INCOME TAX: INCREASE IN SMALL INCOME EXEMPTION LIMITS AND ALLOWANCES, AND INTRODUCTION OF HIGHER RATE

Lodged au Greffe on 19th November 2002
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STATES OF JERSEY

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PROPOSITION

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

(a) to agree, in principle, that -

(i) the small income exemption limits and personal allowances for income tax purposes should be raised in the Budget 2004 by an amount equivalent to the rise in the Jersey Retail Prices Index as at September 2003;

(ii) a higher rate of income tax should be set on income over £100,000 for those taxpayers whose net income after allowances, exemptions and reliefs exceeds that sum, to compensate in full for the shortfall in income tax receipts caused by the proposals in sub-paragraph (i) above;

(b) to charge the Finance and Economics Committee to bring forward the necessary legislation to give effect to these proposals as part of its Budget 2004 proposals.

DEPUTY G.P.SOUTHERN OF ST. HELIER

Note: The Finance and Economics Committee's comments are to follow.

Report

The report into the future of Jersey's tax and spending policies presented to the Finance and Economics Committee in May 2002 by the Committee's financial advisors OXERA, clearly identifies several means of generating additional income to meet our current and projected deficits in Chapter 7 'Addressing the problem on the income side'. In concluding this chapter, the authors are equally clear when they say -

> *"…there are many ways in which the additional tax burden could fall, both within the large structure (neutral, progressive or regressive, etc.) and relatively advantaging (or disadvantaging) particular groups. The limits at which tax avoidance would become a serious consideration do not seem to be approached, at least within the range of generating £50 million per annum of tax revenues. Thus, within quite large limits, the choice of large-scale structure of the tax burden seems to be largely political, not economic."*

The chapter starts by pointing out that a priority for tax policy is to raise an appropriate amount of revenue as efficiently and equitably as possible. The two equity principles that are commonly applied to tax policy are -

The user pays (or benefit) principle
The ability-to-pay principle

The authors point out that only under the latter principle can the social goal of helping those with less material wealth and fortune be met without the need for large-scale reform of the benefit system. In this decade of the eradication of poverty, this is a significant point.

In discussing the distributional aspects of an increased tax burden, the report outlines the main dimension, as follows:

Progressive tax - raised largely from the relatively well-off
Neutral progressive - all taxpayers subject to the same percentage in their existing tax bill
Neutral regressive - all taxpayers subject to the same percentage point increase in their effective tax rate
Regressive - each earner is subject to the same actual increase

In addition they point out that "in general, tax structures operate to increase the tax contributions in both the absolute amounts and as a proportion of income as income rises (i.e. tax rates increase as personal income rises). This is the norm in most jurisdictions.

Jersey, on the other hand, has a single tax rate of 20% no matter how large one's personal income is. Its progressive nature is the result of the use of small income exemptions and the use of the 27% marginal (or entry) rate.

In all the discussion of what we might do to clear the current and projected deficits generated by our tax and spending policies, the possibility of progressive measures has been largely ignored.

The measures outlined in this budget, and the many of the possibilities that are under consideration, are largely regressive in their effects.

The rise in impôt duties - clearly regressive in terms of tobacco and alcohol duty, in that spending on these items will constitute a greater proportion of the budget of those who are the least well off. Additional duty on petrol will increase transport costs and (in all probability) inflation, which will hurt those least able to afford it.

Freezing income tax exemptions and allowances- this is clearly a regressive measure designed to bring a new tranche of the relatively low paid into taxation. It affects those on low to middle incomes far more that those who are better off. Malcolm Campbell, the Comptroller of Income Tax, estimates that the freezing of income tax exemptions and allowances over the past two years has raised an extra £10 million in revenue. Of this, £8 million has been from those on marginal rate i.e., those on lower incomes. He estimates that freezing income tax exemptions and allowances again in 2003 will generate an extra £5 million. Again, most of this will come from those who have lower incomes.

We have seen some aspects of a progressive nature applied to recent moves to generate additional income from changes to stamp duty and vehicle registration duty (VRD). I believe that there has been little opposition to these measures because of the progressive elements.

The only viable alternative to progressive tax changes that has been discussed so far is the introduction of some form of sales tax. This is also a regressive tax, which would most hurt those who currently do not earn enough to pay tax, the poorest on the island. OXERA's advice is that, whatever form this indirect tax takes, an extra £10 - £15 million in some form of benefi would need to be redirected to the poorest if they were not to be further impoverished.

I believe that we have to consider progressive taxation measures to solve our long-term problems in generating sufficient revenue to meet our needs. They will not be the only solution, but they must form part of the solution. In the short term, I believe we cannot continue to increase the burden on those who are less well off at the expense of the better off. This is the inevitable consequence of freezing income tax exemptions and allowances for another year. This proposal does not propose a cut in revenue, but a redistribution of the tax burden. In order to raise the £5 million required to compensate for the uprating of income tax exemptions and allowances, my calculations, which agree with those of the Comptroller of Income Tax, which agree with those of the Comptroller of Income Tax, indicate that a new rate of 23% needs to be levied on incomes over £100,000.

According to OXERA, there were some 200 households with personal annual incomes over £250,000, and fewer than 100 with personal annual incomes over £500,000. In discussing the possibility that some of these households might simply leave the island, the OXERA report admits that there is no precise data on the potential mobility of Jersey residents, but suggests that the relatively rich will be the most mobile. They point out, however, that even under a scenario of much larger tax rise (up to 39% on incomes over £100k), a household on £120,000 annual income would still be almost £10,000 better off than in the U.K. Under these proposals, a household on £120,000 income would pay an additional £600 in income tax.

This proposition asks for an 'in principle' agreement to these proposals. The exact financial and manpower implications, if any, will be known when detailed proposals are brought forward.