

STATES OF JERSEY



DRAFT BUDGET 2017 (S.R.8/2016): RESPONSE OF THE MINISTER FOR TREASURY AND RESOURCES

**Presented to the States on 8th February 2017
by the Minister for Treasury and Resources**

STATES GREFFE

**DRAFT BUDGET 2017 (S.R.8/2016): RESPONSE OF THE MINISTER FOR
TREASURY AND RESOURCES**

Ministerial Response to: S.R.8/2016

Ministerial Response required by: 27th January 2017

Review title: Draft Budget 2017

Scrutiny Panel: Corporate Services

INTRODUCTION

The Minister, as always, welcomes the assistance of the Panel. Whilst the debate on the Budget 2017 has now taken place, full responses are given below to all findings and recommendations.

FINDINGS

	Findings	Comments
1	Increases in Impôts duties for alcohol and tobacco are in part linked to health considerations.	<p>Rather than being in part linked, the strength of evidence for the causal link between the price of alcohol, level of consumption, and related harm to a population is considered extremely robust. Studies demonstrating this link include systematic reviews and meta-analyses, which are considered the gold standard in scientific evidence, as they analyse the results of all available research studies on a particular intervention, in order to calculate an overall effect size.</p> <p>Pricing policies and taxation are therefore employed as one of the most reliable tools to decrease population-level alcohol-related harm and per capita consumption. This approach should be distinguished from provisions targeted at sub-groups with alcohol dependence, who require specialist care and clinical support – although price increases serve to create a supportive environment for these higher tier measures. Universal price increases impact behaviour at a wider population level, and more so among price-sensitive groups such as young people. This wider population-level approach, by impacting behaviour to a small degree, but for a larger proportion of the population, leads to large economic savings; for example, through increased productivity in the workplace, reductions in preventable cancers and other illness in later life, and reductions in alcohol-related crime, violence and road accidents.</p> <p>WHO and OECD both recommend tax increases as part of a strategy to reduce the harm caused to society by the use of alcohol.</p> <p>It is also important to note that while increases on impôts duties are linked to reduced consumption and therefore need to be considered as measures to improve health, these fiscal measures form part of a strategic response that together impact on the known health and social harms.</p>

	Findings	Comments
2	<p>There is a lack of clear statistical evidence showing the impact that rises in impôts duties have on consumption of alcohol and tobacco.</p>	<p>Meta-analysis of 112 research studies on the link between taxes and price and alcohol consumption: http://onlinelibrary.wiley.com/doi/10.1111/j.1360-0443.2008.02438.x/full</p> <p>Systematic review of 50 research studies on impact of price of alcohol on alcohol-related disease, traffic crash deaths, sexually transmitted disease, violence and crime: http://ajph.aphapublications.org/doi/abs/10.2105/AJPH.2009.186007</p> <p>Global research and policy advice: https://www.ncbi.nlm.nih.gov/pmc/articles/PMC3860576/ http://www.who.int/mediacentre/factsheets/fs349/en/ http://www.oecd.org/health/oecdoutlinesactionforgovernmentstotackheavycostofharmfuldrinking.htm</p> <p>The relationship between alcohol taxes and binge drinking: http://onlinelibrary.wiley.com/doi/10.1111/add.12818/abstract</p> <p>Relationship between small increases in tax above inflation on violence-related injuries in England and Wales. http://injuryprevention.bmj.com/content/early/2016/06/16/injuryprev-2015-041884.abstract</p> <p>Relationship between alcohol tax policies and health inequalities. https://www.ncbi.nlm.nih.gov/pubmed/26905063</p> <p>When taken alongside the considerable scientific evidence of pricing impact, our own local evidence of <i>per capita</i> consumption alongside above-inflation impôts duties appears to support the idea that Islanders' alcohol consumption levels are similarly influenced by price mechanisms. https://www.gov.je/SiteCollectionDocuments/Health%20and%20wellbeing/R%20Alcohol%20Profile%202015%2020151112%20MC.pdf</p> <p>Much of the evidence presented above links price and consumption having impact on younger people. Locally, we are able to identify, similarly to other jurisdictions, that with above-inflation rises alongside other strategic measures, that both self-reported alcohol consumption and tobacco consumption have steadily fallen amongst school-age children and young people over the same periods. This is particularly important in delaying unhealthy behaviours and setting healthier behaviours as our Islands young people grow into a healthier adulthood. https://www.gov.je/SiteCollectionDocuments/Government%20and%20administration/R%20A%20Picture%20of%20Health%20Jersey%202014%2020150302%20HL.pdf</p> <p>Price and tax measures are an effective and important means of reducing tobacco consumption by various segments of the population, in particular young persons.</p>

	Findings	Comments
		<p>http://www.who.int/tobacco/publications/economics/tax_administration/en/</p> <p>Smokers are no different to other consumers when spending money: price dominates decision-making. Consequently, increasing the price of tobacco through taxation remains the single most effective way of reducing smoking rates (Wilson L.M., Tang E.A., Chander G., <i>et al</i> 2012) Impact of tobacco control interventions on smoking cessation, and prevalence: a systematic review. <i>Journal of Environmental and Public Health</i> Article ID 961724.</p> <p>Economic models show that a 10% increase in price leads to a 4% drop in smoking prevalence across the population, with higher quit rates among lower-income smokers and younger smokers (Jha & Chaloupka, 2009). <i>Curbing the epidemic: Governments and the economics of tobacco control</i> World Bank.</p> <p><u>Additionally, it should be borne in mind that the Economics and Statistical Departments of the World’s largest Treasuries calculate the price-elasticity of demand for excisable goods such as alcohol and tobacco. These calculate the relationship between price increases and demand. It would be disproportionately expensive for Jersey to attempt such analysis. However, we can conclude from available data that Jersey has not yet reached the tipping point where a duty-increase not only generates reduced demand but also reduces States revenues.</u></p>
3	<p>The purpose of fuel duty is not solely to cover road maintenance costs.</p> <p>Both fuel duty and Vehicle Emissions Duty are levied for environmental reasons.</p>	<p>The purpose of fuel duty – like all impôts duties – is primarily to raise revenue to pay for Jersey’s public services. Excise duties – especially for alcohol and tobacco – have been charged by Governments across the globe for centuries. In recent decades, Governments have become more aware of the environmental, health and social costs of alcohol, tobacco and vehicle emissions and have taken those factors into account when affecting price levels through duty increases.</p> <p>In economic terms, it is rational for Governments to try to “internalise” (i.e. recover) some of the “external” costs (e.g. healthcare, atmospheric pollution) of consumption of certain goods where markets do not automatically adjust for those external costs. In the absence of government intervention, consumers do not face prices which reflect more accurately the costs of consuming particular goods, and this will mean those costs are borne by Society as a whole.</p>
4	<p>A total of £103 million will be withdrawn from returns on the Strategic Reserve between 2016 and 2019.</p>	<p>The proposals for withdrawals from the Strategic Reserve were agreed by the States in P.76/2015. The total amounts have not changed, except for the additional £16 million which may be required following the slight reduction in income forecasts after BREXIT. The use of the Strategic Reserve in the short term, as the economy recovers and sustainable measures are phased-in, is in line with the advice of the FPP and should protect the economic recovery in the short term.</p>

	Findings	Comments
5	Capital expenditure is largely being funded from the Strategic Reserve while the States work towards returning to a budgeted surplus in 2019.	The use of the Strategic Reserve in the short-term, as the economy recovers and sustainable measures are phased-in, is in line with the advice of the FPP and should protect the economic recovery in the short term. Of the £168 million capital programme, it is currently proposed that £82 million, or just less than 50% of the capital programme, is funded from the Consolidated Fund.
6	The proposals in the Budget to introduce reporting for all companies on a 0% tax rate could lead to the introduction of some form of taxation on those companies. This could be similar to the “Tesco Tax” in the Isle of Man.	The Minister for Treasury and Resources first mooted the possibility of applying higher rates (i.e. higher than 0%) of corporate income tax to some businesses in 2015, and work will continue through 2017 with a view to bringing forward proposals in the Budget 2018.
7	There is no evidence yet of a coherent plan to fund the gap left by the rejection of the health charge; however a revised version of the health charge is not under consideration.	<p>The Council of Ministers has been clear that “future revenue-raising measures” will be brought forward to replace the funding from the Health Charge for 2018 and 2019, in advance of the Budget 2018.</p> <p>These “revenue-raising measures” will include consideration of the distributional impacts of such proposals. As noted above, part of this additional revenue may be raised by applying higher rates of corporate income tax to some businesses.</p> <p>After the rejection of the income-based Health Charge, the Treasury will continue to work to identify options for a long-term, sustainable funding mechanism for Health for consideration during the next MTFP period 2020–2023.</p>
8	The Panel’s advisers consider that the revised income forecasts used in the Budget are still optimistic and do not reflect current levels of uncertainty.	<p>The income forecasts for the original MTFP 2016–2019 (June 2016) included an assessment of future uncertainties. The final MTFP Addition forecasts were reduced slightly following the revised economic assumptions from the FPP in August 2016 which were adjusted to reflect the uncertainty created by the UK referendum result. The FPP did highlight that the “impact of the referendum on the Jersey economy is still very uncertain and is likely to remain so at least until negotiations are complete”. However, they provided a central projection, which was their independent assessment at that time of the most suitable economic assumptions to use.</p> <p>The Draft Budget 2017 also includes comparisons of the economic assumptions (August 2016) used in the Budget forecasts against those current at the same time for the UK. These show that in general the economic assumptions used are either in line or less optimistic than those used in the UK.</p>

	Findings	Comments
		The forecasts are presented as the central point of a range, but current reports suggest that 2016 States revenues should achieve those forecasts.
9	Productivity in the economy has fallen by 20% since 2000.	<p>This was highlighted in the Draft Budget 2017 and is not a new development. More recently, productivity in Jersey (as measured by GVA per full-time equivalent employee) declined slightly in 2015 (by 0.2%). However, this was made up of an increase of 3% in non-finance sectors and a decrease of 4% in finance (driven by the fall in profitability).</p> <p>Jersey is not alone in experiencing weak productivity trends, as there has been a sustained worldwide slowdown in productivity since the financial crisis, and raising it is the central long-term economic challenge. Productivity determines living standards in the long term, and improving it is the key to increasing wages. As well as investing in health, education and infrastructure as set out in the MTFP Addition, the Strategic Plan sets out how the Council of Ministers aims to rectify this productivity performance and optimise economic growth.</p>
10	The actual balance on the Consolidated Fund is distorted by the upfront approval of funding for capital projects.	The unallocated balance on the Consolidated Fund is prepared for Annual Budgets and MTFPs in accordance with the Finance Law to ensure that the Fund is not over-committed. The actual cash balance on the Consolidated Fund, which is much higher and includes allocated but unspent capital budgets, is reported each year in the States Annual Report and Accounts. The Minister is aware that the Panel does not favour change to the existing arrangements, but nevertheless the Treasury will continue to consider options to bring forward such change.
11	It is not clear how the States intends to fund the payment of Parish rates on States properties.	<p>The changes to the Rates (Jersey) Law 2005 required to facilitate the States' payment of rates was rejected by the States during the debate of the Draft Budget 2017.</p> <p>The Minister for Treasury and Resources had committed to work with the Connétables and bring forward proposals for the funding of the States' payment of rates.</p> <p>Further work will now be required with the Connétables during 2017 to agree how to progress the payment and funding of the States' payment of rates, which remains a priority from the Strategic Plan, ahead of the Budget 2018.</p>

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
				<p>Customs Officers will continue to consult with Health officers over increases in alcohol and tobacco duties and their impact on importation levels.</p> <p>The Treasury will continue to work to identify a sustainable funding mechanism for Health after the rejection of the income-based Health Charge, but does not consider the hypothecation of impôts duties a sustainable option.</p>	
2	A proportion of Fuel Duty should be hypothecated for road maintenance costs. VED is levied for environmental reasons and should be hypothecated for environmental projects.	T&R	Reject	Impôts duties are part of general taxation that supports the funding of all public services. As noted above, as a matter of principle, the Treasury does not support hypothecation of taxes except in certain specific cases. There are currently no plans for the direct hypothecation of existing impôts duties for health, environmental or road-surfacing budgets.	N/A
3	Once States' budgets have returned to surplus, the capital expenditure programme should be funded in full through annual depreciation. Further work should be carried out by the Department for Treasury and Resources to establish the best way of ring-fencing depreciation in order to achieve this.	T&R	Accept in principle for ordinary capital items	<p>The current financial plan for a return to broadly balanced budgets by 2019 includes a capital allocation broadly equivalent to the annual depreciation level. However, there will always be a need for additional funding strategies for certain Major Projects such as the hospital.</p> <p>Work continues towards potential changes to the capital allocation and approvals process to bring this more in line with the cash flow of capital projects.</p> <p>The Treasury will explore a number of options, including depreciation, before recommending changes to the Finance Law.</p>	<p>From return to surplus</p> <p>Draft Budget 2018</p> <p>October 2017</p>

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
4	Any further tax increases or charges considered by the Minister for Treasury and Resources in the future must take into account the considerable additional burden placed on personal taxpayers in recent years and be supported by reliable evidence and impact assessments.	T&R	Accept	<p>An extensive distributional analysis was provided for the revenue-raising measures contained in the MTFP Addition (in particular the Health Charge proposals).</p> <p>A Review of Personal Income Tax data has been commissioned – to help explain how tax changes since 2007 have affected Islanders across the different income groups. This will include analysis with respect to the proposed commercial waste charges. The Review began in October and is being overseen by a Steering Group of Ministers and other members of the States Assembly.</p> <p>Future tax changes (as has been the case with previous tax changes) will include consideration of the distributional impacts of such proposals. It is the Minister’s intention that the “future revenue-raising measures” to replace the funding from the rejected Health Charge will include options to increase the tax liability of companies.</p>	<p>Draft Budget 2018</p> <p>October 2017</p>
5	The Department for Treasury and Resources should undertake work to analyse the reason for the fall in productivity in Jersey’s economy over a period when the population has grown consistently, in order to identify ways that productivity can be increased.	T&R	Accept in principle	<p>The Council of Ministers have already given very high priority to boosting productivity in light of the trends in Jersey in recent years. As well as investing in health, education and infrastructure as set out in the MTFP Addition, the Strategic Plan sets out the Council of Ministers’ priorities for policy going forward in order to increase productivity. In particular –</p> <ul style="list-style-type: none"> • promoting jobs and growth in the technology sector, with a particular focus on Fintech • delivering and further enhancing the existing Financial Services Policy Framework • promoting higher productivity in all economic strategies, including the new Tourism, Retail and Rural Economy Strategies • developing a new and challenging Enterprise Strategy, a new Innovation Strategy and attracting more inward investment 	Ongoing

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
				<ul style="list-style-type: none"> • reviewing and upgrading the existing Skills Strategy • developing a new Competition Framework and reviewing opportunities to promote competition • identifying and addressing barriers to work for key groups • adopting environmental management principles to help improve productivity and efficiency and attract environmental businesses in line with our economic growth objectives. <p>In addition, the MTFP provides investment in an Economic and Productivity Growth Provision, which is intended to drive growth and productivity across the whole economy.</p> <p>These are the priorities for productivity policy and where Treasury and Resources believe resources can be used most effectively. Particularly as the FPP did substantial analysis of Jersey's economic performance in its 2015 Pre-MTFP Report (https://www.gov.je/SiteCollectionDocuments/Government%20and%20administration/R%20Fiscal%20Policy%20Panel%202015%20annual%20report%2020150130%20JE.pdf) including productivity trends. It concluded that trends over the recent economic cycle were a result of the fall in financial services productivity (driven by the fall in banking profitability).</p>	
6	The treatment of capital allocations within the Consolidated Fund should be changed to better reflect the actual profile of expenditure and to provide clarity on unspent amounts and unallocated funds.	T&R	Accept	<p>Work continues towards potential changes to the capital allocation and approvals process to bring this more in line with the cash flow of capital projects.</p> <p>The Minister is encouraged that following the advice from CIPFA, the Panel is now more inclined to be supportive of a change in approach to capital funding.</p> <p>This may require changes to the Finance Law and once proposals are developed, the Treasury will share these with the Panel.</p>	<p>Draft Budget 2018</p> <p>October 2017</p>

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
7	Forecasts for the Consolidated Fund included in future budgets and MTFPs should be accompanied by an analysis of unspent capital allocations.	T&R	Accept	<p>An analysis of the unallocated Consolidated Fund balance which identifies unspent capital and other unspent allocations is provided in the Annual Report and Accounts each year (<i>see</i> page 220 of the Financial Report and Accounts 2015).</p> <p>The forecast unspent capital balance could be provided alongside capital forecasts if appropriate.</p>	<p>Draft Budget 2018</p> <p>October 2017</p>
8	Consideration should be given to requiring departments to re-apply annually for funding for capital projects which have not commenced.	T&R	Accept in principle	<p>Work continues towards potential changes to the capital allocation and approvals process to bring this more in line with the cash flow of capital projects.</p> <p>The Minister is encouraged that following the advice from CIPFA the Panel is now more inclined to be supportive of this approach.</p> <p>This may require changes to the Finance Law and once proposals are developed, the Treasury will share these with the Panel.</p>	<p>Draft Budget 2018</p> <p>October 2017</p>
9	The States should not proceed with the payment of Parish rates until a funding mechanism has been found.	T&R	Accept	<p>The changes to the Rates (Jersey) Law 2005 required to facilitate the States' payment of Rates was rejected by the States during the debate of the Draft Budget 2017.</p> <p>The Minister for Treasury and Resources had committed to work with the Connétables and bring proposals for the funding of the States payment of rates.</p> <p>Further work will now be required with the Connétables during 2017 to agree how to progress the payment and funding of the States' payment of rates, which remains a priority from the Strategic Plan, ahead of the Budget 2018.</p>	<p>Draft Budget 2018</p> <p>October 2017</p>

CONCLUSION

The Minister looks forward to further constructive dialogue with the Panel on all tax and spending matters.