

CORPORATE SERVICES ZERO-TEN SUB-PANEL

THURSDAY, 13th JULY 2006

Review of Zero-Ten Design Proposals

EVIDENCE OF MR. JOHN SHENTON OF ERNST AND YOUNG

PANEL: **SENATOR JAMES PERCHARD (Chairman)**
SENATOR BEN SHENTON
DEPUTY PATRICK RYAN
DEPUTY GEOFF SOUTHERN
MR RICHARD TEATHER - ADVISOR TO THE PANEL

QUESTIONS

Senator J. Perchard:

Welcome, you are our very first witness to the Sub-Panel looking at the Zero-Ten design proposal. You have in front of you, John, a little bit of paper. I am obliged to read it to you. It is important that you fully understand the conditions under which you are appearing at this hearing. You will find a printed copy of the statement I am about to read in front of you. The proceedings of the Panel are covered by Parliamentary Privilege to Article 34 of the States of Jersey Law 2005 and the States of Jersey Powers, Privileges and Immunities Scrutiny Panels PAC, PPC, Jersey Regulations 2006 and witnesses are protected from being sued or prosecuted for anything said during hearings unless they say something that they know to be untrue. This protection is given to witnesses to ensure that they can speak freely and openly to the Panel when giving evidence without fear of legal action, although the immunity should obviously not be abused by making unsubstantiated statements about third parties who have no right of reply. The Panel would like you to bear this in mind when answering questions. The proceedings are being recorded and transcriptions will be made available on the Scrutiny website. Thank you for that. Now, John, in the Zero-Ten design proposal you are quoted on the back page as being involved in the initial consultation.

Mr. J. Shenton:

Correct.

Senator J. Perchard:

How much input did you have in the consultation process leading up to the production of the documents?

Mr. J. Shenton:

We had a number of meetings whereby the general proposals were obviously considered and discussed. We probably did not put in more than eight hours into the whole process.

Senator J. Perchard:

That is you personally?

Mr. J. Shenton:

Me personally, yes.

Senator J. Perchard:

How satisfied are you with the level of consultation that took place with the industry as a whole?

Mr. J. Shenton:

In order to get to a consultation document, which is obviously where we are, we had to take into account our various backgrounds, our clients and their understanding of the industry. The idea to me of a consultation document is to get into a position whereby you can put down some certain outlines, some facts, some details, some proposals, broad proposals, in order that it then goes out to consultation, and I think that that is what they did. Whether I think there is enough in there, I do not think there is, but it is I think a good starting point for consultation.

Senator J. Perchard:

So, you are not really satisfied with the consultation to date.

Mr. J. Shenton:

Well, I think the consultation to date, yes and no. I think it depends upon what comes out of the new consultation period. I think this is, as I said, this is the starting point and I think that document should be viewed as a starting point. It is not the finished article by any means. It is there for consultation.

Senator J. Perchard:

Do you think the document is too complex at this stage?

Mr. J. Shenton:

Speaking as a tax professional no, I do not. My personal opinion, and I think throughout the consultation period, is I would have liked more detail. I think that in some ways, you probably need two documents. I would have liked a lot more background, I would have liked more information concerning where they get the numbers from. I would like to have seen the projections. But, I am a technical person; that is what I like to see. I would like to actually dig into the basic principles and understanding. That is not technical enough but for the man in the street it probably is slightly too

technical. But, it has actually been reduced from the original consultation document where we started off. We tried very hard to get it down to a more readable level. No matter what you do with it, it is never going to be simple to understand. It is not a simple topic.

Senator J. Perchard:

Did many of your suggestions or advice that you gave in the initial consultation get to be included in the document?

Mr. J. Shenton:

Yes, we spoke around the broad principles and I think there were certain avenues we wanted to push a little bit further, which aren't covered, and we wanted a bit more explanation about some things, but there was obviously a time pressure on it as well and in order to get it out to consultation some things had to be cut.

Senator J. Perchard:

Okay, anybody want to add there?

Deputy G. P. Southern of St. Helier:

You have already mentioned the magic word 'numbers'. Where did the numbers come from? You were saying you would like a bit more detail of the background. Would you like to illustrate that...

Mr. J. Shenton:

Yes, we asked, there are numbers thrown around in the document about how much they are going to get from this and how much they are going to get from that. I have not seen any underlying numbers whatsoever in order to substantiate that.

Deputy G. P. Southern:

I have been asking as well.

Mr. J. Shenton:

If you take the whole Zero-Ten and the Facing the Future and the whole strategy of the States for GST (Goods and Services Tax) and the £45 million, I have not seen those either. We are technical people and I am not sure whether the Zero-Ten as discussed here is going to raise tuppence or £200 million. I cannot tell you.

Deputy G. P. Southern:

And if we were to go forward, are you saying that certainly from your point of view that you would want to see some of those figures if you were going to give this the --

Mr. J. Shenton:

Before I give the thumbs up I would like to see a breakdown of how the numbers are going to be made up. How much money we are going to get and where we are going to get it from, because the whole idea behind Zero-Ten was not meant to be a revenue raising exercise. It was meant to, as far as I was concerned, put us on a sound footing internationally. If I have my finance hat on, then we had to make sure that we were competitive on the international market. It was not meant to create lots more tax and put more money into the kitty for the States to waste. Zero-Ten was one of the things for Facing the Future which said that about the GST £45 million that you, yourselves, were going to save £20 million, economic growth was going to be 3 per cent. I have not seen how they are going to do the economic growth. I have not seen the £20 million saving, I have not seen the GST £45 million, how that has come to. So, if I am looking at Zero-Ten yes, I understand the basic principles but the numbers I have not seen.

Senator J Perchard:

That is interesting. You really have no idea what the target on Zero-Ten is?

Mr. J. Shenton:

Well, we know the broad target and we have been told the broad target is to fill the black hole which is £100 million or whatever it is, and we have had the Oxera Report and some of the fundamentals in there I cannot examine in any great detail because I do not have the same backup documentation which they were working from.

Senator J. Perchard:

Okay, let us move on slightly. Will, do you think the proposals in the Zero-Ten document enable Jersey to remain competitive with regard to its finance industry compared to particularly the other Crown dependencies?

Mr. J. Shenton:

I think if you look at Jersey, Jersey is obviously working in a slightly different market. We are not directly comparable with the Isle of Man, we are not directly comparable with Guernsey, in so far as our mix of business is different, our mix of revenues is different. If you look directly between us and the Isle of Man the majority of the Isle of Man's revenue is actually not gathered from taxation. It is taken from VAT and they have negotiated a phenomenally good deal with the UK government in relation to VAT and VAT recovery. So, their mix of business in relation to trust company business is different. If we are looking at this from a finance industry perspective, which is where the majority of the income comes from, their mix of business is different to ours, as is Guernsey's focus. I think the Guernsey proposals do not go far enough and I think they are heading for bankruptcy, but that is my personal

opinion. I think that theirs do not take enough tax from the finance industry or the people of Guernsey in order to maintain the current standard of living that Guernsey has. I think it does enable us to remain competitive. I think there are some questions which need to be answered. I think the Zero-Ten proposal is basically a solution to the problem which has been put to us by the EU. I think it would have been helpful if we had remembered on some occasions that when we were negotiating this that we are actually not part of the EU. I think that might have been a little bit helpful, that we were actually doing them a favour by coming inside. I know there was a lot of political pressure put on us by the UK government. I also think that it would have been interesting if all our discussions as far as I am aware, because I have not again seen minutes of any meetings which the officials of Jersey have had with the UK treasury, is that we are negotiating with the UK treasury to see whether all these measures are compliant or not. Should we have been negotiating with the EU Code of Conduct Committee, which is obviously not purely UK? I think we are competitive, which was the question you asked, but I think it would have been very interesting to have had, if you do it in a very simplistic form, a menu as to why certain other measures, which have been suggested and rejected, were felt not to have been compliant by the EU Code of Conduct Committee rather than the UK Treasury. There are still an awful lot of unanswered questions. They refer to it even in our Zero-Ten document which we do not have the answer for was the fact that they said that there was a chance that the UK Treasury would not seek to use the Code against publicly owned companies (I think it was point 19 in the 0/10 proposal). I do not think that we ever got to the bottom of that one because some of the proposals in the document, I do not like the RUDL charge, I think that is a political charge.

Senator J. Perchard:

We will go on to that one shortly.

Mr. J. Shenton:

I just think there are certain things where if you look and say, “Are we competitive with the Isle of Man?” the Isle of Man raised the point about could they use the company as collecting agent for the individuals, which I assume you will come back to when you come into the deemed distribution charge. The UK Treasury I understand has said no, they do not like it, but I do not know whether the UK Treasury are actually in this particular instance our masters. I know they are influential but I do not know if they are our masters. I think the end master is the EU Code of Conduct Committee and I would have liked to have seen a little bit more pushing of the envelope to that Committee and got them to have come back to us and say whether it was Code compliant or not. The idea of the Code was certainly not to put anybody out of business.

Senator J. Perchard:

Is the Code an evolving document, the EU Code of Conduct an evolving document simply to catch what they perceive as unfair competitive advantages being evolved by jurisdictions like Jersey? Is it

something that is evolving simply to catch up with us all the time?

Mr. J. Shenton:

Yes and no. It was aimed at harmful tax practices. My personal opinion on harmful tax practices is that it is for the country which feels that another country is abusing its tax system, for that home country to bring in legislation in order to stop that abuse. I do not think it is up to me to insist on third party countries bringing their tax system in line to bring it in line with their own. If I was buying a car I do not think it is up to me to go to Jacksons and say, "You've got to increase your prices by £500 to bring them in line with my own." I think it is up to me to reduce my own price in order to be competitive, and I think tax should be viewed in the same way. For harmful tax practices they have been very selective about which ones they have picked on. I would ask your expert, is the UK non-dom not harmful? Is some of the accelerated benefits and allowances given by Germany in respect of capital assets, are they not harmful? I did not see them in the Code of Conduct paper. Maybe they have a little bit more clout than Jersey has. So, they have been selective in what they are doing. Whether it is a moving feast I do not know, I have not spoken to the Code of Conduct Committee. I do not know who has. I do not know what their agenda is. Nobody has told us what their agenda is. We know what the Treasury stance is, they do not like most of it, but I do not know what the relationship is between the UK Treasury and that Committee.

Senator J. Perchard:

Okay, we are going to move on to RUDL (Regulation of Undertakings and Development Law) now, and I will lead a little series of questions before we are going to talk about anti-avoidance and distribution and attribution after if we may. So, the RUDL charge, what effect, John, do you think the RUDL charge will have on companies keen to start up business in the Island?

Mr. J. Shenton:

I think the RUDL charge is a political charge. I think in some ways maybe we should be asking the two Deputies and the two Senators what the answer to that one is. But, I think in answer to your specific question, none whatsoever. I think it is just an additional cost of running business in the Island. I think, administratively, I do not think you are getting value for money. I do not necessarily think that -- the RUDL charge is a payroll tax by any other name.

Senator J. Perchard:

Okay, we have a series of questions that will develop that, so nothing that will put them off, it will just put up their costs.

Mr. J. Shenton:

It just goes into the same pot of considerations when you are starting a business as to rent, rates, taxes,

the works. If you are a foreigner opening up business you could cross the tax one off if you are a hotel on the waterfront, you can cross the little tax one off as the proposals currently are. So, the RUDL charge is just an additional cost.

Senator J. Perchard:

Okay, well just developing this a little further because we are keen to gain as much evidence on the RUDL proposals as possible, what effect do you think the RUDL charge will have on the cash flow of both existing companies and foreign-owned, in fact all companies wishing to start up, on the cash flow?

Mr. J. Shenton:

Well, it depends. If the charges can be levied when you take on the employee then I think it was estimated that (I don't act for Le Riches or the Channel Islands Group), so I think it was estimated that the RUDL charge for them would be somewhere in the region of £1 million. If obviously it is levied up front then the £1 million will have an effect on their cash flow but, coming back to that, if under the current proposals they do not pay any tax, and I do not know what their tax bill is, I do not know whether it was greater or lesser than £1 million, then I cannot comment. Because they are saving tax at one end but paying out the RUDL charge at the front end. So, there will be an effect on their cash flow. The interesting one really is where you have got under current proposal, for the utilities, for example, will still be liable to the RUDL charge as will everyone in the finance industry. If the finance industry --

Senator J. Perchard:

That is not right actually, the finance industry are exempt from the RUDL charge.

Mr. J. Shenton:

Right, so the utilities are not.

Senator J. Perchard:

It is zero.

Mr. J. Shenton:

For the RUDL charge, utilities are still technically subject to the RUDL charge and still technically subject to tax at 20 per cent under a Zero-Ten proposal.

Senator J. Perchard:

Well, we will get on to that.

Mr. J. Shenton:

My personal opinion of the RUDL charge is that it is a mechanism in order to make Boots, Woollies,

WH Smith, JEP, Ronez, Channel Telly, the Marriott Hotel, or whoever happens to be at the time, contribute to the economy of the Island. I think the principle is right that people who are trading here ought to contribute to the Island. However, the RUDL charge has some very unnecessary consequences for your small trader when the only way to get out of the RUDL charge, or to get credit for the RUDL charge, is to go into this limited trading partnership which, I am trying to think of a polite word to describe it but I am failing, I do not agree with the limited trading partnership for an Island which is an international finance centre and anyone who wants to do business overseas or any international trading entity to come up with a device called the limited trading partnership. Say you take a large business in the Island who trades overseas, take a fulfilment company. Large fulfilment, internationally known fulfilment company, must employ hundreds and hundreds of staff, say 150 staff, and they end up with the RUDL charge. But, they must have, I do not know, again they probably have international borrowings, they have an international presence, and they are trying to get this financing, they are trying to get international backing called a Jersey trading partnership. It is bizarre. Also the fact is we do actually have all the requirements for the limited trading partnership on the statute book already, but it is called the LLP (Limited Liability Partnershhp) with a £5 million cap which no one will get rid of because it is politically sensitive not to get rid of the £5 million cap, which again you are asking to duplicate. The limited trading partnership I think is a non-starter. I think for even local trading partnerships for local traders who have various property finance agreements or venture capitalists coming in who require distribution so you end up controlling your distribution policy in order not to repay your venture capitalists, or you end up having to pay back your loans, if you suddenly metamorphosised into an LTP you would have enormous consequences. Enormous costs of renegotiating your bank funding because obviously you are turning what is a recognised legal entity into something else. The banks then have to get au fait with what is an LTP, recharges, re-mortgages, costs, legal fees, accountancy fees, tax fees, very nice thank you very much, but in the scheme of things not a great answer. But coming back to the RUDL charge, what they are saying is that it was a way to pick up your Boots and your Woollies and your WH Smiths. It has a very adverse knock-on effect to the local community. The cost to the local community will far outweigh the money which you get from the RUDL charge, plus it is another tax through the back door through administration.

Senator J. Perchard:

Can I ask you then, John, you rightly in my opinion suggest it would be nice to find a mechanism where these non locally owned companies can contribute? If it is not through RUDL what mechanism could we use?

Mr. J. Shenton:

Well, I would like to know, as I alluded to earlier, I think there is, if you are a quoted company, HM Treasury have said that they may not come within the Code. I do not know whether that has been explored. I do not know what the answer is, because Smiths, Next, Boots, Woollies, are all quoted

companies. Yes, some of the other ones may be privately owned companies and there is bound to be winners and losers with whatever system you bring into account.

Senator J. Perchard:

If they do not come within the Code what are you implying then?

Mr. J. Shenton:

If they do not come within the Code then we are allowed to discriminate against them and we can tax them however we like.

Senator J. Perchard:

And you are not sure whether they do or do not come within the Code.

Mr. J. Shenton:

HM Treasury have suggested at point 19.1.1 “The position discussed with HM Treasury seems to suggest that publicly owned companies operating in the Channel Islands could be considered as falling outside the scope of the Code.”

Deputy P.J.D. Ryan of St. Helier

So, you would stay with the 20 per cent on that presumably and then they would have a double tax agreement anyway so...

Mr. J. Shenton:

To be honest the way the taxation works and the way the double tax credit system works and the fact that the majority of the entities in Jersey are UK entities makes no difference to Boots, to be honest, whether they pay 1 per cent, 0 per cent, or 30 per cent, because effectively it all flows back to the UK and they end up getting a corresponding credit in the UK for the Jersey tax paid. The only people who will have an issue with paying tax in Jersey is if we put the rate up to 35 per cent, which I do not think we are going to do, or they are in losses, because then it is a cost to them, tax is a cost. But, under the current system and under the current treaty arrangements it works very nicely, thank you very much.

Senator J. Perchard:

So, as an alternative to the RUDL charge you suggest that we explore the opportunity to tax at a different rate the companies that are non locally owned.

Mr. J. Shenton:

I would like them to explore with Treasury further as to whether the publicly owned companies fall in or outside of the Code, yes.

Deputy P. J. D. Ryan:

Would you just agree with me though, that any RUDL charge on those companies that are UK owned, because they are a real cost addition to the companies, is likely to be inflationary, they are likely to pass on the charge?

Mr. J. Shenton:

Any cost is likely to be inflationary because obviously you end up with profit margins and we are all in business, you get sent your budgets each year and you know how much money you have to make.

Deputy P. J. D. Ryan:

What do you think of the assertion from the Treasury that those companies would absorb those charges because they are already charging, this is getting across to GST as well, but they will absorb them because they are making enough profits to be able to do that?

Mr. J. Shenton:

Well, I am no economist but you charge what the market will stand. If you think the market is going to stand you passing on those costs then you will pass those costs on. However, you are not going to run your business as a loss and if you think that you can get an extra £1.50 out of anybody then you are going to charge them the extra £1.50.

Deputy P. J. D. Ryan:

So, it depends to the extent that those companies have market power in their particular market.

Mr. J. Shenton:

Correct.

Senator J. Perchard:

John, we want to wrap up with RUDL in the next couple of minutes. Does the variable RUDL rate as by industry, according to the document, cause you concern?

Mr. J. Shenton:

No more so than the RUDL charge in itself.

Senator J. Perchard:

I thought you would say that. Tell me about LTPs. Are there any other advantages with LTPs other than the possibility if one disincorporates of reclaiming your RUDL charge? Are there any other advantages?

Mr. J. Shenton:

It gets you out of the deemed distribution charge, which is mentioned further on in the document.

Senator J. Perchard:

Does anybody want to say anything else on RUDL?

Deputy G. P. Southern:

It is pretty clear.

Senator J. Perchard:

Yes, it is pretty clear. You would confirm also that RUDL would probably have an inflationary effect on the economy as it is an extra cost.

Mr. J. Shenton:

It is an extra absolute cost, it is an extra absolute cost to a business because the way it flows through the double tax credit relief.

Senator J. Perchard:

Okay, well unless there is anything else on RUDL.

Mr. R. Teather

Just on that one actually, do you know whether these Jersey-owned companies, Boots and so on, tend to be owned directly from the UK or via some other offshore structure?

Mr. J. Shenton:

The ones I know they are owned via structures which allow credit to flow back to the UK, yes.

Mr. R. Teather

So, the credit still does flow back.

Mr. J. Shenton:

Yes, you obviously have an issue with foreign entities but I do not actually think that we have very many of those. You might have problems with your French supermarket.

Deputy P Ryan:

I have a little question. One of the things that has been said by certain Jersey-owned businesses is that without RUDL they will be at a trading disadvantage to non Jersey-owned businesses. Do you think

that is true?

Mr. J. Shenton:

No, because it is simply one of the....

Deputy P Ryan:

This is one of the bases for the need – let's tax them. You did actually a little while ago you said that you agreed with the concept of those particular companies.

Mr. J. Shenton:

I agree that if people are in the Islands, and I think this goes all the way back down to personal taxation and GST and everything else, people who are in the Island should contribute to their Island. With regard to someone being competitive or not, if you take two building suppliers, one locally and one UK-owned, then the net amount of money which they have in their pocket at the end of the day to distribute to their shareholder will be Jersey will end up effectively with 80 per cent because they are going to pay 20 per cent and they will end up with 80 per cent to pay out, and the person in the UK will end up with 70 per cent because they are paying tax in the UK at 30 per cent. So, saying that without the RUDL charge they are going to be uncompetitive no, I think if the RUDL charge is brought in for the UK-owned entities in some ways we are actually distorting the market in favour of the Jersey company because the RUDL charge is not a direct cost for them. So, their argument is fundamentally flawed. Without the RUDL charge it is a level playing field, with the RUDL charge they are actually asking the government to give them a subsidy.

Senator B. Shenton:

So is that an unfair tax practice?

Mr. J. Shenton:

No, because a RUDL charge isn't a tax.

Senator J. Perchard:

So, just to sum up on that, abandon the RUDL proposals?

Mr. J. Shenton:

I can see from a public level that the people who are trading in Jersey ought to contribute to the Island and be seen to contribute to the Island, and I think going back to detail and broad statements I think politically you probably need Boots to contribute to the Island but the RUDL charge is not the right way to do it.

Senator J. Perchard:

Okay, into politics when you have finished at your accountancy practice. We are going to move on to distribution and attribution and Senator Shenton is going to lead a series of questions there.

Senator B. Shenton:

Actually before I start, and before I forget – IBC status.

Mr J. Shenton:

Gone.

Senator B. Shenton:

What are we going to do about the, or what do they intend to do about the companies that currently have IBC status?

Mr. J. Shenton:

That one has been parked. Obviously as you know the IBC (International Business Company) status has been effectively abolished so you don't have any new IBCs from 1 January 2006. You can in Guernsey, bizarrely, but you cannot in Jersey. However, because of the arrangements reached prior to 31st December 2005 the IBC status has effectively been grandfathered until 2011 and any existing agreements will run until then. The IBC status of paying at 0-2 really affects us looking south. It does not affect going north. If you look to Barclays or someone like that they did not need an IBC status because again as I alluded to before they pay tax at 30 per cent. So, what you are actually looking at with the IBCs is the Zero-Ten, the large foreign-owned banks and trust companies. Your Swiss banks, your Belgian banks etc, we have a number of French banks as well. France is a different position in so far as the tax works slightly differently there. You are really looking at the effect on the Swiss banks whereas tax in Jersey is viewed as an absolute cost. What are they going to do about it? They were thinking of bringing in a cap in relation to the amount of tax which will be payable by those entities, which we are allowed to do.

Senator B. Shenton:

Are we allowed to bring in a two-tier system?

Mr. J. Shenton:

Until we get the proposals ratified by the Code of Conduct Committee.

Senator B. Shenton:

Not the Treasury?

Mr. J. Shenton:

Not the Treasury. Well, the law has to go through the Treasury and the law has to go through Privy Council. However, I think the Isle of Man have basically brought in some proposals which the Treasury do not like and they are taking it to the Code Committee, and I think they are being slightly more aggressive with Treasury saying, well, yes you can stop these at Privy Council if you want to but then you are going to have a constitutional problem on your hands. Are you up for the fight? I do not know whether we will take the same view. The advantage we have got is that we are not first. The Isle of Man are first and technically Guernsey is second. I would expect Guernsey to put theirs back a year in order to come from 1st January 2009 when push comes to shove. So, we can wait a little bit to see what the UK Treasury and Privy Council do in relation to some of the proposals put forward by the Isle of Man. Going back to your specific point about IBCs, we will need to find a solution to the problem of Zero-Ten in relation to the IBCs and until we see the legislation and see what everyone else has done and get the views back from the Code of Conduct Committee we will not know how much room we have to manoeuvre around those. Obviously there are suggestions that because you do effectively have two rates, you have the 10 per cent rate for your financial services business and a 0 per cent rate for your other business of splitting businesses and partnerships and everything else, in some ways that will probably come back to us as the tax professionals.

Mr. R. Teather

Do we know that we are allowed to cap or do we just hope that we are allowed to cap?

Mr. J. Shenton:

I understand that the cap has been mooted and has not been rejected but I would want something in writing and or anything else in order to believe that.

Deputy P. Ryan:

Could you tell us, you mentioned the Isle of Man being more aggressive with the Treasury and effectively saying that to the Treasury, okay, we hear you don't like it but nevertheless we want it to go forward to the Committee, could you tell us in what areas they are being more aggressive?

Mr. J. Shenton:

One of the ones I've got at the moment is the point I alluded to earlier – is they would make the company the agent for the directors, the minority shareholders and everyone else in relation to the collection of tax.

Deputy P. Ryan:

So, this is round the deemed distribution.

Mr. J. Shenton:

This is round the deemed distribution idea, so they are being slightly more aggressive there. Some of their early proposals were thrown out by Treasury and they have not gone back with the redrafting yet. They are still sitting there with Privy Council. I am not quite sure what the Isle of Man are going to do in some of their areas. But, it will be interesting because some of the areas they were looking at were they did try to pick up a branch tax which got thrown out by UK Treasury. I do not know whether they intend to revisit that or not. One could liken the branch tax to the remittance basis for UK non-doms, whereby if you've got a UK resident non-dom individual he only effectively gets assessed on profits derived in the UK and not his foreign profits, which in some ways is what you would be looking for for Boots or someone where you are only actually looking to tax profits arising in Jersey rather than anywhere else. The same with foreign branches and everything else, the problem we have is we want to keep the 0 per cent rate for the exempt company because that is where we derive the majority of our income from. So, with regards to the Isle of Man I think we just have to just be mindful of what they are doing.

Senator B. Shenton:

Moving on to the attributions, I mean it is exceedingly complex – do you think it's too complex?

Mr. J. Shenton:

I actually do not think it is that complex. It is not that complex if you change the basis on which profits are coming out onto a FIFO basis rather than a LIFO basis.

Senator B. Shenton:

Well, why did they go for?

Mr. J. Shenton:

LIFO - no idea.

Deputy P. Ryan:

Could you explain that?

Mr. J. Shenton:

Well, at the moment the deemed distribution charge when you refer it back to the distributions made over the previous years, they are saying it is on a LIFO basis so therefore every three years you have to distribute everything in order to get back to where you started. Otherwise you end up with a deemed distribution charge in relation to the first year of trading. So, effectively every three years you end up having to start again, which is completely bizarre. They might as well have a complete look-through and do it on a year-by-year basis as they're proposing to do with investment companies. If you did it on

a FIFO basis then at least it allows the company to maintain its distributable reserves to reinvest for a rolling three-year period, which I think from a commercial perspective is probably right, in order that it gives some flexibility to reinvestment for the company and gives them enough opportunity through adverse trading conditions or where they're looking for expansion or merger in order to keep their balance sheet relatively strong going forward. I think when you have a certain amount of borrowings from the bank you require certain things to be in your balance sheet and you require a strong balance sheet. If you are being asked because there is no other provision, to effectively wipe out all your reserves every three years, before we even get on to the minority shareholder profit, then I do not think that is right. I think if you do it on a FIFO basis, first in first out, then it gives the companies far more flexibility to maintain a strong balance sheet, to be able to plan much better for the future in order to maintain and grow their business and get your 3 per cent economic growth, but on the basis of LIFO which has been proposed where, I do not know where that came from, that is completely absurd. It is looked on as being difficult in order to administer. I do not actually think it probably is that difficult. The thing with the deemed distribution charge however, is they are talking about picking these distributable profits up under accounting profits as computed under GAAP or IFRS or whatever accounting treatment we use. For small companies there is no requirement in Jersey for a company to be audited. The majority of these companies are probably not compliant with GAAP, IFRS or even some of the probably standard accounting practices. In order for you to have a distribution on GAAP or whatever system you use I think is fundamentally wrong. I think that if you are going to do a distribution policy then you have to compute the distributable profits in accordance with standard tax principles as you would tax a sole trader. For example, say you had a plumber who had given options to his staff and had done all this that and the other through a corporate entity and the plumber is a sole trader, the accounting profits and the tax profits are going to be completely different. Therefore, you are actually either penalising somebody depending on where your accounting principles go for being a sole trader, or you are penalising somebody for being a corporate, depending upon how the principles of accounting go. You have to have one regimented view in that the same tax principles, which have been built up over hundreds of years through case law and everything else, apply to both sets, to both the sole trader and to the corporate, that you have a level playing field. The deemed distribution charge, to me, is not that difficult to administer and for my clients - I notice in some of the representations you have had that you have only been talking to the big four and do not take into account the small trader. But, my clients will not go into a limited trading partnership in order to avoid a RUDL charge. They might go into a limited trading partnership if you insist on the UK GAAP or IFRS in order to compute the profits being attributed to them, that is a far more real case to me than the RUDL or the other issues surrounding it. So, the deemed distribution charge, not that difficult to do, if you've worked out your taxable distribution for £100 it is only a little Excel spreadsheet which anyone can do, it is probably about five minutes to work out what you have left. The issues come where you have change of shareholder or options kick in or your accounting date is slightly bizarre. We still have prior year-based assessment which is bizarre, which they will bring up to date, but then you are going to still end up with

the accounting period in the year in which the charge is made. So, you are going to end up with complexities like that. But, the deemed distribution I do not actually have a problem with that. I think it is a way for companies in order to keep their balance sheet, to keep the banks happy.

Senator B. Shenton:

Well what about the poor old minority shareholders that may be taxed on something he hasn't got?

Mr. J. Shenton:

Well, I think this is the -- you will have this issue whether you have a deemed distribution charge or you actually assess them on a straightforward distribution -- you effectively look for deemed distribution in the year of the company, where you get a three-year delay. One would say that on the deemed distribution charge you at least get a three-year holiday. It does not work. You have to protect, which is where we come back to the Isle of Man point whereby a company can act as an agent for the individual. If you have a minority shareholder then you can effectively turn off the tap in relation to dividend. You have seen it in the paper. If you read the FT you have Hargreaves at Matalan trying to take Matalan private and he has gone to the market and he said, "I'm going to turn off the dividend and I'm going to force you to sell your shares." I do not think it works, the guy at Monsoon tried to do the same thing and Monsoon still is not private, but you have a problem with your minority shareholder. Because if you are a minority shareholder the majority shareholder can turn the dividend tap off, and if he wants to try and acquire your shares there is an argument to and fro as to whether it actually increases the capital value of the company or decreases the capital value of the company, I will not go into that now, but he could on the face of it force him to sell his shares back to him because of the size of the tax charge. If you have some old Jersey companies you still have grandfather who probably still has 15 per cent of the company, who does not have a clue what he is doing. It is just sitting there. He has no day-to-day involvement in the business, and I am going to send him a tax bill for £50,000. Maybe I will be sending it to his estate, I do not know, I think you need protection for the minority shareholder. You cannot force, under company law, I cannot force a company to pay a dividend. That is the other option and that is completely absurd. You cannot look through the corporate veil in a company which sells financial services and companies and trusts and everything else to say that they are going to try and look through the corporate veil is just bizarre which was the other suggestion. The solution to that is if you go to zero there is no other way round it. You cannot allow your trading profits to be rolled up in a company.

Senator B. Shenton:

But they can't be rolled up forever?

Mr. J. Shenton:

Well, they cannot be rolled up forever, no. They have got to come out. There is reams and reams of legislation. If I am a wealthy individual then I can roll up the profits in my company tax free and

therefore I get a -- if I am a wealthy individual with a trading company then I am getting, unless you put in reams and reams of anti-avoidance legislation about matching loans and capital distributions of a company which is going to take the tax law from this big to this big and you are going to end up more anti-avoidance than you are with actual legislation. Then, he is getting cash flow benefits (...inaudible) against me who is a poor employee. Because I do not have a choice. Or, do I actually then form a co-operative of 21 employees. There was also talk about where you have the de minimis on your shareholding, which was talked about in the paper. I do not know where they have got with that. It is bizarre that you have to look through everything, because you have to go through, if I had a share in BP I would have to go through every single BP set of accounts and all their subsidiaries, all 250 odd companies, in order to find out how much of BP I owned. But, there was talk, they were talking about if I did not take a dividend then it should be treated as a loan to the company. Again, that is bizarre. Have I loaned BP money because I have an investment in them? It is complete nonsense. So, you need to protect the minority shareholder. If you have, in some ways there is a slightly similar provision in trust law about where you have a right of recovery from the trust. If you have taken distribution out of the trust and you are the settlor of the trust in the UK then effectively, under certain circumstances, you get assessed on the income of the trust whether you get it or not, and there is tax right of recovery from the trust in order for the settlor in order to get his money back out of the trust. The problem you have here is you have corporate, and therefore you are running against all the principles of corporate law in order to get a shareholder to have statutory rights of recovery out of the company...

Senator J. Perchard:

This is a very complex issue. There may be some human rights issues involved here as well.

Mr. J. Shenton:

Well, I read the bit on your website about human rights and I thought I hope they're not going to ask me anything about human rights.

Senator J. Perchard:

Well, in view of the time can we press on?

Deputy G. P. Southern:

How easy do you think it would be for the finance sector to avoid much of this 10 per cent charge? I mean there are ways of manipulating business so that if you have got a balance between Zero and Ten.

Mr. J. Shenton:

To be honest I do not think it is actually going to happen I think that you have -- because of the international structures of all these companies, because of Plc rules, because of the relatively minor profits which are held in Jersey by some of the big corporates, it will not happen. HSBC for example,

again not a client of mine, are not going to bring in some elaborate scheme in order to avoid a little bit of Jersey tax when their overall tax bill is 30 per cent and they are a large Plc and they have all the reporting conditions along to the bank authority and everyone else. It is simply not going to happen. The ones where it could happen would be your small, locally owned company but there is no point them avoiding the 10 per cent charge because effectively it is going to get picked up through their shareholding. So, I do not think there will be, I may be wrong, but in my personal opinion I do not think there will be any abuse of the 10 per cent charge.

Mr. R. Teather

So, you think it is possible but there is no motive.

Mr. J. Shenton:

It is possible, as a tax adviser most things are possible, it depends upon your appetite, but I do not actually think it will happen. I think there are too many external influences. I do not think any of the entities which are subject to the 10 per cent tax in Jersey would have sufficient clout in order to go through the process. They are all terribly reputational. Their reputation is effectively what they trade on. They do not want front line headlines in the FT or even the Jersey Evening Post saying that they are using some mechanism in order to flout the 10 per cent tax charge. It is simply not in their interests to do so.

Deputy G. P. Southern:

Can I take you on to the Tier 1 capital zero rating, those Tier 1 capital – I think the Isle of Man is looking at 10 per cent on Tier 1 are we being over generous?

Mr. J. Shenton:

I think we are probably being a little over generous but I think it depends how we are rolling that up into the -- how that actually then -- you have to look at it in the proposals because obviously what you've got in the Isle of Man they are not trying to assess the banks or the trust companies at all. They are all subject to 0 per cent . So, we are not taking the Tier 1 charge because it was subject to the 10 per cent by a different route. I have not seen a mechanism where you are going to avoid the 10 per cent charge and the Tier 1 capital charge because I would expect you are going to fall into a 10 per cent tax band. So, if you look to the Isle of Man proposals they are not intended to tax banks, they are not intended to tax trust companies, and the Isle of Man saw that as a way in order to get trust companies to effectively move to the Isle of Man. Probably you have the expertise, labour and the onward profit repatriation. So, yes it may work for a Swiss trust company who may get an absolute saving by moving to the Isle of Man but to save 10 per cent in tax to relocate?

Deputy G. P. Southern:

So, going back to the different nature of the businesses that we do compared to the Isle of Man.

Mr. J. Shenton:

Yes.

Deputy G. P. Southern:

When we talk about competition then, it is fairly limited competition?

Mr. J. Shenton:

It is limited competition, but you do not want to open up -- there is the opportunity for them to open up and expand into other areas. What you have is, we do not want to make the regime so punitive that they want to move. The Isle of Man concentrates on banks, which is why there is a 10 per cent Tier charge for around capital because that is the fundamental make up of their economy is banks and VAT and that is where the Isle of Man finance themselves. You have to look at each different market and see where they are specialist. Nobody is going to relocate 300 staff, their computer systems and everything else, in my opinion, to save 10 per cent tax, especially if they end up with tax further up the line. So, I do not think that is a big risk. The cost of doing business in Jersey is a risk in so far as they may want to outsource some of the lower tier jobs overseas. I think that is a risk.

Deputy G. P. Southern:

Have they said that, is that already happening? The back room jobs have largely been --

Mr. J. Shenton:

There are some. It is creeping up. Mauritius is cheap, if you go to the UK the UK is cheap if you back office your admin and your accountancy and everything else, that is cheap. But in some ways the policy pursued by the government several years ago was to try and move the low value jobs overseas. I think when you wanted a regulation of undertaking that that was seen as an opportunity to get rid of some of these lower jobs in order to concentrate on higher value, therefore higher profits, higher taxes in Jersey by effectively moving Jersey up the fee ladder so to speak. So, that has happened. Bizarrely in the UK a lot of their outsourcing to India and everywhere else is coming back. I think a lot of their call centres are coming back into the UK. So, that will continue because people will always look for, you know, if I have to pay an accountant £50,000 in Jersey and I can get one for £20,000 in Mauritius and they are exactly the same then it is pure economics. But you need to service your client and it is the front office interface with your client, which is what we are good at. They also need to be here for management and control reasons, for certain tax planning, so you need the high level bit to stay in Jersey. But if you end up outsourcing the back office well, it will probably continue as long as other people are more competitive. We do not have the resources. If you go round the trust companies or the banks, there are probably a thousand vacancies, we cannot get staff, or we cannot get decent quality staff.

Deputy G. P. Southern:

There's an argument that because of the structure of the Isle of Man economy that it can afford to play games, and go down the spiral as far as it wants and that actually in rushing down the spiral with them we are going to end up the loser.

Mr. J. Shenton:

Which is what I have said is we have to keep an eye on what the Isle of Man are doing. We do not have to follow the Isle of Man. They are a different competitive market to us and I think we have to acknowledge that. 80 per cent of their income comes from VAT so they can afford, if they get economic growth by getting more people to come and live on the Isle of Man, which then is going to increase their VAT take, they can afford to take a far more aggressive view with the banks and the trust companies. As I said, the trust companies under their proposals is 0 per cent but their proposals, the Isle of Man proposals came out that they were going to be 0 per cent 18 months ago it must be somewhere around there, and the Isle of Man proposals under Zero-Ten remember have already kicked in. They have kicked in from 1st April this year. I have not seen anyone relocating.

Mr. R. Teather:

Well, it is not actually passed yet.

Mr. J. Shenton:

Well no, but they have been charging, they have been using the 0 per cent proposal since then and I have not seen anyone seriously looking at moving back there, and going back to investment in Jersey the number of trust companies recently been taken over, Capita took over Channel House; the Royal Bank of Canada took over Abacus which was a locally owned business, and the Royal Bank of Canada is foreign money, and they merged, these acquisitions have taken place within the last year when Zero-Ten has been on the table, when all of the Code of Conduct proposals have been on the table. And that is not showing an outflow of investment, it is showing an inflow of investment. So, we need to concentrate on what we are doing, but we need to keep an eye on what everyone else is doing and if they have got through any nuggets then we have to make sure that we sail along on the back of what they have done but we do not blindly follow them down the alley they are going. Because if Jersey and Guernsey followed the policy of the Isle of Man, which is what Guernsey in some ways are doing, we would go bankrupt and we would have VAT at 17.5 per cent because it would be the only way to stay in in order to sustain our services.

Deputy G. P. Southern:

You mentioned before that in Jersey we have a problem, and the problem is the resources/the skills that we cannot get enough people. Is that the major problem you see in the medium term? Short to medium

term?

Mr. J. Shenton:

It is a problem for me in my business, yes, certainly. And I think it is probably -- the finance industry is very buoyant, no doubt at all about that, the finance industry is very buoyant at the moment, and there is a skill shortage. We have a phenomenal reputation abroad and I do not think that should be underestimated, and if we can get some more staff in then we can make more money. But, I am not naïve enough to think that if I suddenly fill in Jersey with 200,000 people that it is going to be as nice a place to live that it is at the moment. We need to get the staff, we need to get the right quality staff in, but we need to make sure that we do not overpopulate or under-populate, and I will leave that to you four. Going back to where you were before about the question you said, was there an alternative to the RUDL charge, there probably is. If Treasury do not like the Plc there is one which has the same effect but does not cause the same anguish down to the lower Jersey company. Under the GST proposals for the finance industry, which I am sure you have all read, that they are effectively exempt and there will be restriction on their recovery of import tax, you could, because we are allowed to discriminate on indirect tax and I can discriminate between anyone I like as long as I do not contravene human rights, you could put a restriction on the amount of recovery which on a turnover basis and say, "I am sorry, if your turnover is greater than £X million and you are in the retailing sector", for example say you are a large chemist, "then we are going to restrict your recovery to 95 per cent of your input or output." You can do that, you can draw a line wherever you like, and then it is administered by the same people who administer GST. So, you end up effectively it is non-creditable. It is a cost on their business but it achieves the same without bringing all the individuals in.

Senator J. Perchard:

Would that not catch some of our large Jersey businesses?

Mr. J. Shenton:

Well, it depends how discriminatory you are in what you are doing. It depends where you set the level. If you set it on retail for example and said it relates to turnover in excess of £X million, I do not know what Boots or Woollies turn over. Which local business?

Senator J. Perchard:

Well, Le Riche.

Mr. J. Shenton:

But they are not paying any tax. To be honest Le Riche are going to end up in the same position as Boots basically, at the end of the day. Le Riches are a quoted company. So, you end up with the same problems -- at the end of the day there is not going to be that much difference between me having a

share holding in Boots as there is in Le Riche. The one thing you may catch would be, again I do not know how much debt and how it is structured, is you might catch poor old Gerald, you know, Gerald Voisin, or --

Senator J. Perchard:

Some of the bigger --

Mr. J. Shenton:

Some of the bigger retail businesses, you know, probably talking about Le Lievres, in our terms, as a large local business.

Senator J. Perchard:

You make a good point.

Mr. J. Shenton:

And I do not know whether they are quite in the same category as Boots and Woollies. Yes, you would catch Dandara, but Dandara are going to get caught through the development profit tax anyway, so you would end up excluding building suppliers or property developers from that charge. Because I can discriminate, I can discriminate GST and, I am sorry, it applies to me, I can put GST on hair care products where me and my brother are obviously fine, and I am discriminating against the rest of the people in the room. The beauty about GST is actually I am allowed to discriminate in the same way as I am with income tax and it is a way to actually attack your foreign entity without seemingly attacking them. But again, they would have to then again, going back to the point you had before about whether it is inflationary, I am effectively putting 5 per cent on their costs which would then be passed back to the consumer so yes, it would be inflationary. But, taking money out of the economy may not be a bad thing. If you discriminate between Boots and Le Quesnes then Boots may be forced to keep their prices lower or you may end up with a more equalisation of prices, I do not know.

Senator B. Shenton:

Did you put the subject to the consultation?

Mr. J. Shenton:

No, I only thought about it last week. It was only when I was going through some other bits and pieces that I thought well, what can we discriminate about, and it was really a way to try and avoid the RUDL charge so no, sorry, I only thought about it last week.

Senator J. Perchard:

Just a couple to wind up on. There is a proposal in the Zero-Ten design document that rental income

will continue to be taxed at 20 per cent, are you familiar with that?

Mr. J. Shenton:

Yes.

Senator J. Perchard:

With a withholding tax if necessary for non-resident landlords. What are your views on that? It will clearly give an advantage to businesses who own their own premises.

Mr. J. Shenton:

Well, no it will not, because they pay for the upkeep and they pay rent and everything else. I think that is a misnomer that you end up with the upkeep, you end up with the financing costs and everything else. If I own my own building it means that I do not have £5 million in the bank earning bank interest which the guy who rents the building probably does have. So, I think rent against non-rent, especially on the business sector, is a bit of a red herring. The UK have a non-resident landlord scheme. If you own a property in the UK (...inaudible) you pay tax on the rental income on that property whether you live in Jersey or you live in Mongolia, it makes no difference. For Jersey to follow suit I think it is right, I think they are using Jersey resources. There are obviously you get deductions against your rental income, you have financing, you will end up with rates, insurance, whatever else you pay. Remember we do not tax the gain, we are not suggesting that if you buy BHS for £5 million and you sell it in three years' time for £8 million they are not thinking about assessing the £3 million to capital gains tax. All they are saying is that we will assess you on the income which has effectively been taken out of Jersey by way of rent. I completely agree and I think it is a good move, as I think the change to superannuation funds in relation to rental income is also a good move.

Senator J. Perchard:

Okay, just one final question then. Is there an alternative to, bearing in mind the detail needs to be ironed out of the Zero-Ten proposal, but is there an alternative revenue raising proposal that we have not considered?

Mr. J. Shenton:

Which you have not considered? No, which you have not considered, no, I do not think capital gains would send the right message out, I do not think inheritance tax would send the right message out, I do not think it would bring in the required amount. I think Zero-Ten and GST is the right way to go. I think the problem you have is a perception problem in so far as Jersey in some ways has paid too little tax for too long. All our services are effectively financed by foreign investment. If you go back to the Evening Post yesterday the average disposable income in Jersey is 40 per cent higher than in the UK. We pay less tax than the UK, we pay less national insurance than the UK, we pay less rates à la council

tax than they do in the UK. We do not have VAT. Our tax allowances are phenomenally higher, our direct rates of income tax are lower, corporate tax rates are lower. Everything when you compare us to the UK we are phenomenally lower but we enjoy a much higher standard of living, and I think that what we have is we are saying that, you know, Jersey is up here somewhere and the UK is here and everyone thinks that we are trying to take Jersey from here to here but actually what you are trying to do is take Jersey from there to there, and I think that it is a perception issue. I do not think it is right that people who earn £40,000 a year do not effectively pay any tax. So, I think that we need to get it over to people it cannot always be a free lunch. I think that we should slowly put taxes up and people start to appreciate what a high standard of living they've got. So, if you look around the developed world as to various tax raising initiatives I think we have discounted most of them and I think the answer lies in Zero-Ten 20 per cent tax on the individual. Although it will affect me, 20 per cent means 20 per cent, unfortunately I think is a necessity. I think that once people earn, which does not affect me, more than £150,000 a year I do not think they should have personal allowances. I think they probably have enough disposable income to pay in an extra bit into the community. I think we need a cap for the 1 (1) K's, I think that needs to be looked at. I think if somebody is coming to the Island and is agreeing to pay £100,000 to £120,000 in tax then they should be subject to a different regime because of the amount of other benefits they bring to the island when you've got, and they can go to Switzerland and pay nothing, so there is a real competition there. We have lost people to Switzerland who had looked at coming to Jersey. I think unfortunately GST is a good thing as long as you make sure that the less well off in the community are compensated for its effects and in some ways, unfortunately, there is a stigma about tax credits and handouts from the state and I think that that in some ways the problem you have is that stigma. Because to even it up these people have to be entitled to this money and no one is saying that they should not get it out and they should pay it back to them and that you need a level playing field, but unfortunately coming through all the proposals, even though I have not seen the numbers, I think Zero-Ten together with GST is probably the best way forward.

Senator J. Perchard:

Thank you. Any further questions? With that I would like to formally thank you, John. It has certainly been enlightening and I close our session and wish you well.

Mr J. Shenton:

Thank you very much. Obviously if you need anything, ask (... inaudible) Shenton.