STATES OF JERSEY

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INCOME TAX: ADDITIONAL LIABILITY

Lodged au Greffe on 20th April 2005
by Deputy G.P. Southern of St. Helier

STATES GREFFE

PROPOSITION

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

(a) to agree that the Income Tax (Jersey) Law 1961 should be amended to provide for the charging of an additional charge of income tax for a year of assessment, at the rate specified below, upon the amount of a person's liability to tax for that year as follows –

(1) for the year of assessment 2006, 0.87%;
(2) for the year of assessment 2007, 1.75%; and
(3) for the year of assessment 2008 and ensuing years, 2.65%.";

(b) to charge the Finance and Economics Committee to bring forward for approval the necessary legislation to give effect to the proposal.

DEPUTY G.P. SOUTHERN OF ST. HELIER

REPORT

20% means 20%

There can be no doubt that the fiscal measures taken in response to EU/ECOFIN directives concerning harmful tax practices will have the most far reaching and dramatic effects on the island's fiscal structure for many decades. In particular, the zero/ten proposals have resulted in two major measures that give particular concern to both members and Islanders –

The introduction of a Goods and Services Tax (GST), and
The phasing out of allowances (20% means 20%).

I am very concerned about the introduction of the 20% means 20% on a number of grounds –

In concentrating on a small sector of middle to high earners, these measures produce some very significant increases in taxation for some. There is evidence that, in some cases, these rises could be described as punitive.

Principles

But further to this, and far more fundamental, are the reservations I have about the principles that underpin the "20% means 20%" proposals. Here I turn to the Committee's own advisors, OXERA, in their document of May 2002, where they state in section 7.1 (p.64) under the heading "Principles of Taxation" –

"A priority for tax policy is to raise an appropriate amount of revenue as ***efficiently*** *and* ***equitably*** *(OXERA emphasis) as possible…Efficiency is important to avoid creating excessive market distortions, leading to disincentives to work and lower productivity, and to avoid using up excessive resources in the economy…"*

In simple terms, this boils down to 4 principles of taxation –

Taxation should be fair and equitable, often based on ability to pay
Taxation should be able to be collected efficiently
Taxation should be economically efficient
Taxation should be simple and understandable

I believe the Committee's 20/20 proposals fall down on all four of these principles.

Equity and fairness

We talk blandly of the principle of equity or fairness in taxation, and when we do, we cite income tax as the best example of a tax measure designed to be fair. The income tax system has been built up painstakingly over many years to be as equitable as possible by individualising peoples' tax bill to take their personal circumstances into account. There are 2 mechanisms for doing this –

- graduated rates, and
- a system of allowances.

These can be manipulated to ensure that those with low incomes are protected whilst those on high incomes pay proportionately more, in the name of fairness. As we know, the possibility of a higher rate has been ruled out. So that leaves only manipulation of allowances to get the required flexibility in the name of fairness. The Committee's aim is to make the higher earners pay more tax.

So is this a fair way to raise additional tax? The data reveal that the tax increases for some of the individuals and families affected are between 19% and 29%, at the top end. For example, a single person without dependants or a mortgage the rise in tax payable starts at £25,000 (below the average wage) with the maximum around £40,000 (a reasonable professional salary). Details for the types of family chosen by Finance and Economics to illustrate how the system works are given in the Appendix. Members will note that the absolute additional tax figure given only

at the top end of the scale serves to mask the substantial percentage increases lower down the scale.

Examination of the examples in the Appendix will reveal that the people who are most affected are the middle earners, whilst the rises for very wealthy are proportionately less. To claim that this measure is progressive, as the president does, is simply untrue.

In terms of economic efficiency one has to question whether the committee's measures damage incentives for individuals to better themselves or promote entrepreneurship? I believe that they manifestly do the opposite.

Complexity

Further concerns must be expressed about the complexity of the proposals. The President often states that keeping the tax system simple is high on his agenda. Certainly whenever a higher rate is mentioned, for example, the simplicity of the single rate is always raised. One has to ask whether the withdrawal of allowances obeys the President's simplicity rule. It does not. It is almost impossible to understand. What is more, I am convinced that the scheme's complexity will lead to administrative inefficiency and additional costs.

On each of the 4 grounds I have outlined above I believe that the IOD share my reservations and have expressed their opposition to the proposals. Members may pause to consider whether, if I can come to the same conclusions as the IOD, we might actually be right.

The absence of any assessment of interaction with the housing/mortgage market is a further concern. House prices are currently broadly static. Last year we capped mortgage tax relief. This proposal will further remove mortgage tax relief from those on middle-to-high incomes. The question must be asked – will this be the step that produces house price collapse and negative equity? The Committee have produced no evidence on this serious issue.

There is also concern that the Student Grant contributions system and the "20% means 20%" proposals target families over similar income ranges. What will be the extent of the impact on the family budgets of those families with mortgages and children at university? The Committee have not addressed this question.

Surcharge

So what is the alternative that I present? My amendment proposes that we abandon the punitive, unfair, inefficient and complex method that is the Finance and Economics Committee's 20/20 proposal, and replace it with a surcharge.

The ECOFIN surcharge on all tax bills, named after Council of Economic and Finance ministers of the EU (ECOFIN), is a far less complex method of raising £10 million; It is one that is far simpler for the public (and politicians) to understand; and one that spreads the load proportionately over all tax payers instead of only some.

In simple terms, every person's tax bill (including companies) will be calculated using the exact system in place today, and then be subject to the ECOFIN surcharge. To raise £10 million, the rate would be 2.63%. To mimic the phasing-in of "20% means 20%", it, too, can be phased in over 3 years from 2006, thus –

Year	*Rate*	*Additional tax*
2006	0.87%	£3.3m
2007	1.75%	£6.65m
2008	2.63%	£10m

To illustrate its effect, we only have to examine some projected tax bills using the maximum proposed rate of 2.63%.

Tax bill 2005

£100 £1,000 £10,000 £100,000 £1,000,000

Total tax 2008

£102.63	£1,026.30	£10,263	£102,630	£1,026,300

Spreading the load over every current taxpayer produces a rise in tax that is far more reasonable. It is manifestly fair and proportionate. It is also flexible, in that, should tax revenues improve in the future, the surcharge can easily be reduced, and vice-versa.

Financial and manpower considerations

Once again there are no manpower considerations to be accounted for as the scheme simply builds of the current income tax system. The scheme will generate the £10 million additional revenue required by the Fiscal Strategy.

APPENDIX

SINGLE No children No mortgage

Extra tax START	£25,000			
MAX at	£42,500	MAX INCREASE	2008	16.4%
			2007	11%
			2006	5.5%
Salary	£37,500	INCREASE	2008	13.5%
			2007	12.6%
			2006	6.3%
Salary	£30,000	INCREASE	2006	6.75%
Salary	£100,000	INCREASE	2008	6.4%
			2007	4.2%
			2006	2.1%

MARRIED No children No mortgage Wife earning

START	£48,000	MAX	£85,550	18%

SINGLE PARENT 1 child £120,000 Mortgage

START	£38,800			
MAX	£94,000	MAX INCREASE		26%
BUT EVEN AT £60,000 SALARY		INCREASE	2007	18%
			2006	16%

MARRIED 2 children £120,000 mortgage Wife earning

START	£59,500			
MAX	£129,370	MAX INCREASE	2008	23%
			2007	15.5%
			2006	7.7%
SALARY	£100,000	INCREASE	2007	19%
			2006	11%
SALARY	£80,000	INCREASE	2006	13%

MARRIED 2 children £200,000 mortgage Wife earning

START	£64,000			
MAX	£146,000	MAX INCREASE	2008	25%
BUT EVEN AT £80,000 SALARY		INCREASE	2006	11%