# STATES OF JERSEY

# PROPOSED GOVERNMENT PLAN 2023-2026 (P.97/2022): TWENTY-THIRD AMENDMENT (P.97/2022 AMD.(23)) – COMMENTS

# REMOVING THE UPPER EARNINGS CAPS

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**Presented to the States on 8th December 2022**
**by the Council of Ministers**

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**STATES GREFFE**

## COMMENTS

**Summary**

This amendment proposes to remove the Upper Earnings Limit on Social Security and Long-Term Care Contributions. This proposal:

a) Goes against the advice of the Fiscal Policy Panel to consider the future funding of the Social Security Fund after the actuarial reviews are published in 2023;

b) Would pose a significant risk to Jersey's international competitiveness, particularly for the financial and legal services sectors;

c) Would be likely to raise less income than estimated if businesses and individuals take steps to avoid the additional charges, possibly leading to a loss of revenue if they chose to leave Jersey; and

d) Would increase the cost of doing business at a time of economic uncertainty, increasing the overall tax burden without identifying any need for raising this additional income.

The Council of Ministers opposes this proposal and asks the Assembly to reject this amendment.

Following the publication of the actuarial reviews of the Social Security Fund and the Long-Term Care Fund in the first half of 2023, the government will consider whether any action is needed to maintain the Funds for future generations or to raise funding to support any other areas.

**Background**
**Social Security Fund**

1. Until the late 1990s, the Social Security scheme was run based on a pay as you go system - the contributions collected each year were designed to meet the cost of benefits paid in that year. The scheme included a maximum standard earnings level (SEL) for contributions. The Social Security Fund ("the Fund") received income from employers, employees, and the government in roughly equal shares.

2. In the late 1990s contribution rates were increased to build up the Fund to support the population bulge of pensioners that would arrive in a few decades. This policy has worked well, and the Fund now holds a large reserve. Until 2012 no contributions were levied above the SEL.

3. A Fiscal Strategy Review was undertaken in 2010. This identified the need for more government revenue and led to an increase in GST from 3% to 5% and the introduction of contributions above the SEL for the first time, levied on employers and Class 2 individuals (mainly self-employed individuals but also including non-working people below pension age).

4. In 2012 a new upper earnings limit (UEL) was introduced at £150,000 per year. The contribution rate between the SEL and the UEL was set at 2%. The extra contributions received from employers and Class 2 individuals were used to reduce

the level of the States Grant into the Fund, releasing funding for general government expenditure. This provided an additional £7M per annum to support public spending requirements.

**Long Term Care Fund**

5. The Social Security scheme and the Long-Term Care (LTC) scheme share a common Upper Earnings Limit. However, the operation of the two schemes is quite different.

6. The LTC scheme was introduced in 2014 to support the increasing costs of long-term care within an ageing population. The LTC Fund receives income from Jersey residents who pay income tax and an annual grant from the government. Individual contributions are levied at a headline rate of 1.5% on taxable income up to the UEL.

7. The level of the long-term care contribution is discounted for most taxpayers in the same way as marginal rates apply to income tax liability. For example, an individual who has an effective tax rate of 10% (half of the headline rate of 20%) will pay an LTC contribution at 0.75% (half of the headline rate of 1.5%). Only standard rate taxpayers (about 10% of all taxpayers) pay the maximum 1.5% rate.

8. The SEL and UEL are increased automatically each year in line with the earnings index.

**Current situation**

9. In 2019, the States agreed to increase the Upper Earnings Limit (UEL) in 2020 from £176,232 to £250,000 a year and to increase the Social Security contribution rate at this level from 2% to 2.5%. This represented an increase of more than 40% in the UEL and doubled the maximum social security contribution paid above the Standard Earnings Limit (SEL) to nearly £5,000 a year. The income from these additional contributions supported the cost of the expansion of contributory parental benefits.

10. Disruption in overall business activity due to the Coronavirus pandemic means it is not yet possible fully to evaluate the impact of increasing the UEL and contribution rate on the Fund. Due to the Coronavirus pandemic in 2020 and 2021, and the increased cost of living this year, the main contribution rates were temporarily reduced by 2 percentage points at various times since this change was implemented. To make further changes before the impact of the 2020 increase becomes clear would conflict with the principle of evidenced-based policy making.

11. The report to the amendment suggests that there are ongoing payments being made from the Fund as part of the cost-of-living measures. This is not correct: direct payments are being made from tax funded budgets and not from ring fenced funds. The temporary reduction in income into the Fund for the last quarter of 2022 has been fully budgeted for and does not create any ongoing pressure on the sustainability of the Fund.

12. Actuarial reviews of the Social Security and Long-Term Care Funds will be published in 2023. Any decision to adjust contribution rates or limits should only be taken after those reviews are complete.

**2023 contributions**

13. The UEL is currently £21,724 per month (£260,688 a year) and is due to increase to £23,072 per month (£276,864 a year) on 1 January 2023 in line with the increase in average earnings during 2022.

14. In 2023, the UEL will have increased by more than 10% since it was set at the new higher level of £250,000 in 2020. It is therefore inaccurate to suggest that there is no increase in the amount of money going into the Social Security Fund.

Summary of Social Security rates and maximum annual contributions as at 1/1/23

| | Charged from | Charged to | Employee | | Employer | | Class 2 | |
|---|---|---|---|---|---|---|---|---|
| | | | % rate | Max contribution | % rate | Max contribution | % rate | Max contribution |
| **SEL** | £0 | £ 60,720 | 6% | £ 3,643 | 6.5% | £ 3,947 | 12.5% | £ 7,590 |
| **UEL** | £60,720 | £ 276,864 | - | £ - | 2.5% | £ 5,404 | 2.5% | £ 5,404 |
| **Total maximum contribn.** | | | | £ 3,643 | | £ 9,350 | | £ 12,994 |

15. A UEL of £276,864 will see those making maximum Class 2 contributions contributing £1,080 each month in 2023 (£12,994 a year). Employers of high earning employees will pay £9,350 for the year.

16. Separately, a UEL of £276,864 will see individuals (employed or self-employed) making a maximum LTC contribution of £4,153 pa.

17. The annual increase to the UEL in line with average earnings is enshrined in legislation and ensures that these contributions increase in value each year.

**Proposed change – Government Plan Amendment**

18. This proposal would remove the monthly UEL on Social Security contributions and Long-Term Care (LTC) contributions before the end of 2023.[1]

19. This amendment would require:

- Employers to pay an extra 2.5% Social Security contributions on employees' earnings above £276,864
- Self-employed and other Class 2 people below the pension age to pay an extra 2.5% Social Security contributions on income exceeding £276,864
- Class 2 contribution payers on the high value residency scheme below the pension age to pay an extra 2.5% Social Security contributions on income above £276,864.

20. The proposed amendment to Social Security contributions will only impact those who pay Class 2 contributions and employers. Employees pay Social Security (Class 1) contributions up to the Standard Earnings Limit of £60,720 (2023 level). No contributions are levied on income above this level

[1] While no implementation date is provided in the report to the amendment, the amended Proposition refers to the balances of the Funds being increased "by the end of 2023".

21. This amendment would also require individuals with incomes above £276,864, including high value residents, to pay an extra 1.5% LTC contributions on their income above the UEL.

**Fiscal Policy Panel**

22. In its 2022 Annual Report the Fiscal Policy Panel advised that high and continued inflation should not be seen as a reason for increased taxes.[2] Although there are some tax rises in the proposed Government Plan, these are targeted and designed to drive behavioural changes, thus following the Panel's advice. With inflation at the highest level since the early 1990s, this amendment contradicts their recommendation that this is not the time for significant fiscal consolidation.

**International competitiveness**

23. This proposal has the potential to significantly reduce Jersey's international competitiveness. Financial and legal services comprise almost two-fifths of Jersey's economy, with each full-time employee in the financial services sector amounting to over £145,000 by Gross Added Value.

24. Elements such as cost and ease of doing business are critical to the perception of Jersey's competitiveness, particularly during the current economic climate. The importance of support for businesses was stressed in stakeholder submissions, and the Corporate Services Scrutiny Panel's final report on the recent Mini-Budget.

25. The most affected businesses could limit their activity or even leave Jersey, resulting in a significant reduction in not only the Social Security and LTC contributions received, but also the income tax and GST that these businesses pay.

26. Any measure that would make Jersey less attractive must be carefully considered; this amendment would make it less likely that Jersey could continue to appeal to the highly skilled and successful individuals who make a valuable contribution to our society and economy.

**Estimated income from the proposal**

27. The estimates of income provided apply the proposed changes to a snapshot of taxpayer earnings and incomes from 2020. It does not take in to account any changes in behaviour that could take place to minimise the impact of the proposal themselves.

28. The estimated income of £7m from Social Security contributions depends on approximately 600 employed and self-employed people, including Islanders on the high value residency scheme.

29. The estimated income of £6.5m from LTC contributions depends on approximately 920 individuals.

[2] FPP 2022 Annual Report.pdf (gov.je), p.39

30. It is very likely that some of these people will change their financial arrangements to avoid paying the significant extra contributions.

**Sustainability of the Social Security and Long-Term Care Funds**

31. As stated in the Government Plan 2023-2026, the Social Security Fund is still forecast to hold four times annual spend by the 2070s. From 2024, the annual States Grant payment into the Social Security Fund will be reinstated at its full value. There is no indication that any action is needed, particularly in advance of the actuarial review, in order to address the sustainability of these Funds.

32. The Long-Term Care Fund will also be subject to an actuarial review. The current rate of contribution is sufficient to maintain the Fund throughout the period of the Government Plan. The report to the amendment suggests that the removal of the UEL in respect of the Long-Term Care Fund would protect low and middle earners from an increase in the LTC rate. As stated above, for around 90% of taxpayers, LTC contributions are paid at a lower, marginal rate. Lower and middle earners are therefore protected under the existing system with an effective rate of LTC contribution below the headline 1.5% rate. People earning below the income tax threshold do not pay LTC contributions.

33. The maximum income that might be achieved from the removal of the UEL in this proposal is estimated at £6.5 million. As noted above, the actual income received is like to be variable from year to year and could be considerably below the estimate based on current taxpayers. The need to increase LTC rates will not be removed by the provision of this additional income. As the report notes, LTC rates have been forecast to need to rise to 3% over time as the number of people needing care increases as a proportion of the population. A 1-percentage point increase in the LTC rate would produce additional income of approximately £20 million and this is the scale of the future challenge.

**Conclusion**

34. The decision to raise additional income at this difficult time from local businesses and residents should be clearly linked to a need for government spending in a specific area. The amendment makes no attempt to identify the need for this additional burden. As such, it should be rejected as premature.

35. It is also premature for the Assembly to decide now on one specific revenue raising option, clearly identified as a political manifesto commitment, without a full understanding of the impact of the change and in advance of the publication of detailed information on the state of the Funds.

36. Following the publication of the actuarial reviews of the Social Security Fund and the Long-Term Care Fund in the first half of 2023, the government will consider whether any action is needed to maintain the Funds for future generations or to raise funding to support any other areas.

37. This amendment focuses solely on the removal of the UEL.

38. If the need for additional funding is identified in the future, other options for increasing income in respect of the SSF include:

- increasing the contribution rate up to the UEL from 2.5% to a higher rate
- extending the contribution rate up to the UEL to include higher earning employees as well as employers and Class 2 individuals
- making broader changes to the SEL and UEL levels and rates to maintain the sustainability of the Fund.

39. These options will be considered once the actuarial reviews have been published.

40. Members are strongly urged to reject the proposition and to allow the Council of Ministers to proceed with the planned actuarial reviews