident with an interest in a foreign corporate will also have the corporate profits of that foreign company assessed on him in proportion to his interest in that foreign company.

Locally-owned finance corporates which suffer corporate tax of 10% under the proposed corporate structure will also have their profits assessed on their Jersey resident owners under the 'look-through' provisions, with credit given to the owners for the 10% tax suffered at corporate level.

Any Jersey resident who attempts to avoid or evade assessment on him through the 'look-through' provisions of the profits of any Jersey resident corporate in which he has an interest or the assessment on him of any profits of any foreign corporate in which he has an interest, will be liable to penalties, or prosecution where there is wilful neglect or fraud, under revised Articles 136 and 137 of the Income Tax Law.

Special purpose vehicle (SPV) companies used, for example, in 'off-balance sheet' financings, are typically owned by a trustee of a charitable trust and the company in question is often referred to as an 'orphan'. The profits made by the trustees through receiving dividends on the shares of the SPV for the benefit of the beneficiaries of the trust are paid to charities or applied for charitable purposes, so these profits will not be assessed on the Jersey resident trustees or, where the trustee is a company, on that company's Jersey resident owners.

Accumulated profits under the current corporate tax regime will have the same treatment as now if distributed prior to 1st January 2009. It is proposed that any accumulated profits under the current corporate tax regime which are distributed after 1st January 2009 will have the tax appropriate to that gross dividend unavailable for

repayment in the hands of the shareholder.

It is proposed that losses incurred by a trading corporate will be set off against other income of the corporate in the same year with the net income only assessed on the Jersey resident owners. Any surplus loss after such a set off will be carried forward and set off against future trading income of the corporate with the balance of profit for that future year, if any, assessed on the owners. Unutilised management expenses of an investment holding company will be carried forward and set off against future investment income and the balance of income, if any, assessed on the owners. Concession 23 group relief will still be available but the 'common ownership' rules will be more tightly drawn than at present. It is proposed that Article 107A be abolished as it not thought to be appropriate to carry back a corporate loss to earlier years of assessment thereby ensuring a tax repayment to the owner which, in all probability, would never find its way back to the corporate suffering the loss.

Even if a Jersey resident corporate is liable at a zero rate of tax, if trading or other accounts are presented for the purposes of assessing profits under the 'look-through' provisions on Jersey resident owners and the accounts so delivered are incorrect, whether through negligence or fraud, it is proposed that the corporate itself will be liable to any additional tax and the penalties laid out in the Income Tax (Jersey) Law, as agent for the owners.

The Comptroller of Income Tax will take a pragmatic approach to the administration of these proposals. In the appropriate circumstances, generally applicable concessions will be published.

The Comptroller of Income Tax has consulted on these proposed 'look-through' arrangements with professional bodies and various other professionals and the general view is that, in the majority of cases, these proposals will work without any real difficulty, although they will add an extra dimension of administrative and operational complexity to the work of both the Income Tax Office and professionals. Two issues were, however, highlighted during the consultation.

The first is the perceived difficulty in ensuring sufficient funds are available to the business to re-invest in the business. The answer to this particular issue is that the business will be no worse off than now, as it pays tax at 20% on all its profits now and these 'look-through' proposals will make matters no worse.

Another perceived difficulty is the so-called 'oppression of minority' argument. In simple terms, whether forcing the company to distribute some profits to enable some of those who own the company, for example Jersey residents, to pay their 'look-through' profits tax bill, was oppressing a minority, that being, other minority shareholders, by diminishing their wealth in the company through such a distribution. If this problem does indeed exist, it is one for the company and its shareholders to resolve, not the Income Tax Law.

These proposals are still out for consultation with the Comptroller of Income Tax, who would welcome comments on them, and proposals to address any perceived difficulties, during the next few months.

The timeframe for these proposed 'look-through' arrangements to be legislated for is likely to be in Budget 2007, as the averaging provisions mentioned above need to be introduced first and they are scheduled for Budget 2006.

Summary of proposals

- **profits of Jersey resident corporates to be assessed on Jersey residents under 'look-through' arrangements;**
- **amount of profit to be assessed will be in proportion to the individual's interest in the corporate;**
- **profits of foreign corporates to be similarly assessed;**
- **but if foreign corporate established for a proper commercial reason and not to avoid Jersey tax, clearance will be granted and no assessment of profits will be made, but dividends will be taxed;**
- **any losses incurred by a corporate will be set off to ensure only net profits assessed;**
- **'*de minimis*' limit likely to ensure small holdings in multi-national companies**

are assessed as dividends rather than attributable profits.

SELECTIVE TAXES

The move to a general corporate rate of tax of 0% has been essential to protect the Island's economy and to address the E.U. 'harmful' taxation initiative. The loss of corporate taxes will be mitigated by Jersey-owned companies through the 'look-through' arrangements, whereby Jersey owners of companies will pay tax at 20% on the proportion of Jersey corporates' profits attributable to them. Unfortunately, it has not been possible to apply a similar arrangement to non-resident owners of corporates, as they pay tax in their country of residence.

The Finance and Economics Committee has spent considerable effort in investigating whether a selective tax could be implemented which would help restore a Jersey tax liability to Jersey for non-finance sector companies that are owned by non-resident shareholders.[8] These companies will be subject to a zero corporate profit tax rate in Jersey. It should be emphasized that most, if not all, of these companies will not be paying less tax in future – they will merely be paying the same amount of tax but in another jurisdiction rather than in Jersey. Any additional tax liability imposed on them will usually be an additional cost of doing business in Jersey.

In order to comply with the E.U. 'harmful' taxation initiative it is not possible to discriminate against non-locally owned companies. The only solution to this is to apply a new tax against all local and non-locally owned companies, but to allow local companies to offset tax paid by their owners against this new tax. However, by making payment of this new tax off-settable against any Jersey corporate profits tax liability, and capping it at a maximum of 10% of profits, it would be possible to ensure that no additional tax liability would fall to Jersey-owned companies, or financial services companies. It is also necessary to ensure that non-trading Jersey companies which form the corporate vehicles for the customers of the international financial services provided in Jersey do not acquire a tax liability. If they did, Jersey would become uncompetitive in much of its main export market.

Broadly speaking, 3 possible options have been identified – a tax based on number of employees, total cost of payroll, or on property occupied (some form of commercial rate). Whilst all 3 options are technically feasible in terms of implementation, they all potentially suffer from undesirable economic consequences for the people of Jersey. To varying degrees they could to lead to increases in prices locally or a relocation of jobs in non-Jersey, non-financial services companies.

In addition, the technical complexity of all 3 taxes, which would have to be both capped and off-settable, so as not to impact adversely on locally owned businesses, would make them relatively easy to avoid in the absence of intrusive anti-avoidance measures.

It is estimated that the maximum level of tax revenue that could be raised from any one of the 3 options under consideration would be at most £5-£6 million per annum. However, there is a possibility that the damage to the competitive environment may disadvantage Jersey residents more than any additional tax revenue generated.

Initially the loss of tax revenues from non-resident, non-finance companies was estimated to be £20-£25 million. Whilst this figure is correct, further analysis has shown that regardless of the Fiscal Strategy, £10-£12 million was going to be lost anyway. The reason for this is that a small number of specialist non-resident, non-finance companies, will be leaving the Island before 2008 for reasons unconnected to the move to 0/10%. In the initial calculations this tax revenue was incorrectly included in the amount that would be lost as a result of 0/10%. In reality, whilst it will still be lost, it would be lost irrespective of the change. As has already been stated, of the remaining £10-£12 million lost, the maximum amount recoverable is likely to be no more than £6 million, but the cost of seeking to recover this loss of revenue, in terms of increased prices and lost jobs, is likely to be greater. Accordingly, the Committee does not propose, in the first instance, introducing new off-settable taxes on employees, payroll or property but will review the situation once the 0/10% corporate regime is implemented.

Summary of proposals

- **A Selective tax on non-resident, non-finance companies could lead to these businesses becoming uncompetitive, job losses, an increase in prices paid by local residents and the revenue raised could be marginal.**
- **It is therefore proposed that a selective tax is not applied to non-resident, non-finance companies.**

ANTI-AVOIDANCE MEASURES

The move to a 0% corporate tax rate and the introduction of 'look-through' arrangements will necessitate a strengthening of anti-avoidance legislation.

It is the Committee's view, therefore, that Article 134A should be strengthened by placing an obligation on every taxpayer to report to the Comptroller any investment or financial scheme that will result in the avoidance, deferral or reduction of Jersey tax. Where the scheme is related to an employment, the employer must automatically report the scheme for a ruling. These measures will ensure consistency of treatment and greater fairness in the distribution of the tax burden.

All submissions must have a full and complete description of the transaction or scheme and the amount of Jersey tax that will be avoided, deferred or reduced.

There will also be enhanced information powers introduced to ensure the disclosure of the names and addresses of all companies and trusts, whether in Jersey or offshore, in which a Jersey resident has any interest.

Revised penalty provisions will also be introduced, so as to ensure that penalties are levied on any taxpayer who makes a false or incorrect disclosure in relation to these new provisions, or who conceals, destroys, alters or disposes of any document which may contain information relevant to a taxpayer's liability to Jersey tax.

It is anticipated that these new enhanced powers will be brought forward in the Budget 2006, prior to the 0/10% reforms and related 'look-through' provisions.

The Comptroller of Income Tax has also consulted on these measures and there is a general acceptance amongst professionals that these new enhanced powers are needed, so the Comptroller has had very little adverse reaction to these proposed new powers.

One issue which was highlighted is the need to have a list of exclusions prepared to show which 'common life events' would be exempted from having to be reported for pre-clearance to the Comptroller under an enhanced Article 134A.

Another point which was made is that the current very quick turn-around of rulings by the Comptroller ought to be continued and that these new powers should not slow down this process.

Summary of proposals

- **any arrangement, scheme or transaction that results in the avoidance, deferral or reduction of Jersey tax to be reported for a ruling under an enhanced Article 134A;**
- **'common life events' exclusion list to be prepared;**
- **where arrangement relates to an employment, the employer to disclose;**
- **current quick turn-around of rulings to continue;**
- **enhanced information powers to ensure Jersey residents declare all interests in trusts and corporates.**

ENVIRONMENTAL TAXES

In P.106/2004 the States charged the Finance and Economics Committee to undertake further research into environmental taxes. Working with the Director of the Environment the Committee commissioned Oxera to undertake this work, the findings of which are summarised below.[9]

Background

The development of environmental taxes is usually recognised to have 2 principal purposes –

1. to raise revenues from activities that are seen to be damaging towards the environment so as to cause a change in behaviours and attitudes by making those behaviours more expensive;

2. to raise revenues from activity that damages the environment, so as to create funds to invest in measures that will reduce or mitigate this damage.

These purposes are not mutually exclusive and in fact both may be happening at the same time in a well-structured approach.

In the first example there needs to be sensitivity to price to cause the required shift in behaviour. If the behaviour shifts as predicted then the amount of revenue recovered will of course fall unless the tax rate is increased again.

In the second example the investment of tax revenues may be used to create alternatives that allow a change in the damaging behaviour (e.g. a tax on congestion that is used to fund a better and more regular bus service, or a tax on domestic fuel that is used to subsidise home insulation and other energy efficiency measures).

As with most taxes the behaviour of those exposed to them is to minimise their need to pay. For environmental taxes this is often possible by a shift in behaviours, so there is a need to anticipate revenues falling over time or to plan for a ratcheting-up strategy to keep revenues stable or growing.

The cost of setting up the tax collection regime may seriously defray the value of the revenues collected – particularly in Jersey where the yields can be quite low. For instance, it has been assumed that establishing a plastic bag levy similar to Ireland's would not be cost-effective in Jersey (although it might achieve the second purpose of shifting attitudes and behaviours at neutral cost).

Environmental taxes are often similar to sales taxes in their distributional impact. Such taxes can often be socially regressive because their application is across the whole spectrum of the population and ability to pay is not considered. A regressive effect can be mitigated if those affected can change their behaviour and limit their tax exposure.

Acceptance of environmental taxes is likely to be greatest when the revenues are hypothecated toward a purpose that is related to the activity being taxed. So for instance, a congestion charge which is used to improve public transport; or an energy tax that allows the payment of subsidies for the installation of household insulation.

An Environmental Tax Strategy for Jersey

If environmental taxes are to have credibility they need to be seen to be contributing to delivering an overall strategy to improve the environment; if not they will quickly be discredited as a backdoor attempt to increase personal and business taxation. It important, therefore, that before any environmental tax is brought forward it meets environmental objectives, such as the 5 key environmental priorities identified in the "State of Jersey" report recently published by the Environment and Public Services Committee. These are –

1. Tackling climate change – reducing consumption of fossil fuels.

2. Dealing with Waste – being efficient with our resources.

3. Traffic and Transport – Reducing congestion, improving air quality and taking cars out of the urban streetscape.

4. Water – Quantity and Quality.

5. Countryside and Natural history – preventing the development of greenfield sites.

Approach

For the purpose of the analysis into environmental taxes, user pays charges, whilst not strictly taxes, should be included given their similar mode of action.

This analysis was divided into 2 stages.

In the **first stage** the environmental taxes were examined simply to assess if they had the capability to make a significant contribution to the **financial** revenue targets required by the fiscal strategy.

In the **second stage** the environmental taxes are being examined to determine if they are capable of achieving the **environmental** goals of the States Strategic plan.

Revenue-raising potential

The first stage analysis is described in Appendix 1 of the Oxera Report '*Which tax is best suited to Jersey's objectives'(February 2005).*

The methodology used in assessing which environmental taxation options might have significant revenue-raising capacity in Jersey was been based on 2 stages:

– identifying a full range of environmental tax options, drawing on international experience, suggestions from the States of Jersey, and Oxera;

– examining in more detail those environmental taxes within this range that might have 'substantial' revenue-raising capacity. Revenue-raising estimates were calculated on the basis of 'reasonable' rates (i.e. similar to those levied in other countries) and rates required to achieve a 'substantial' level of revenue (defined as £10 million).

The conclusions of this study were that overall, environmental taxes could offer ways to raise significant levels of revenue, but do not prevent the incidence falling on the population of Jersey, and their distributional impact may not be benign. Those that might be feasible and which are capable of generating significant revenue include taxes on motoring (possibly including congestion taxes for St. Helier), taxes on energy use and taxes (direct charges) for waste disposal.

However, the environmental benefits of taxes that are reasonably efficient at raising revenue may not be that great, while the efficiency of tax may be low compared to using general taxes to raise the same amount of money. The exception to this is where the tax infrastructure already exists (e.g. road fuel) or where the existing billing/distribution system would mean that a new tax would be (relatively) easy to administer (e.g. tax on energy consumption).

In the case of congestion taxes/charging and taxes/charges for waste disposal a suitable infrastructure does not currently exist in Jersey. The revenue-raising efficiency of taxes using these 2 tax bases is, therefore, likely to be low compared to using existing taxes. Thus the additional administrative costs of these taxes would need to be justified by their environmental benefits – in the absence of environmental benefits the population of Jersey will have to pay for an administrative process that is actually unnecessary to achieve a net increase in general tax revenues (or their equivalent).

Finally, the distributional consequences of environmental taxes are harder to manage, and the large tax bases with appropriate administrative infrastructures for tax collection (i.e. energy consumption and car use) tend to have an inbuilt regressive structure, overlaid with significant variation in the incidence of any tax within any income group. The distributional consequences of any environmental tax need to be taken in the context of the overall tax burden, but in the absence of a significant environmental benefit there is little benefit in using taxes that have more problematic distributional implications just to raise revenue.

This suggests that in developing an efficient tax structure to deliver both revenue and environmental benefits environmental taxes should be primarily evaluated on the basis of their environmental benefits. If such a tax (or equivalent in charges) is justifiable on environmental grounds then it may also be an efficient way of raising additional revenue, and this should then be evaluated against the main revenue raising alternatives. ***Using environmental taxes primarily to raise additional revenue runs the distinct risk of creating a tax structure that is inefficient in terms of overall costs and equity in the delivery of both environmental benefits and general taxation revenues.***

However, notwithstanding these reservations, it is clear that energy taxes, car taxes and motor fuel taxes could both deliver significant revenues and be designed to deliver some environmental benefits, but most likely with a fairly regressive impact. The potential taxes would include:

– annual vehicle tax, based on emissions;
– additional taxes on petrol and diesel;
– tax on energy input use.

Whether or not these taxes should actually be used to raise significant amounts of revenue is largely a political question, in particular whether the distributional consequences are acceptable. In addition, the general consequences of levying taxes on final consumers, or on inputs to industry, should be taken into account.

Potential to achieve environmental goals

In the second stage, under the direction of the Environmental Adviser to the States of Jersey, further research is taking place into the potential of the environmental taxes to achieve environmental objectives and this work is focussing on motoring charges, waste management and energy/climate change. The test framework for this second stage looks at the following questions.

(i) What is the environmental issue, and is it important?

(ii) Is the current policy package sufficient, and could existing instruments be improved?

(iii) What are the negative impacts of tackling the problem?

(iv) What environmental tax is proposed?

(v) What are the advantages of a tax over other options, and would a tax be effective?

(vi) Would other measures be removed if there were a tax?

(vii) What are the negative impacts of the tax, and how can they be mitigated?

Areas that have been examined for their potential to deliver environmental goals are as follows –

- pollution from agriculture;
- climate change;
- motoring charges;
- waste management;
- land development tax.

Of these 5 it was possible to eliminate 2 fairly quickly. Pollution from agriculture can be tackled more efficiently by using other instruments that already exist and by changes in practice that can be assisted through the new agri-environment funding. Land development Tax was not seen to deliver any real environmental benefits as the principal control mechanism for new development is the planning law. However, Land Development Tax is being examined under the revenue raising options of the fiscal strategy (see further details in next section).

Current focus for the development of environmental taxes is therefore on energy, waste and motoring charges.

Summary of proposals

- **A range of possible environmental taxes have been examined in the work undertaken by the Environmental Adviser in conjunction with Oxera.**
- **Environmental taxes could not make a significant contribution to the £80-£100 million tax deficit.**
- **This is because either environmental taxes succeed in altering behaviour, in which case they do not raise significant revenue, or alternatively they require redeployment of the revenues raised in order to achieve their environmental objectives.**
- **Environmental taxes tend to be regressive.**
- **However, there are compelling reasons to further consider environmental taxes to deliver the environmental objectives of the States Strategic Plan.**
- **Further research work will continue to be advanced on the promising and appropriate environmental taxes – these being those that deal with motoring charges, waste management and energy/climate change**

DEVELOPMENT LEVIES

Development gains occur when land is reclassified from a lower value use (e.g. agricultural) to a higher value use (e.g. housing). As the increase in value is due to a decision of government rather than through the efforts or risk of the landowner, taxes are advocated as a means of capturing some of the substantial gain through a development levy, hereinafter referred to as a 'Development Gain Tax (DGT)'.

In approving the Fiscal Strategy (P.106/2004), the States charged the Finance and Economics Committee to "… undertake further research into …development levies…in order to investigate the feasibility of their introduction, and to bring forward details to the States with recommendations for approval by February 2005".

Research has been undertaken by Oxera[10] in conjunction with officers of the Treasury and elsewhere, within the context of other associated issues –

- The development of a draft framework for the Use of Planning Agreements/ Obligations.
- The advance of development proposals for land rezoned in 2002 for 'Category A' housing.
- The publishing of the final 'Barker report' by the U.K. Office of the Deputy Prime Minister.

By rezoning land for development, government by its action increases the value of that land. This is particularly the case where land has a low initial economic value in use, such as in the agricultural sector.

There is a perceived inequity in bestowing substantial wealth on a small number of landowners with no mechanism within the current taxation system to recover any of the gain for the benefit of the wider community.

Revenue-raising potential

The 2002 zoning proposition rezoned 11 sites in Phase One (H2), with an expected yield of 560 units c 'Category A' accommodation, split 45% social rented housing and 55% first time buyer housing.

Development of these sites has not yet progressed sufficiently to determine the likely uplift in value, however, based on experience from the previous rezoning and discussions with landowners and prospective developers, a plot value of £30,000 for social rented units and £80,000 for first-time buyers would seem to be a reasonable, conservative estimate.

On this basis, if the 2002 rezoned sites were developed as stated in the Island Plan, an overall plot value of £32.2 million would be achieved. Assuming an 'across the board' agricultural value of £4,000 per vergée for the 103.3 vergées rezoned, the sites prior to rezoning would have achieved a value of £413,000. The uplift on this basis would be some £31.8 million.

The above assumption gives a ratio of agricultural to residential land price of 1:78. The Barker report[11] provides uplift ratios for the United Kingdom, as shown in Table 1 below. U.K. figures reflect all types of residentia property not just 'affordable' equivalents to the Jersey 'Category A' properties.

Assuming an average plot value of £160,000 for 'Category B' properties with 5 properties per vergée, the 'Category B' uplift would be in the ratio 1:200.

Table 1:

Region	Value of arable agricultural land per vergée (£)	Value of land for residential use per vergée (£)	Ratio of agricultural to residential land price
North East	1,355	221,223	1:163
East Midlands	1,340	318,345	1:238

South East	1,641	496,403	1:303
Jersey (Cat ‘A’)	4,000	311,713	1:78
Jersey (Cat ‘B’)	4,000	800,000	1:200

The 2002 Island Plan contains a second phase of 11 sites for rezoning (H3), comprising some 55 vergées with a estimated yield of 313 dwellings. On the same assumptions as used above, the agricultural value of these sites would be £220,000 and the rezoned residential value some £18 million– an uplift of around £17.8 million at a ratio of 1:82.

Although the potential uplift in land values for the rezoned H2 and H3 sites approaches £50 million, rezoning on this scale is a rare event and revenues generated by DGT would be sporadic in nature. The States considered rezoning propositions in 1987, 1989, 1990 (two), 1999 and 2002, which included urban, urban fringe and greenfield sites, with a mix of ‘Category A’ and ‘Category B’ properties, varying from a few vergées on former commercial sites to significant ‘new estate’ developments.

Future sites for rezoning are identified in the current Island Plan (the ‘H4 and H5 sites’), but the speed at which these and other sites could be developed is subject to demonstrable need based on economic demand, social and demographic factors and, not least, political appetite.

Land as a tax base

The Oxera report acknowledges that land is a good base on which to levy a tax as ownership can usually be defined and it is the least mobile of all tax bases. There is a clear profit incentive for landowners to seek to have their land rezoned and DGT should not remove this incentive providing the rate is not excessive and there is a reasonable expectation that the tax is to be permanent.

Economic factors and tax incidence

The size of the uplift in value would suggest that there is scope for a significant share to be captured by government, whilst still providing landowners with a surplus that would not otherwise be achieved. This assumption is only valid in a market where sufficient land is rezoned to generate competition between landowners.

The higher the level of ‘tax’, the greater the incentive to not release land in the hope that a future government will adjust downwards or remove the ‘tax’. This behaviour pattern will be strengthened where –

- the landowner exists in an uncompetitive market;
- there are a small, finite number of sites available for rezoning; and
- there is a low risk of the land being ‘de-zoned’ back to agricultural use.

There does seem to be a case for the government to participate in the gain and ensure the wider community benefits. However, if the aim is to increase the supply of land for development (e.g. to meet the needs of the Strategic Plan) then the interaction with the planning system is vital. That is, taxing an activity normally reduces it and to ensure this is not the case in Jersey it would need to be backed by the right planning policy.

Introduction of DGT without the backing of the right planning policy could actually mean that supply of land for development drops, pushing up property prices as less residential property comes on stream. This would suggest that a differential tax structure would be required to avoid discouraging development in pursuance of States objectives (e.g. social housing or utilisation of ‘brownfield’ sites).

Assuming the housing market is economically efficient, there is limited opportunity for landowners to pass on DGT to developers (and ultimately into the property purchase price). In a small market, with limited available rezoned land, landowners may be able to influence supply and successfully pass on some of the DGT to

developers (and thereby increase house prices).

However, as 'new build' properties compete with the much larger 'second hand' housing market, the scope to pass on DGT is likely to be limited even under these circumstances. This risk can be reduced through the rezoning of sufficient land to ensure that the market remains in equilibrium.

Tax design

In order to make it effective, DGT would need to have the following characteristics –

- **Credibility** – that the proposed 'tax' is applied consistently and equitably. The 'tax' must be considered as a long-term policy that will not be amended or withdrawn should rezoned land not be brought forward for development.

- **Be simple to understand and administer** – the valuation regime supporting the policy must be transparent, easily understood and robust enough to avoid the sort of lengthy challenges that accompany acquisition by compulsory purchase. The cost of administering and collection, whether incurred by government or other parties, must be minimised.

- **Well-targeted** – that the proposed 'tax' is applied equitably. It should be able to withstand avoidance measures that could be applied by both major developers and individual landowners.

- **Set at an effective 'tax' rate** – that maximises the potential return to government without encouraging landowners not to bring forward land for development. Various U.K. schemes have been in place since the War, with rates as high as 100% of the gain (1947) and different rates for companies and individuals based on the Capital Gains Tax regime (1973)

Three broad areas could be investigated to determine whether they have the potential to capture an element of the 'windfall' gain –

Income Tax System – the identified gain could be included as declarable income or profit for taxation purposes, with the individual or company liable to pay tax at a defined rate.

The Comptroller of Income Tax considers that such a tax would be a fair and equitable tax and, if set at a high enough rate, say 50%, could yield significant but erratic revenues.

The legislation would not sit well within the current Income Tax Law and there would need to be separate legislation, such as, for example, a Development Land Tax Law, perhaps similar to the Guernsey Dwelling Profits Tax Law.

It would not be onerous for Income Tax staff to administer, but problems could arise in respect of –

- the need for a new reporting regime;

- avoidance (for example, changing land into company shares then selling shares);

- concealment of transaction data. There is a financial incentive to seek to conceal evidence of a transaction.

- There may be a time-lag between assessing the relevant uplift value and collecting the tax due.

Where a developer is engaged in the trade of property development, for example producing luxury housing on a disused hotel site, such a developer would currently pay income tax on all his profits.

Capital Gains Tax on 'Hope Value' – a condition of obtaining planning approval could be the payment of a contribution to the Government, based on the uplift sum associated with the scheme seeking approval. The

fundamental issue of whether the Planning process is the appropriate mechanism to extract 'tax' would need to be carefully considered.

Valuation methods and timing consideration would also need to be addressed, as would the need to clearly differentiate between the 'tax' on the increased value due to rezoning and any commuted sums applied through planning obligations.

Stamp Duty – a form of 'super stamp duty' could be applied to capture an element of the windfall from the vendor of the land at point of sale.

It would not be feasible for the Judicial Greffe to be made responsible for the collection of 'super stamp duty' (i.e. to capture an element of windfall) from the vendor of rezoned land at the point of sale. The present conveyancing system in Jersey does not enable this.

Whichever instrument is considered, the key issues of quantifying the level of uplift and ensuring that DGT is not avoided, present significant difficulties.

The Oxera report discusses the alternative of 'Planning Gain' to extract some of the uplift value through acquiring 'benefits in kind' in the form of public goods. Article 8A of the new Planning Law gives the States powers ir relation to planning agreements, but this does not extend to a 'betterment tax' as extraction of value must be directly related to the proposed development and be fair, reasonable, necessary and in scale with the development.

Planning gain has some way to go before it has matured into an accepted and commonplace part of the development process in Jersey, but it may be a more effective way of capturing uplift from rezoned sites.

The economic considerations relating to the imposition of planning gain are similar to those inherent in DGT and its success relies on many of the characteristics of successful DGT being in place.

Conclusions

The Oxera report concludes that –

- There appears to be scope for DGT.
- DGT would not impact on house prices if the housing market were operating efficiently.
- DGT would need to have sufficient credibility as a long-term instrument to ensure landowners did not collude to prevent release of land to the market as a means of forcing the withdrawal of the tax.
- Differential tax rates would be required to promote developments of a specific type or on specific sites.

DGT is considered not to be a suitable tax to mitigate the loss of tax revenues from a move to the '0/10%' tax regime for the following reasons –

- An accurate assessment of yield cannot be easily ascertained, but it is not likely to meet a significant proportion of the anticipated £80-£100 million shortfall.
- Revenues generated would be sporadic, against the need to deliver an ongoing, regular replacement revenue stream; to maintain the revenue, land would need to continue to be re-zoned, a policy which may not be desirable or sustainable.
- Assessing the value of uplift in land, and when it has been realised, is complex and could be open to legal challenge.
- Concern has been expressed that the tax may be avoided and that there are incentives to seek to evade

disclosure of relevant information.

- Introducing DGT at the same time as developing planning gain policy will cause uncertainty in the market and may run contrary to the policy of encouraging the provision of homes, particularly in the social rented/first time buyer sectors.

Summary of proposals

- **A Development Gains Tax is not an appropriate measure to make a significant, recurring contribution to the £80-£100 million shortfall, but**
- **such a measure should be further considered in conjunction with the development of a planning gain policy.**

SECTION 3 – ALTERNATIVE TAX OPTIONS

PAYROLL TAX

In response to the States decision, in P.106/2004, to charge the Committee to undertake further research into a payroll tax, the Committee commissioned the attached Report ***'Which tax is best suited to Jersey's objectives – An evaluation of alternative tax options?' (February 2005)*** by Oxera. This work compares and contrasts the relative merits of the different tax options in both the short-term (transitional effects) and the longer term, concentrating particularly on the GST and Payroll Tax options.

In terms of this compare and contrast exercise the Oxera research has concluded that in particular –

- A Goods and Services Tax (GST) has a broader tax base and leads to a more diversified tax system. Consumption taxes are paid by everyone, whatever the source of income. By contrast, payroll taxes would not help to diversify the Island's overall tax base given the narrowness of the tax base to which they relate.

- Payroll taxes can only be levied on wages and salaries. In addition, payrolls already form part of the tax base in Jersey – via the social security contributions system.

- The advantages of a diversified tax system are that the tax revenue would tend to be more stable and predictable, and incentives for tax avoidance and evasion of tax would be diminished.

- Employee payroll taxes directly reduce the rewards from working, possibly leading to changes in work incentives, such as a reduction in the number of hours worked, or by creating disincentives for the unemployed to seek new jobs.

- GST has an advantage over employer payroll tax (and employee payroll tax) in that it removes the ability to avoid the tax for those who can move their own earnings from pay to dividends. This can also have an impact on competition between small and large businesses.

- Employer payroll taxes will increase employment costs, which may lead firms to reduce their demand for labour by opting for less labour and more capital-intensive production techniques, a reduction in activity, or by outsourcing labour-intensive business activities.

- Employer payroll taxes may also lead to the relocation of jobs in export industries if the demand can be served at lower costs from other locations.

- Employer payroll taxes do not offer a mechanism of excluding payroll taxes from final output prices, and directly increases a firm's costs. As a result, until the economy has adjusted by reducing the costs of other inputs (e.g. wages), the international competitiveness of Jersey businesses suffers.

- A major advantage of GST is that in general exports would be zero-rated, meaning that there is no direct adverse impact on competitiveness from its introduction. This benefit cannot be delivered by payroll taxes.

- Both GST and payroll taxes have the ability to trigger a wage-price inflation spiral (the main differences between the alternative tax options relate to initial impact effects).

- A GST would be relatively more expensive to set up and run.

Whilst this analysis focuses on the relative merits of GST and payroll tax and suggests reasons why the former may be preferred, the Oxera analysis does suggest an eventual economic outcome in the long term which might be much the same under either option. Nevertheless, the nature and experience of the transition towards that similar

economic outcome is suggested by the research to be different according to which tax option is taken. It is in this respect – in the particular context of Jersey – where real concerns over whether payroll tax is an appropriate option for the Island.

The Oxera analysis makes a base case for payroll tax as a relatively inappropriate option founded on its narrow base, erosion of competitive advantage in Jersey's vital export markets, relative ease of avoidance and potential distorting impact on internal competition on the Island. It is clear that the real costs of a payroll tax would be borne by Jersey residents either by feeding through into higher prices or by a forced downwards adjustment in real wages. Given that a reduction in nominal wages is likely to prove impossible to impose, the obvious alternative way to achieve the adjustment required to a rise in employers' real costs is by a reduction in the aggregate stock of jobs in the economy. To hope that employers will absorb a rise in their real costs through a reduction in profit margins (returns on capital) seems to have no precedent in any major market experience previously seen and is thus viewed as unrealistic.

For all of these reasons, payroll tax might in any event be considered unattractive but becomes all the more so when overlaid with a particular feature of the Jersey economic fabric.

The Island is host to a number of multinational players, primarily banks, which are both major employers and major contributors, through the significant profits they generate in Jersey, to the public purse. However, these large concerns are equally represented in all other major finance centres where they also have significant employment and activity bases. In a global economy, Jersey's cost base, particularly unit wage costs, are constantly being assessed and compared to similar costs elsewhere, given the propensity of large financial services firms to centralise/relocate activities to exploit maximum possible economies of scale. At a time when Jersey's wage costs are already considered to be high, it seems a significant risk to be considering adding major non-wage costs in the form of an employer's payroll tax when a component of the Island's major industry, which already has a high concentration of jobs and profits taxes within the Island's overall economy, is vulnerable to such outsourcing. The effect might well be to encourage relocation of significant activity and employment away from the Island in a high value sector, with the subsequent 'hollowing out' of the activity in the Island bringing an even more critical future assessment by shareholders of the costs of maintaining the same presence as hitherto.

Outside the banking sector, there is less of a critical exposure to outsourcing. However, much of the Island's high-earning, knowledge-based businesses such as those in the Trust sector are also careful to manage costs where skilled people are at a premium and ultimately similar considerations to those which apply in other areas as outlined above are likely to come to the fore.

These particular features of Jersey's open international economy do suggest that embrace of an employer's payroll tax might mean undue risk to Jersey jobs as a particular consequence of the economic transition process which plugging the fiscal deficit entails.

In such circumstances, given that a payroll tax may well lead to lower wages and/or businesses employing fewer workers and given an ageing population, a downward spiral could develop. Reduced employment and wages could lead to a reduction in the tax take, which could mean that the rate of payroll tax would need to increase further, paid for by a smaller workforce, to fund the demands of an ageing population and to meet the shortfall in taxation revenue. These further hikes in the rate of payroll tax could lead to yet more job losses and decrease in real wages, and so the downward spiral would develop.

The effect may also be to change the nature of economic activity in the Island with migration of higher value business to the detriment of the economy's depth and diversity.

On the basis of the Oxera research the Committee has come to the conclusion that of the prime tax raising measures i.e. GST, income tax and a payroll tax, the most damaging for the Island is an employer payroll tax. Such a tax is a tax on jobs. It will directly increase the cost of employing people and so encourages employers to shed staff and/or move work to less expensive jurisdictions. It is likely to lead to a painful economic adjustment of increased unemployment leading to lower wages. There is a significant risk that it could lead to one or more

major employers in the finance sector leaving the Island. This would have an immediate substantial reduction in tax revenues and increased unemployment with knock-on consequences right the way through the economy.

Furthermore, employee payroll taxes are inherently unfair. They result in those in employment paying for the services consumed by those living on unearned income, who although perhaps quite affluent, do not pay the tax. In addition, with a growing proportion of retired people in Jersey it will result in a rising tax burden increasingly being shouldered by the declining proportion of the population in employment. For these reasons a payroll tax is not favoured by the Committee.

The Finance and Economics Committee recognises the strong attraction of a payroll tax such as an increase in employer and employee social security contributions. The mechanisms are already in place to collect the tax so the administrative costs would be minimal. The sums raised are also significant. An increase in employer and employee social security contributions of 1% on either side, combined with the removal of the social security ceiling, would for instance raise about £45 million[12].

Furthermore, it can be argued that it is only fair for business, through the employer contribution, to contribute to the loss of tax arising from the reduction in the corporate tax rate. The flaw in this argument is that the corporate tax rate is being reduced to maintain the Island's competitiveness and hence its prosperity. Accordingly, seeking to recoup the lost tax through an increase in business taxation will have taken the Island economy full circle and make Jersey less competitive and hence less prosperous.

Conclusion

Whilst appearing administratively simple, a payroll tax would be the most damaging to the Island of the three major tax options. It is a tax on jobs which could lead to unemployment and reduced rates of pay. It could also start a downward spiral of fewer people in employment creating the need for further payroll tax rises which in turn generate more unemployment. For these reasons a payroll tax is not favoured by the Committee.

INCOME TAX CHANGES

It has been suggested that insufficient attention has been given to the option for raising the required taxation revenue by revising the income tax system. Such amendments were considered and rejected at the time of the debate on P.106/2004, and the reasons for rejecting them remain equally valid now.

However, for the sake of providing further information, and in order to make realistic comparisons, an indication of the measures necessary to raise the sum of £55 million solely from income tax is shown below–

- **Option 1:** Tax all taxpayers with net taxable incomes above £80,000 at a higher rate of 40% on income over £80,000, and increase both the standard rate and marginal rate of income tax from 20% to 25%, and from 27% to 32% respectively.

- **Option 2:** Increase the standard rate of income tax from 20% to 25% and reduce personal tax exemptions and allowances by 25%.

Option 1: Introducing higher rates of income tax

The Committee considered various ways of introducing higher rates of Income tax for those with higher incomes. It sought to achieve a level of greater tax contribution from wealthy residents, which would not ultimately be counter-productive by causing this highly mobile segment of the population to move to jurisdictions with a lower tax burden.

If a higher rate of income tax was levied on taxable household income over £80,000 it would be likely to raise

slightly more than £1 million per annum per one per cent point increase above 20%. So a rate of 40% migh potentially yield somewhere in the order of £22 million.

However, at this rate of 40%, the highest income households in the Island could save a considerable amount of tax by moving to a lower tax rate jurisdiction like the Isle of Man or Guernsey. If only 2 in 5 of taxpayers who suffered a sharp rise in income tax (i.e. more than about £20,000 per year) decided to move, the total tax revenue collected would increase by only £4 million. Alternatively, if the around 60 households with the highest ta liability, and who had seen their tax bill rise by more than £80,000 per year, decided to move, again there would be little or no increase in the total tax revenues raised. At this level of movement the rest of the Island is likely to be worse off.

In addition to the direct impact on tax revenues, emigration of this sort would be likely to cause a reduction in on-Island expenditure and other economic activities, so there would be additional knock-on effects in the economy.

In the unlikely event that a 40% tax rate did raise £22 million without any leakage this would still require £33 million to be raised further down the income scales.

The Committee takes the view that at a top rate of even 30%, let alone 40%, there is a real risk that a significant amount of taxable income would leave the Island and that this would have negative consequences for the rest of the economy. It is almost impossible to accurately estimate such a risk, but nonetheless the judgement of the Committee is that the risk is real and should be taken into account. The Committee believes that with a top rate of tax of 20% in Guernsey and 18% in the Isle of Man it is vital not to increase Jersey's headline rate.

Option 2: Increasing the standard rate and reducing allowances

The Committee has also considered the option of increasing the standard rate of income tax to 25% and reducing personal allowances and exemptions by 25%. There would be 2 main effects from this proposal.

The first, stemming from the reduction in personal allowances and exemptions, is that all income taxpayers would see their tax bills raised by an amount that would not vary smoothly with income, but would vary by household composition. For example, a single person with no children would see their tax bill rise by around £740 per annum if they were a current taxpayer with a low income (between £11,000 and £19,000 if they don't have a mortgage). At higher incomes the increase in tax is lower, reflecting the current lower personal allowances compared to income exemptions, and the lower rate of tax (20% compared to 27%). So a single person with an income above £26,000 will pay an additional £300 in tax. (Between £19,000 and £26,000 the additional tax declines from £740 to £300).[13]

The more personal allowances there are in a household the higher the increase in tax, although the income at which the tax increase starts is also higher. So a couple with 2 children, both working and no mortgage will pay about an additional £1,800 per year at incomes between about £30,000 and £40,000, and around £900 at incomes above £54,000. Although this measure does not increase the tax of the poorest members of society the effect of a substantial reduction in exemptions and allowances is still to concentrate the additional tax at relatively low income levels.

The second effect stems from the introduction of the higher tax rate of 25% on taxable incomes above £80,000. This is a progressive measure, and for those with incomes above the threshold there is an increase in tax of £50 per year for every £1,000 over the threshold. However, this does require the headline rate of tax to increase. As a result of these two effects the Committee sees difficulty in such an approach.

The Committee has concluded that there are considerable advantages in maintaining the current 20% headline rate of income tax. These advantages stem from maintaining Jersey's international reputation as a low tax rate jurisdiction; its ability to attract workers with high incomes and, therefore, high contributions to the States tax revenues by the comparatively high levels of unearned (and, therefore, highly mobile) income that might leave the Island if the rate was raised substantially.

The Committee does not favour solely using changes to income tax to fund the £55 million deficit. Continued reliance on income tax would do nothing to diversify the Island's tax base, leaving it vulnerable to the damaging effects of possible future volatility in tax revenue streams.

All of the £55 million additional tax would be paid for by Island residents under the sole use of the income tax option, whereas with a GST the spending of visitors to the Island would also form part of the additional tax revenue collected.

Using just income tax also increases incentives for tax avoidance – whereas to diversify the tax base by introducing new taxes, such as GST, makes it more difficult for taxpayers to avoid paying tax.

Island income taxpayers would be subject to substantial reductions in their take-home income under both income tax options. For example, if the standard rate if income tax was to rise to 25% and income tax allowances were to be reduced by 25% the effect on typical households would be as follows –

- Example 1– single person household, no children, no mortgage, annual income of £30,000 – income tax would rise by **£780** per year.
- Example 2– married person, wife working, 2 children at school, mortgage £240,000, household income £60,000 – income tax would rise by £**1,835** per year.
- Example 3– married person, wife working, one child at school, one child at university, mortgage £360,000 (capped at £300,000), annual income £100,000 – income tax would rise by **£4,000** per year.
- Example 4– married old age pensioner couple, annual income of £20,000 – income tax would rise by **£1,300** per year.

For further examples see Appendix 2.

Conclusion

For the reasons stated, the Committee has decided not to rely solely on income tax changes to raise the additional £55 million. It does, however, believe that higher earners should contribute more in tax and proposes to withdraw income tax allowances and exemptions under its 20% means 20% proposals, as detailed earlier in this Report, to ultimately generate about £10 million.

CAPITAL GAINS TAX (CGT)

Capital Gains Tax (CGT) has also been considered by the Committee. There is no data on the capital gains currently enjoyed by the residents of Jersey but it is unlikely that a Capital Gains Tax applied to the gains of non-Jersey residents would be generate significant amounts of revenue. In the U.K., where personal capital gains are taxed, the tax yield is low – on average around £45 per person.[14] Given the higher average incomes on Jersey perhaps more per person would be realised if the same tax rates as the U.K. were applied. The Comptroller of Income Tax has estimated that a CGT could raise up to £5 million per year in Jersey. Such an amount, however would not remotely fill the fiscal deficit.

CGT also has a relatively high cost of collection. The U.K. statistics for 2002/03 show costs at 2.73p for every £1 collected. This is some 66% higher than the U.K. cost to collect £1 of Income tax [1.64p]. This figure is about double the cost of tax collection in Jersey [0.87p] and it is highly likely that the cost of start-up of CGT in Jersey would be very significantly higher than the current 0.87%.

CGT is also a tax where avoidance measures are common, not least because the sums at stake can be substantial

and those affected can afford expensive professional help. The quest for loopholes leads to remedial anti-avoidance action and what is already complex legislation becomes increasingly labyrinthine. This feeds back into the administrative and compliance cost burden mentioned above. The easiest of all gains to assess to CGT, that of the gain made on a principal private residence, would have to be excluded from the CGT charge to tax, as it is in the U.K., so what might be thought of by some as a major source of revenue, would not materialise. In addition, some believe that property developers make capital gains and escape tax on their gains. This is not correct. Property developers are engaged in a trade and pay income tax on their property development profits like every other trader. They would not be subjected to CGT on these gains as well.

Neither of Jersey's principal competitors (Guernsey/Isle of Man) tax capital gains. The Island's finance industry offers some products to avoid U.K. capital taxes – not just CGT but Inheritance Tax (IHT) too. Precise figures are not known but one must suspect that those shielding assets under Jersey companies to avoid U.K. CGT or IHT would not be enamoured of the idea of paying local Jersey CGT. This business would simply migrate and the loss would impact upon the revenues of local service providers. This issue could lead to an Income Tax take less than expected which would in turn serve to negate any new CGT yield.

The U.K. has seen quite a relaxation in CGT rules recently because many believe that it has acted as a discouragement to business expansion and entrepreurship. Fairly generous taper relief provisions have been introduced so that traders can invest in their business and enjoy the returns of growth without what were seen as punitive tax 'hits'. The U.K. has a range of reliefs to assist business but they themselves can be esoteric and complex to claim/administer. Even meeting the compliance burden for reliefs can be a disincentive.

The complexity of the legislation cannot be overlooked. For example, working out the CGT liability on share pools is really rather difficult. The Law Draftsman would have a great deal of work to do to emulate the U.K.'s CGT law. If it was only a watered down Jersey version then one would need to similarly dilute the expectations of CGT yield. Such a watered down version would offer ample scope for tax avoidance by professionals. There would also be a steep learning curve for all. Apart from a few tax professionals versed in some aspects of the U.K. CGT system there is no current expertise in the Island to build upon. Gains can arise on any of a complex, and evolving, range of financial instruments and rules have to exist to apply to each as funds can flow quickly to any area of perceived advantage.

The Committee is of the firm opinion that even contemplation of a Capital Gains Tax would significantly undermine the credibility of Jersey as a leading offshore financial centre.

WEALTH TAX

Wealth tax has also been considered by the Committee.

A wealth tax would be an uncertain and volatile source of revenue.

It would also send out a message totally contrary to the current Jersey philosophy of being a low tax rate jurisdiction. If a wealth tax was applied to Jersey residents such as existing and potential 1(1)(k)s, the majority, if not all, existing ones would leave, resulting in another reduction in direct tax revenues, and potential 1(1)(k)s, who may have been attracted to take up residence in Jersey, would be disinclined to do so. Other wealthy residents, not 1(1)(k)s, who would also be affected would seriously consider relocating elsewhere. So a wealth tax would almost certainly encourage mobility of capital and skills.

Quite apart from these important factors, there is the administrative and operational complexity of such a tax. It will be difficult to administer and there will be loopholes which will potentially allow quite easy avoidance of the tax. Trying to close down all such loopholes would result in a much more complex law and anti-avoidance provisions, all of which would come at quite a significant additional resource and staff cost.

For these reasons, the Committee has not commissioned (nor indeed was it charged to do so by the Assembly) the work that would need to be done to estimate what yield a wealth tax would generate.

TAXES AND INFLATION

Concerns have been expressed that GST will exacerbate the inflation problem in the Island. For the reasons set out in this Report, the application of either GST or an employer payroll tax is likely to result in prices higher than they would otherwise have been. This would be expected to be reflected in the RPI. The result is that Jersey residents will get slightly less goods and services for any given level of income.

The alternatives – of income tax or employee payroll tax – achieve exactly the same outcome (Jersey residents getting slightly less goods and services from their income) by *reducing* after-tax ('take-home') income. These taxes do not directly feed through into measured inflation (i.e. the RPI), but the effect on Jersey residents is the same.

In addition, if *any* of these tax changes result in increased wages to compensate for the loss of purchasing ability then there will be *additional* inflation. The economy will be given a wage-push kick to inflation, which will make Jersey even less internationally competitive and will, after a while, be likely to put the economy into a recession.

So all the main tax options will have the same general effect – reduce the purchasing power of Jersey residents: GST and employer payroll taxes by increasing prices; income tax and employee payroll taxes by reducing take-home pay. All of them have the ability to give wage-push inflation a kick, which would be very damaging to the economy.

However, all of them are better than doing nothing. Doing nothing results in a severe reduction in economic activity in the Island, a very large deficit which is unsustainable and, therefore, very large tax increases or severe reductions in government services a bit further down the line. (Although under these circumstances there is unlikely to be inflation – indeed, significant deflation, especially of house prices, is likely.)

What the Island must achieve is the introduction of the required tax changes (GST, income tax or payroll) without triggering wage-push inflation. This is not an easy task, but the Committee believes it is achievable and within this need to raise significantly more tax revenue from residents, **the Committee believes that the proposed combination of 20% means 20% and GST (with the income support system protecting the least well-off) is the best way to achieve this.**

THE NEXT STEPS

Following the lodging au Greffe of its Fiscal Strategy proposals the Committee will concentrate on explaining these proposals, and the reasons for them, to all the residents of Jersey. A thorough and detailed communications programme will be undertaken between March and May 2005 in order to explain in the clearest possible way why the Committee has reached its conclusions.

Following the Debate in the States on the Fiscal Strategy scheduled in May 2005, the Committee intends to implement these proposals as laid out in this Report and in the Implementation Plan of the Crown Agent's Final Report (Annex E).**However, this is not the end of the consultation and communication process. The Finance and Economics Committee will continue to consult with Island residents, businesses and stakeholder groups as the Fiscal Strategy proposals are developed and rolled-out over the coming weeks and years.**

Financial and manpower implications

The main tax measures proposed in this report will raise approximately £55 million a year.

Under the simple, broad-based GST system proposed, 10 additional staff would be needed to administer GST at a total cost, including overheads, of approximately £500,000 a year.

In addition, there would be one-off development and set up costs for GST in the order of £1 million.

The "20 means 20" proposals, the "look-through" arrangements and the additional anti-avoidance measures will be implemented within the Income Tax Departments existing staffing complement and budget.

The research into environmental taxes and a development gains tax will be funded from within existing budgets. It is not possible to quantify either the yield or administrative costs of such taxes until this research has been completed.

Supporting papers to include:

- ***'Which Tax is best suited to Jersey's objectives? An evaluation of alternative tax options' OXERA (February 2005)***

- ***'Economic consequences of the application of a selective tax' Oxera (February 2005)***

- ***'Proposal for the Design of a Prototype Goods and Services Tax' Crown Agent's Final Report (February 2005)***

- ***'General Guide to GST in the Form of Frequently Asked Questions' Crown Agents (February 2005)***

APPENDIX 1

Examples of the impact of the 20% means 20% proposals on typical households

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Single, no children, no mortgage	£12,000.00	£264.60	2.21%	£264.60	2.21%	£0.00	0.00%
Single, no children, no mortgage	£20,000.00	£2,424.60	12.12%	£2,424.60	12.12%	£0.00	0.00%
Single, no children, no mortgage	£30,000.00	£4,800.00	16.00%	£5,124.60	17.08%	£324.60	1.08%
Single, no children, no mortgage	£40,000.00	£6,800.00	17.00%	£7,824.60	19.56%	£1,024.60	2.56%
Single, no children, no mortgage	£50,000.00	£8,800.00	17.60%	£10,000.00	20.00%	£1,200.00	2.40%
Single, no children, no mortgage	£60,000.00	£10,800.00	18.00%	£12,000.00	20.00%	£1,200.00	2.00%
Single, no children, no mortgage	£70,000.00	£12,800.00	18.29%	£14,000.00	20.00%	£1,200.00	1.71%
Single, no children, no mortgage	£80,000.00	£14,800.00	18.50%	£16,000.00	20.00%	£1,200.00	1.50%
Single, no children, no mortgage	£90,000.00	£16,800.00	18.67%	£18,000.00	20.00%	£1,200.00	1.33%
Single, no children, no mortgage	£100,000.00	£18,800.00	18.80%	£20,000.00	20.00%	£1,200.00	1.20%
Single, no children, no mortgage	£110,000.00	£20,800.00	18.91%	£22,000.00	20.00%	£1,200.00	1.09%
Single, no children, no mortgage	£115,000.00	£21,800.00	18.96%	£23,000.00	20.00%	£1,200.00	1.04%
Single, no children, no mortgage	£120,000.00	£22,800.00	19.00%	£24,000.00	20.00%	£1,200.00	1.00%
Single, no children, no mortgage	£130,000.00	£24,800.00	19.08%	£26,000.00	20.00%	£1,200.00	0.92%
Single, 1 child at school, no mortgage	£30,000.00	£3,234.60	10.78%	£3,234.60	10.78%	£0.00	0.00%
Single, 1 child at school, no mortgage	£40,000.00	£5,400.00	13.50%	£5,934.60	14.84%	£534.60	1.34%
Single, 1 child at school, no mortgage	£50,000.00	£7,400.00	14.80%	£8,634.60	17.27%	£1,234.60	2.47%
Single, 1 child at school, no mortgage	£60,000.00	£9,400.00	15.67%	£11,334.60	18.89%	£1,934.60	3.22%
Single, 1 child at school, no mortgage	£70,000.00	£11,400.00	16.29%	£14,000.00	20.00%	£2,600.00	3.71%
Single, 1 child at school, no mortgage	£80,000.00	£13,400.00	16.75%	£16,000.00	20.00%	£2,600.00	3.25%
Single, 1 child at school, no mortgage	£90,000.00	£15,400.00	17.11%	£18,000.00	20.00%	£2,600.00	2.89%
Single, 1 child at school, no mortgage	£100,000.00	£17,400.00	17.40%	£20,000.00	20.00%	£2,600.00	2.60%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Single, 1 child at school, no mortgage	£110,000.00	£19,400.00	17.64%	£22,000.00	20.00%	£2,600.00	2.36%
Single, 1 child at school, no mortgage	£120,000.00	£21,400.00	17.83%	£24,000.00	20.00%	£2,600.00	2.17%
Single, 1 child at school, no mortgage	£130,000.00	£23,400.00	18.00%	£26,000.00	20.00%	£2,600.00	2.00%
Single, no children, mortgage £120,000	£30,000.00	£3,407.40	11.36%	£3,407.40	11.36%	£0.00	0.00%
Single, no children, mortgage £120,000	£40,000.00	£5,528.00	13.82%	£6,107.40	15.27%	£579.40	1.45%
Single, 1 child at school, mortgage £120,000	£30,000.00	£1,517.40	5.06%	£1,517.40	5.06%	£0.00	0.00%
Single, 1 child at school, mortgage £120,000	£40,000.00	£4,128.00	10.32%	£4,217.40	10.54%	£89.40	0.22%
Single, no children, mortgage £200,000	£50,000.00	£6,680.00	13.36%	£7,662.60	15.33%	£982.60	1.97%
Single, 1 child at school, mortgage £200,000	£50,000.00	£5,280.00	10.56%	£5,772.60	11.55%	£492.60	0.99%
Single, no children, mortgage £240,000	£60,000.00	£8,256.00	13.76%	£9,790.20	16.32%	£1,534.20	2.56%
Single, no children, mortgage £240,000	£70,000.00	£10,256.00	14.65%	£12,490.20	17.84%	£2,234.20	3.19%
Single, no children, mortgage £240,000	£80,000.00	£12,256.00	15.32%	£15,190.20	18.99%	£2,934.20	3.67%
Single, no children, mortgage £240,000	£90,000.00	£14,256.00	15.84%	£17,890.20	19.88%	£3,634.20	4.04%
Single, no children, mortgage £240,000	£100,000.00	£16,256.00	16.26%	£20,000.00	20.00%	£3,744.00	3.74%
Single, no children, mortgage £240,000	£110,000.00	£18,256.00	16.60%	£22,000.00	20.00%	£3,744.00	3.40%
Single, no children, mortgage £240,000	£120,000.00	£20,256.00	16.88%	£24,000.00	20.00%	£3,744.00	3.12%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Single, no children, mortgage £240,000	£130,000.00	£22,256.00	17.12%	£26,000.00	20.00%	£3,744.00	2.88%
Single, 1 child at school, mortgage £240,000	£60,000.00	£6,856.00	11.43%	£7,900.20	13.17%	£1,044.20	1.74%
Single, 1 child at school, mortgage £240,000	£70,000.00	£8,856.00	12.65%	£10,600.20	15.14%	£1,744.20	2.49%
Single, 1 child at school, mortgage £240,000	£80,000.00	£10,856.00	13.57%	£13,300.20	16.63%	£2,444.20	3.06%
Single, 1 child at school, mortgage £240,000	£90,000.00	£12,856.00	14.28%	£16,000.20	17.78%	£3,144.20	3.49%
Single, 1 child at school, mortgage £240,000	£100,000.00	£14,856.00	14.86%	£18,700.20	18.70%	£3,844.20	3.84%
Single, 1 child at school, mortgage £240,000	£110,000.00	£16,856.00	15.32%	£21,400.20	19.45%	£4,544.20	4.13%
Single, 1 child at school, mortgage £240,000	£120,000.00	£18,856.00	15.71%	£24,000.00	20.00%	£5,144.00	4.29%
Single, 1 child at school, mortgage £240,000	£130,000.00	£20,856.00	16.04%	£26,000.00	20.00%	£5,144.00	3.96%
Single, no children, mortgage £300,000	£115,000.00	£18,620.00	16.19%	£23,000.00	20.00%	£4,380.00	3.81%
Married, wife working, no children, no mortgage	£20,000.00	£0.00	0.00%	£0.00	0.00%	£0.00	0.00%
Married, wife working, no children, no mortgage	£30,000.00	£2,111.40	7.04%	£2,111.40	7.04%	£0.00	0.00%
Married, wife working, no children, no mortgage	£40,000.00	£4,811.40	12.03%	£4,811.40	12.03%	£0.00	0.00%
Married, wife working, no children, no mortgage	£50,000.00	£7,380.00	14.76%	£7,511.40	15.02%	£131.40	0.26%
Married, wife working, no children, no mortgage	£60,000.00	£9,380.00	15.63%	£10,211.40	17.02%	£831.40	1.39%
Married, wife working, no children, no mortgage	£70,000.00	£11,380.00	16.26%	£12,911.40	18.44%	£1,531.40	2.19%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Married, wife working, no children, no mortgage	£80,000.00	£13,380.00	16.73%	£15,611.40	19.51%	£2,231.40	2.79%
Married, wife working, no children, no mortgage	£90,000.00	£15,380.00	17.09%	£18,000.00	20.00%	£2,620.00	2.91%
Married, wife working, no children, no mortgage	£100,000.00	£17,380.00	17.38%	£20,000.00	20.00%	£2,620.00	2.62%
Married, wife working, no children, no mortgage	£110,000.00	£19,380.00	17.62%	£22,000.00	20.00%	£2,620.00	2.38%
Married, wife working, no children, no mortgage	£120,000.00	£21,380.00	17.82%	£24,000.00	20.00%	£2,620.00	2.18%
Married, wife working, no children, no mortgage	£130,000.00	£23,380.00	17.98%	£26,000.00	20.00%	£2,620.00	2.02%
Married, wife working, no children, no mortgage	£140,000.00	£25,380.00	18.13%	£28,000.00	20.00%	£2,620.00	1.87%
Married, wife working, no children, no mortgage	£150,000.00	£27,380.00	18.25%	£30,000.00	20.00%	£2,620.00	1.75%
Married, wife working, no children, no mortgage	£160,000.00	£29,380.00	18.36%	£32,000.00	20.00%	£2,620.00	1.64%
Married, wife working, no children, no mortgage	£170,000.00	£31,380.00	18.46%	£34,000.00	20.00%	£2,620.00	1.54%
Married, wife working, no children, no mortgage	£180,000.00	£33,380.00	18.54%	£36,000.00	20.00%	£2,620.00	1.46%
Married, wife working, 2 children at school, no mortgage	£50,000.00	£6,161.40	12.32%	£6,161.40	12.32%	£0.00	0.00%
Married, wife working, 2 children at school, no mortgage	£60,000.00	£8,380.00	13.97%	£8,861.40	14.77%	£481.40	0.80%
Married, wife working, 2 children at school, no mortgage	£70,000.00	£10,380.00	14.83%	£11,561.40	16.52%	£1,181.40	1.69%
Married, wife working, 2 children at school, no mortgage	£80,000.00	£12,380.00	15.48%	£14,261.40	17.83%	£1,881.40	2.35%
Married, wife working, 2 children at school, no mortgage	£90,000.00	£14,380.00	15.98%	£16,961.40	18.85%	£2,581.40	2.87%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Married, wife working, 2 children at school, no mortgage	£100,000.00	£16,380.00	16.38%	£19,661.40	19.66%	£3,281.40	3.28%
Married, wife working, 2 children at school, no mortgage	£110,000.00	£18,380.00	16.71%	£22,000.00	20.00%	£3,620.00	3.29%
Married, wife working, 2 children at school, no mortgage	£120,000.00	£20,380.00	16.98%	£24,000.00	20.00%	£3,620.00	3.02%
Married, wife working, 2 children at school, no mortgage	£130,000.00	£22,380.00	17.22%	£26,000.00	20.00%	£3,620.00	2.78%
Married, wife working, 2 children at school, no mortgage	£140,000.00	£24,380.00	17.41%	£28,000.00	20.00%	£3,620.00	2.59%
Married, wife working, 2 children at school, no mortgage	£150,000.00	£26,380.00	17.59%	£30,000.00	20.00%	£3,620.00	2.41%
Married, wife working, 2 children at school, no mortgage	£160,000.00	£28,380.00	17.74%	£32,000.00	20.00%	£3,620.00	2.26%
Married, wife working, 2 children at school, no mortgage	£170,000.00	£30,380.00	17.87%	£34,000.00	20.00%	£3,620.00	2.13%
Married, wife working, 2 children at school, no mortgage	£180,000.00	£32,380.00	17.99%	£36,000.00	20.00%	£3,620.00	2.01%
Married, wife not working, no children, no mortgage	£20,000.00	£626.40	3.13%	£626.40	3.13%	£0.00	0.00%
Married, wife not working, no children, no mortgage	£30,000.00	£3,326.40	11.09%	£3,326.40	11.09%	£0.00	0.00%
Married, wife not working, 1 child age 3, no mortgage	£30,000.00	£2,651.40	8.84%	£2,651.40	8.84%	£0.00	0.00%
Married, wife not working, no children, no mortgage	£40,000.00	£6,026.40	15.07%	£6,026.40	15.07%	£0.00	0.00%
Married, wife not working, 1 child age 3, no mortgage	£40,000.00	£5,351.40	13.38%	£5,351.40	13.38%	£0.00	0.00%
Married, wife not working, 1 child age 3, mortgage £160,000	£40,000.00	£3,061.80	7.65%	£3,061.80	7.65%	£0.00	0.00%
Married, wife working, no children, mortgage £200,000	£50,000.00	£4,649.40	9.30%	£4,649.40	9.30%	£0.00	0.00%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Married, wife working, 2 children at school, mortgage £200,000	£50,000.00	£3,299.40	6.60%	£3,299.40	6.60%	£0.00	0.00%
Married, wife working, 1 child at school, 1 child at university, mortgage £200,000	£50,000.00	£2,624.40	5.25%	£2,624.40	5.25%	£0.00	0.00%
Married, wife working, no children, mortgage £240,000	£60,000.00	£6,777.00	11.30%	£6,777.00	11.30%	£0.00	0.00%
Married, wife working, 2 children at school, mortgage £240,000	£60,000.00	£5,427.00	9.05%	£5,427.00	9.05%	£0.00	0.00%
Married, wife working, 1 child at school, 1 child at university, mortgage £240,000	£60,000.00	£4,752.00	7.92%	£4,752.00	7.92%	£0.00	0.00%
Married, wife working, no children, mortgage £240,000	£70,000.00	£8,836.00	12.62%	£9,477.00	13.54%	£641.00	0.92%
Married, wife working, 2 children at school, mortgage £240,000	£70,000.00	£7,836.00	11.19%	£8,127.00	11.61%	£291.00	0.42%
Married, wife working, 1 child at school, 1 child at university, mortgage £240,000	£70,000.00	£7,336.00	10.48%	£7,452.00	10.65%	£116.00	0.17%
Married, wife working, no children, mortgage £300,000	£80,000.00	£10,200.00	12.75%	£11,318.40	14.15%	£1,118.40	1.40%
Married, wife working, 2 children at school, mortgage £300,000	£80,000.00	£9,200.00	11.50%	£9,968.40	12.46%	£768.40	0.96%
Married, wife working, 1 child at school, 1 child at university, mortgage £300,000	£80,000.00	£8,700.00	10.88%	£9,293.40	11.62%	£593.40	0.74%
Married, wife working, no children, no mortgage	£85,000.00	£14,380.00	16.92%	£16,961.40	19.95%	£2,581.40	3.04%
Married, wife not working, 2 children at school, no mortgage	£85,000.00	£14,280.00	16.80%	£16,826.40	19.80%	£2,546.40	3.00%
Married, wife working, 2 children at school, no mortgage	£85,000.00	£13,380.00	15.74%	£15,611.40	18.37%	£2,231.40	2.63%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Married, wife working, 1 child at school, 1 child at university, mortgage £340,000 (capped at £300,000)	£85,000.00	£9,700.00	11.41%	£10,643.40	12.52%	£943.40	1.11%
Married, wife working, no children, mortgage £340,000 (capped at £300,000)	£85,000.00	£11,200.00	13.18%	£12,668.40	14.90%	£1,468.40	1.73%
Married, wife working, 2 children at school, mortgage £340,000 (capped at £300,000)	£85,000.00	£10,200.00	12.00%	£11,318.40	13.32%	£1,118.40	1.32%
Married, wife working, no children, mortgage £360,000 (capped at £300,000)	£90,000.00	£12,200.00	13.56%	£14,018.40	15.58%	£1,818.40	2.02%
Married, wife working, 2 children at school, mortgage £360,000 (capped at £300,000)	£90,000.00	£11,200.00	12.44%	£12,668.40	14.08%	£1,468.40	1.63%
Married, wife working, 1 child at school, 1 child at university, mortgage £360,000 (capped at £300,000)	£90,000.00	£10,700.00	11.89%	£11,993.40	13.33%	£1,293.40	1.44%
Married, wife working, no children, mortgage £360,000 (capped at £300,000)	£100,000.00	£14,200.00	14.20%	£16,718.40	16.72%	£2,518.40	2.52%
Married, wife working, 2 children at school, mortgage £360,000 (capped at £300,000)	£100,000.00	£13,200.00	13.20%	£15,368.40	15.37%	£2,168.40	2.17%
Married, wife working, 1 child at school, 1 child at university, mortgage £360,000 (capped at £300,000)	£100,000.00	£12,700.00	12.70%	£14,693.40	14.69%	£1,993.40	1.99%
Married, wife working, no children, mortgage £360,000 (capped at £300,000)	£110,000.00	£16,200.00	14.73%	£19,418.40	17.65%	£3,218.40	2.93%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Married, wife working, 2 children at school, mortgage £360,000 (capped at £300,000)	£110,000.00	£15,200.00	13.82%	£18,068.40	16.43%	£2,868.40	2.61%
Married, wife working, 1 child at school, 1 child at university, mortgage £360,000 (capped at £300,000)	£110,000.00	£14,700.00	13.36%	£17,393.40	15.81%	£2,693.40	2.45%
Married, wife working, no children, mortgage £360,000 (capped at £300,000)	£120,000.00	£18,200.00	15.17%	£22,118.40	18.43%	£3,918.40	3.27%
Married, wife working, 2 children at school, mortgage £360,000 (capped at £300,000)	£120,000.00	£17,200.00	14.33%	£20,768.40	17.31%	£3,568.40	2.97%
Married, wife working, 1 child at school, 1 child at university, mortgage £360,000 (capped at £300,000)	£120,000.00	£16,700.00	13.92%	£20,093.40	16.74%	£3,393.40	2.83%
Married, wife working, no children, mortgage £360,000 (capped at £300,000)	£130,000.00	£20,200.00	15.54%	£24,818.40	19.09%	£4,618.40	3.55%
Married, wife working, 2 children at school, mortgage £360,000 (capped at £300,000)	£130,000.00	£19,200.00	14.77%	£23,468.40	18.05%	£4,268.40	3.28%
Married, wife working, 1 child at school, 1 child at university, mortgage £360,000 (capped at £300,000)	£130,000.00	£18,700.00	14.38%	£22,793.40	17.53%	£4,093.40	3.15%
Married, wife working, no children, mortgage £400,000 (capped at £300,000)	£140,000.00	£22,200.00	15.86%	£27,518.40	19.66%	£5,318.40	3.80%
Married, wife working, 2 children at school, mortgage £400,000 (capped at £300,000)	£140,000.00	£21,200.00	15.14%	£26,168.40	18.69%	£4,968.40	3.55%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Married, wife working, 1 child at school, 1 child at university, mortgage £400,000 (capped at £300,000)	£140,000.00	£20,700.00	14.79%	£25,493.40	18.21%	£4,793.40	3.42%
Married, wife working, no children, mortgage £400,000 (capped at £300,000)	£150,000.00	£24,200.00	16.13%	£30,000.00	20.00%	£5,800.00	3.87%
Married, wife working, 2 children at school, mortgage £400,000 (capped at £300,000)	£150,000.00	£23,200.00	15.47%	£28,868.40	19.25%	£5,668.40	3.78%
Married, wife working, 1 child at school, 1 child at university, mortgage £400,000 (capped at £300,000)	£150,000.00	£22,700.00	15.13%	£28,193.40	18.80%	£5,493.40	3.66%
Married, wife working, no children, mortgage £400,000 (capped at £300,000)	£160,000.00	£26,200.00	16.38%	£32,000.00	20.00%	£5,800.00	3.63%
Married, wife working, 2 children at school, mortgage £400,000 (capped at £300,000)	£160,000.00	£25,200.00	15.75%	£31,568.40	19.73%	£6,368.40	3.98%
Married, wife working, 1 child at school, 1 child at university, mortgage £400,000 (capped at £300,000)	£160,000.00	£24,700.00	15.44%	£30,893.40	19.31%	£6,193.40	3.87%
Married, wife working, no children, mortgage £400,000 (capped at £300,000)	£170,000.00	£28,200.00	16.59%	£34,000.00	20.00%	£5,800.00	3.41%
Married, wife working, 2 children at school, mortgage £400,000 (capped at £300,000)	£170,000.00	£27,200.00	16.00%	£34,000.00	20.00%	£6,800.00	4.00%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Married, wife working, 1 child at school, 1 child at university, mortgage £400,000 (capped at £300,000)	£170,000.00	£26,700.00	15.71%	£33,593.40	19.76%	£6,893.40	4.05%
Married, wife working, no children, mortgage £400,000 (capped at £300,000)	£180,000.00	£30,200.00	16.78%	£36,000.00	20.00%	£5,800.00	3.22%
Married, wife working, 2 children at school, mortgage £400,000 (capped at £300,000)	£180,000.00	£29,200.00	16.22%	£36,000.00	20.00%	£6,800.00	3.78%
Married, wife working, 1 child at school, 1 child at university, mortgage £400,000 (capped at £300,000)	£180,000.00	£28,700.00	15.94%	£36,000.00	20.00%	£7,300.00	4.06%
Single, no children, mortgage £120,000, Life Assurance Premiums £1000	£30,000.00	£3,407.40	11.36%	£3,407.40	11.36%	£0.00	0.00%
Single, 1 child at school, mortgage £240,000, Life Assurance Premiums £1000	£60,000.00	£6,656.00	11.09%	£7,900.20	13.17%	£1,244.20	2.07%
Single, no children, mortgage £240,000, Life Assurance Premiums £5000	£90,000.00	£13,256.00	14.73%	£17,890.20	19.88%	£4,634.20	5.15%
Married, wife working, 2 children at school, mortgage £200,000, Life Assurance Premiums £1000	£50,000.00	£3,299.40	6.60%	£3,299.40	6.60%	£0.00	0.00%
Married, wife working, no children, mortgage £360,000 (capped at £300,000), Life Assurance Premiums £5000	£90,000.00	£11,200.00	12.44%	£14,018.40	15.58%	£2,818.40	3.13%

Description of Household	Household Income	Total Tax due in 2004	Effective rate (please see notes for explanation)	Tax due after full implementation of '20% means 20%'	Effective rate after full implementation of '20% means 20%' (from 2011)	Increase in Tax Paid	Increase in effective rate
Married, wife working, 2 children at school, mortgage £360,000 (capped at £300,000), Life Assurance Premiums £5000	£90,000.00	£10,200.00	11.33%	£12,668.40	14.08%	£2,468.40	2.74%
Married, wife working, 2 children at school, mortgage £400,000 (capped at £300,000), Life Assurance Premiums £10,000	£170,000.00	£25,200.00	14.82%	£34,000.00	20.00%	£8,800.00	5.18%
Single OAP (63 for the whole year)	£12,000.00	£0.00	0.00%	£0.00	0.00%	£0.00	0.00%
Single OAP (63 for the whole year)	£20,000.00	£2,079.00	10.40%	£2,079.00	10.40%	£0.00	0.00%
Single OAP (63 for the whole year)	£35,000.00	£5,800.00	16.57%	£6,129.00	17.51%	£329.00	0.94%
Married OAP (63 for the whole year)	£20,000.00	£0.00	0.00%	£0.00	0.00%	£0.00	0.00%
Married OAP (63 for the whole year), wife has pension by virtue of her own contributions	£30,000.00	£1,417.50	4.73%	£1,417.50	4.73%	£0.00	0.00%
Married OAP (63 for the whole year), wife has pension by virtue of her own contributions	£45,000.00	£5,467.50	12.15%	£5,467.50	12.15%	£0.00	0.00%

Notes: Where examples for single parents are given the calculations assume additional personal allowance is due. Where wife working this assumes income over £4500.
Where child allowance given this assumes any income in the child's own right does not exceed £2500.
Allowable Mortgage interest calculated at 5.3%.
The effective rate is the percentage of your income you pay in tax.
All OAP calculations assume no children and no mortgage.

APPENDIX 2

Examples of the impact of the Income Tax Option on typical households (standard rate of 25% and 25% reduction in personal allowances and exemptions)

Description of Household	Household Income	Total Tax due in 2004	£ increase under income tax only	Total tax paid following income tax changes
Single, no children, no mortgage	£12,000.00	£264.60	£743.85	£1,008.45
Single, no children, no mortgage	£20,000.00	£2,424.60	£743.85	£3,168.45
Single, no children, no mortgage	£30,000.00	£4,800.00	£1,068.45	£5,868.45
Single, no children, mortgage £120,000	£30,000.00	£3,407.40	£743.85	£4,151.25
Single, 1 child at school, mortgage £120,000	£30,000.00	£1,517.40	£1,216.35	£2,733.75
Single, 1 child at school, no mortgage	£30,000.00	£3,234.60	£1,216.35	£4,450.95
Single, no children, mortgage £120,000	£40,000.00	£5,528.00	£1,323.25	£6,851.25
Single, 1 child at school, mortgage £120,000	£40,000.00	£4,128.00	£1,305.75	£5,433.75
Single, 1 child at school, no mortgage	£40,000.00	£5,400.00	£1,750.95	£7,150.95
Single, no children, mortgage £200,000	£50,000.00	£6,680.00	£1,726.45	£8,406.45
Single, 1 child at school, mortgage £200,000	£50,000.00	£5,280.00	£1,708.95	£6,988.95
Single, 1 child at school, no mortgage	£50,000.00	£7,400.00	£2,450.95	£9,850.95
Single, no children, no mortgage	£60,000.00	£10,800.00	£3,075.00	£13,875.00
Single, no children, mortgage £240,000	£60,000.00	£8,256.00	£2,278.05	£10,534.05
Single, 1 child at school, mortgage £240,000	£60,000.00	£6,856.00	£2,260.55	£9,116.55
Single, 1 child at school, no mortgage	£60,000.00	£9,400.00	£3,150.95	£12,550.95
Single, no children, no mortgage	£70,000.00	£12,800.00	£3,575.00	£16,375.00
Single, no children, mortgage £240,000	£70,000.00	£10,256.00	£2,939.00	£13,195.00
Single, 1 child at school, mortgage £240,000	£70,000.00	£8,856.00	£2,960.55	£11,816.55
Single, 1 child at school, no mortgage	£70,000.00	£11,400.00	£3,662.50	£15,062.50
Single, no children, no mortgage	£80,000.00	£14,800.00	£4,075.00	£18,875.00
Single, no children, mortgage £240,000	£80,000.00	£12,256.00	£3,439.00	£15,695.00
Single, 1 child at school, mortgage £240,000	£80,000.00	£10,856.00	£3,526.50	£14,382.50
Single, 1 child at school, no mortgage	£80,000.00	£13,400.00	£4,162.50	£17,562.50

Description
Single, no ch
Single, no ch
Single, 1 chi £240,000
Single, 1 chi
Single, no ch
Single, no ch
Single, 1 chi £240,000
Single, 1 chi
Single, no ch
Single, no ch
Single, 1 chi £240,000
Single, 1 chi
Single, no ch
Single, no ch
Single, no ch
Single, no ch
Single, 1 chi £240,000
Single, 1 chi
Single, no ch
Single, no ch
Single, 1 chi £240,000
Single, 1 chi
Married, wi mortgage
Married, wi mortgage
Married, wi

mortgage
Married, wi
mortgage

[1] *Some £10-£12 million of this tax revenue will disappear before 2008 in any case, as a result of location decisions which are not related to the move to 0/10%. Therefore, only £10-£12 million of the reduction in tax revenues from this category of company can be attributed to the move to 0/10%. However, the loss of tax is real, so must still be made up by alternative means.*

[2] *A payroll tax on employers will immediately raise the wage costs for the States. Hence the total amount raised by a payroll tax has to be higher than using other taxes, so as to raise a net amount of £55 million after taking into account the higher wage costs incurred by the States.*

[3] *The Committee did consider only raising the standard rate of income tax from 20% to 25% (and the marginal rate from 27% to 32%), however this only yields around £37 million. Also, introducing a higher rate of income tax for those on higher incomes does not raise significant sums of revenue. For example, if a higher rate of income tax was levied on taxable household income over £80,000 it would be likely to raise slightly more than £1 million per annum per one per cent point. So a higher rate of 40% is required to get the total up to £55 million. Because so many people are outside the tax system due to the high level of personal income tax allowances and exemptions the only realistic method of raising the £55 million through the income tax option without very high top rates of tax is to significantly reduce these allowances and exemptions. With the standard rate of tax set at 25% (and the marginal rate left at 27%) a 25% reduction in personal allowances and exemptions raises an additional £35 million.*

[4] *See Section 3 for an example of this effect.*

[5] *'Proposal for the Design of a Prototype Goods and Services Tax' Crown Agents Final Report (January 2005).*

[6] *'Proposal For The Design Of A Prototype Goods And Services Tax – Final Report' Crown Agents (January 2005).*

[7] *'General Guide to GST in the Form of Frequently Asked Questions' Crown Agents (February 2005).*

[8] *For a detailed analysis refer to the OXERA paper 'Economic Consequences of the Application of a Selective Tax' (February 2005) which is published with this Report.*

[9] *'Which tax is best suited to Jersey's objectives?' Appendix 1 (February 2005).*

[10] *'Which tax is best suited to Jersey's objectives', Appendix 2 (February 2005).*

[11] *Barker, K., 'Review of Housing Supply. Delivering Stability: Securing our Future Housing Needs', ODPM. HMSO March 2004.*

[12] *The £45 million arises from the following: removing the social security ceiling (currently around£34,000) raises about £10 million from employees and£11 million from employers: the additional one per cent over the entire income base raises about £12 million from employers and the same from employees.*

[13] *An extensive list of examples of how income tax changes may affect typical households is shown in Appendix 2.*

[14] *£2,225 million in 2003-04, personal capital gains tax. Source – Inland Revenue, Table T1.2, http://www.inlandrevenue.gov.uk/stats/tax receipts/table1-2.pdf*