

Corporate Services Scrutiny Panel

Second Report

Goods and Services Tax Review



Presented to the States on 4th April 2007

S.R.7/2007

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Introduction

Panel membership

The Corporate Services Scrutiny Panel is constituted as follows –

Deputy P. J. D. Ryan, Chairman
Senator J. L. Perchard, Vice Chairman
Connétable J. Le Sueur Gallichan
Connétable D. J. Murphy
Deputy C. H. Egré

Officer support: Mr M. Haden and Miss S. Power

For the purposes of this review the Panel formed a Sub Panel, which was constituted as follows –

Deputy P. J. D. Ryan, Sub Panel Chairman
Connétable J. Le Sueur Gallichan
Connétable D. J. Murphy
Connétable M.K. Jackson

Independent expert adviser

The Panel engaged the following adviser to assist it with the review –.

Mr. Richard Teather, BA, ICAEW, a senior lecturer in Tax Law at Bournemouth University; a Freelance Tax Consultant and a writer on Tax Law and Policy.

Terms of reference

The Panel adopted the following terms of reference for its review:

To review the draft law to implement a Goods and Services Tax in Jersey (R.28/2006), together with the draft Regulations, particularly in respect of -

- i. The anticipated yield from a broad based tax set at 3%
- ii. The proposed 'zero ratings' and 'exemptions'
- iii. The impact of potential additional exclusions (such as basic foodstuffs and children's clothes) on the anticipated yield
- iv. The statutory provision for relief for certain specific groups of consumers (such as charities)
- v. The treatment of the financial services industry
- vi. The resource implications for the Income Tax and Customs departments

To review the impact of the draft Goods and Services (Jersey) Law 200- and the forthcoming Regulations on consumers and the business community.

To review the responses received by the Treasury and Resources Minister in respect of the public consultation both on the primary law and the regulations.

To report to the States before the States debate on the draft legislation.

Interim Report

The Sub Panel prepared an Interim Report in order to inform the States debate, scheduled for 24th October 2006, on Senator S. Syvret's proposition entitled: Goods and Services Tax: Exempt or Zero-rated Items (P.86/2006).

The Interim Report dealt with the following aspects of the GST scheme which were relevant to the debate on 24th October 2006

- i. The anticipated yield from a broad based tax set at 3%
- ii. The proposed 'zero ratings' and 'exemptions'
- iii. The impact of potential additional exclusions (such as basic foodstuffs and children's clothes) on the anticipated yield
- iv. The statutory provision for relief for certain specific groups of consumers (such as charities)

Key Findings

1. We acknowledge that the overall exemption for charities, combined with a method of reclaiming tax incurred on expenses, represents a considerable concession by the Treasury and Resources Minister. Jersey's arrangements for charities will be among the most generous of all the jurisdictions studied by the Sub Panel. (paragraphs 7 & 8)
2. The question of charities running commercial enterprises and activities as part of their fundraising activities is a difficult issue to resolve. As an increasing number of charities develop new fundraising strategies to maximise their income this point will need to be monitored. (paragraph 11)
3. We welcome the fact that the Education and Home Affairs Scrutiny Panel has agreed to review the Early Years Strategy. (paragraph 27)
4. We are concerned that the effect of GST on childcare provision does not appear to have been fully considered by the Early Years Strategy Review Group. (paragraph 28)
5. We believe that it is unacceptable for some private childcare provision to be subject to tax while a situation remains in which the States is unable to offer a facility for universal free entitlement for 3 to 4 year olds. (paragraph 28)
6. We welcome the exemption for residential and nursing homes. This exemption will have a significant benefit for individuals and families already paying high costs for the care of elderly relatives. (paragraph 30)
7. We welcome the fact that the Minister has accepted our recommendation not to zero rate extensions, improvements, maintenance and repair of domestic housing. (paragraph 44)
8. We find it disappointing that legal issues should have been raised at a late stage in finalising the draft legislation. We question why attention was not drawn to any legal problems with drafting at an earlier stage, and the length of time it took to resolve the issues once they were raised. (paragraph 54)
9. We also find it disappointing that the Treasury's financial forecasts have until very recently continued to include a full year's revenue from GST in 2008, based on the assumption that the law would be introduced in January 2008. Clearly this delay will cause a significant loss in revenue in the first year of the introduction of the new law. (paragraph 55)
10. Unlike GST the effects of Zero/ten and the creation of the 'Black Hole' will not be postponed. We believe that it may be in the best longer term interest of the Island not to limit the Minister's ability to respond to the fiscal circumstances which will arise following the introduction of zero/ten as part of his December 2010 (for 2011 fiscal year) budget planning process as was envisaged before the delays to the start of GST became apparent. (paragraph 68)
11. We believe that the arguments in favour of a margin scheme for used cars are convincing. (paragraph 108)

12. We intend to report on further discussions with the Financial Services Industry in the next stage of our review when we consider the proposed Regulations. (paragraph 121)
13. We welcome the assurance that the Commission of Appeals will continue to act in a manner which is consistent with existing Jersey principles and procedures. (paragraph 146)

Recommendations

1. A review of the definition of charitable status should be undertaken by the **Income Tax Department**. Consideration should be given to a requirement for a charity to be of public benefit in order to qualify for exemption from GST. (paragraph 14)
2. **Jersey Law Commission's** proposal for a Charities Commission should be progressed with some urgency, and even if no change is made in the definition of a charity there should be an independent review of the status of existing approved charities. (paragraph 15)
3. The **Treasury and Resources Minister and the Education, Sport and Culture Minister** should work towards an urgent resolution of the problem of inequity in childcare provision before the introduction of GST in 2008. (paragraph 28)
4. Assurances we have been given about the pragmatic and non prescriptive approach of the Tax Office should be made explicit in guidance notes on the operation of the law. (paragraph 89)
5. A review of the operation of the GST scheme should be undertaken by the **Corporate Services Panel** in two or three years' time. (paragraph 90)
6. A margin scheme for the used car market should be introduced via Regulations. (paragraph 108)
7. The **Treasury and Resources Minister** must consider the needs of on-Island businesses as well as the Tax Office's costs when setting a de minimis level for the value of imports (paragraph 127)
8. Early action should be taken by the **Treasury and Resources Minister** to strengthen the constitution of the Commissioners of Appeal to enable it to respond quickly to any problems that may arise during the implementation of GST. (paragraph 140)
9. In the early stages of the introduction of GST, market forces should be allowed to determine whether or not prices are marked inclusively or exclusively. (paragraph 160)
10. The distinction in the draft law between residential rentals (which are zero-rated) and holiday lets (taxable) should be amended to take account of practice in the non-qualified residential sector. (paragraph 167)

Proposed Amendments to the Draft Law

We propose amendments to the following articles of the draft law in order to bring about the change specified below

1. **Article 8(4)** - to bring forward the date on which the Treasury and Resources Minister might vary the general rate of GST. (See paragraph 68 of our report)
2. **Article 41(2)** - to specify in Regulations the powers of the Comptroller to determine the evidence required to claim input tax credit to be specified in Regulations (paragraph 91)
3. **Article 51(2)** - to allow GST to be reclaimed in the case of a conversion of a non-residential property (such as a barn) to residential use (paragraph 47)
4. **Article 88(4)** - to reduce the level of penalty to international norms (paragraph 151)
5. **Article 89(3)** - to reduce the level of penalty to international norms (paragraph 151)
6. **Article 92(1)** - to redefine the liability of a director, manager or other officer (paragraph 155)
7. **Article 7 of Schedule 8** - to restrict the circumstances in which the power of entry to business premises can be exercised (paragraph 96)

Developments since the Interim Report

1. The Corporate Services Panel presented the Interim Report (SR6/2006) of its GST Sub Panel to the States on 18th October 2006 in advance of the debate on Senator's Syvret's proposition on exempt and zero-rated items (P.86/2006).
2. In our Interim report, we studied the potential impact of the tax on various sectors of the community and found that the effect of zero rating a range of essential items, including basic foodstuffs, as proposed by Senator Syvret, would give relatively little benefit to the average low income household. We concluded that the Income Support scheme would, if it matched expectations, provide a greater level of protection to low income households. We found therefore that we could not support the Senator's bid to introduce a range of exemptions and zero-ratings.
3. We also commented on a number of other areas where the potential impact of GST was onerous and made some recommendations for modification or reconsideration. Below, we examine the Minister's response to our recommendations and other developments which have taken place since the debate in November.

Charities

4. We heard evidence in public hearings from a number of the larger organisations on the Island, such as Family Nursing and Home Care, Hospice and Mencap, who were concerned that the tax would increase their problems in fund raising and create difficulties for vulnerable people in our community. In response we carried out an in-depth study of the potential impact of GST on the income and administration costs of a selected number of major charities. In September we arranged a public meeting in Trinity bringing together the Treasury Minister and many of the Island's charities. We welcomed the Minister's public commitment to giving charities favourable treatment under the GST law, recognising the immense contribution these organisations make to our community.
5. We are delighted that the Minister has responded so positively to our recommendation. Under Schedule 5 article 5 of the draft law the supply of any goods and services by a recognised charity shall be exempt.
6. In addition, charities will benefit from a 'pay and claim' system under which they will be able to recover tax on their business expenditure. This will be covered under a general provision in the law which allows the States to refund input GST in circumstances prescribed in Regulations (article 56).
7. **We acknowledge that this overall exemption for charities, combined with a method of reclaiming tax incurred on expenses, represents a considerable concession by the Treasury and Resources Minister.** The solution avoids the complexities of the treatment of charities in the United Kingdom VAT system^[1] for both the Tax Office and the charities. Although there will inevitably be some increased administrative burden for charities in accounting for the pay and reclaim system the benefit is likely to outweigh any disadvantage.

8. **Jersey's arrangements for charities will be the most generous of all the jurisdictions studied by the Sub Panel**^[2]. It meets the objectives of groups such as the Charities Tax Reform Group^[3] in the United Kingdom and elsewhere in Europe, which have been campaigning strongly to remove heavy financial burdens suffered by charities from VAT.
9. The cost of this concession in reduced revenue to the States is estimated to be in the region of £0.5 million per annum^[4]. The Minister told us that this would be compensated by increased revenue from the application of GST to maintenance and repairs of domestic housing. This amendment had been brought about as a result of another of the recommendations in our Interim Report (see paragraph 44 below).
10. Among the organisations to benefit from the concession to charities will be **Durrell Wildlife Conservation Trust**. Durrell is an important visitor attraction in the island and is in direct competition with all the other visitor attractions. Its admission, restaurant and retail sales would normally be liable to GST. These commercial activities are crucial in supporting Durrell the charity and this organisation had claimed in evidence to the Sub Panel that GST on its business activities could undermine the confidence of their benefactors and threaten the viability of their continued presence in the Island.
11. The general question of charities running commercial enterprises and activities as part of their fundraising activities is a difficult issue to resolve. Charities might be seen as gaining an undue advantage, through their exemption from the tax, over normal commercial businesses. It may be that there are relatively few charitable organisations in Jersey which are large enough in scale to compete on a commercial basis. **However, as an increasing number of charities develop new fundraising strategies to maximise their income this point will need to be monitored.**
12. A charity is defined for GST purposes by reference to corporations, associations or trusts recognised by the Income Tax Office. The criteria used by Income Tax for recognition of charities are based on a standard interpretation of 'purpose' under four activity headings (poverty, education, religion, and benefit to community).
13. The total number of bodies recognised by Income Tax as charities extends considerably beyond the 288 public charitable bodies which are registered members of the Jersey Association of Charities. We understand that there are many organisations whose status has not been reviewed by Income Tax for many years.
14. **We believe that a review of the definition of charitable status should be undertaken by the Income Tax Department and that consideration should be given to a requirement for a charity to be of public benefit in order to qualify for exemption from GST.**
15. The Jersey Law Commission has recently published a revised consultation paper on possible reform and modernisation of the Law of Charities including the establishment of a non-governmental Charities Commission or a Charity regulator which would take over the role of assessment of charitable bodies from the Comptroller of Income tax^[5]. This issue has been under discussion for some time without to date reaching a

conclusion. **In our view, the proposed treatment of charities under GST lends further weight to the arguments in favour of this reform and we believe that the proposal for a Charities Commission should be progressed with some urgency. Furthermore whatever the outcome of the reviews in paragraphs 14 & 15 above, the Panel recommends that a review of the organisations that currently benefit from charitable status be undertaken.**

Education

16. A high number of submissions were received during the first stage of our review from parents with children at the three Church schools^[6] in the Island, drawing attention to the important contribution made by these schools, including considerable financial savings to the States, due to parents opting for fee-paying education. We did not support their call for exemption but recommended that the relevant Ministers undertake a review of the grants for non-states Schools.
17. As a consequence of the exemption of charities the Island's fee-paying Church schools, as well as other institutions registered as charities, including St George's and St Michael's, will now be exempt from GST. Thus, by indirect means, the concerns over the impact of GST on school fees will have been resolved.
18. Based on a combined estimated annual fee income for 2007 of approximately £9.9 million^[7] this exemption will mean a gross loss of 'output' tax to the States of approximately £297,000. The schools will also be entitled to recover non-staff related expenses (cost unknown).
19. It is understood by the Sub Panel that States fee paying schools, Victoria College and Jersey College for Girls will still be liable for GST. This clearly is inequitable with regard to the parents at those schools who will have to bear the tax. We understand that the matter has been under discussion between the Minister of Education, Sport and Culture and the Treasury and Resources Minister and that Senator Vibert is seeking exemptions provided for under Part 4, Article 20 (f) and/or (g) of the GST Law in order to provide equity.
20. **We would support an equitable solution which would restore parity for all fee-paying parents while preserving the benefit to the charitable educational institutions.**

Childcare

21. We heard evidence in the first stage of our review regarding the current inequalities in the provision of childcare in the Island. We were told that the introduction of GST would only enhance existing inequities in childcare provision at a time when the Council of Ministers Working Group for 0 - 5 year olds was striving to improve access for working parents to more affordable childcare^[8].

22. We have noted that the arrangements granted to charities will further increase the inequities in childcare provision. There are currently 755 Charitable and 960 Non-charitable registered childcare places (not including ESC Activity Clubs - number of registered places unknown) in a total of 33 providers in the Island^[9].
23. Subsequent to our Interim report, in December 2006, the Education, Sport and Culture Minister published the progress report of the Working Party^[10]. This Group had been tasked to consider ‘*appropriate arrangements for financial support for parents and carers of this age group, including benefits and tax allowances.*’ The group examined the impact of Child Care Tax Relief and Child Care Allowance schemes. However, no major recommendations regarding changes to these benefits were made due to the group not wishing to jump ahead of the new Income Support System. We note that no specific consideration was given to the potential impact of GST. The Review Group simply recommended that the relevant Departments ‘*monitor impact of Income Support and tax relief for families with children of 0-5 years and assess the effectiveness of these benefits in facilitating access to early education and care.*’
24. A more positive proposal to emerge from the Review Group was for free entitlement to 20 hours per week, 38 weeks per year for all three to four year olds. It is intended that this would be achieved through investment in private sector provision to complement States provided nursery classes. This initiative would be a major step in removing significant inequity in our community.
25. The Minister for Education, Sport and Culture has targeted September 2008 for the commencement of this scheme. However, whilst the proposal has been supported in principle by the Council of Ministers, funding has not been identified within the current total of cash limits so progress remains uncertain for the present.
26. The Jersey Early Years Association commented:
- JEYA feel very strongly that this has not been considered in the depth that the situation deserves and that GST will create discrepancies within private sector provision.... An even greater inequality will exist between GST nurseries and States Nurseries. Not only will those parents unable to get a place at a school nursery need to pay fees, they will also have to pay tax on those fees.*
27. We recognise in our Interim report that there were complex social and funding issues which were beyond the remit of our review. We recommended therefore that the Social Affairs Scrutiny Panel (now the remit of the Education and Home Affairs Panel) should prioritise a study of the outcome of the Strategy review group in their work programme for 2007. **We welcome the fact that this recommendation has been accepted by the Panel.**
28. **We are concerned that the effect of GST on childcare provision does not appear to have been fully considered by the Review Group. We believe that it is unacceptable for some private childcare provision to be subject to tax while a situation remains in which the States is unable to offer a facility for universal free entitlement for 3 to 4 year olds. We urge the Treasury and Resources Minister and the Education, Sport and Culture Minister to work towards an urgent resolution of**

this problem before the introduction of GST in 2008.

Residential and Nursing Homes

29. At the time of our Interim report we were awaiting clarification of the treatment of this sector from the Treasury
30. We note that Schedule 5 article 5 of the draft law excludes the supply of any goods and services to patients or residents in a registered Nursing or Residential Home. **We believe that this is a sensible exemption. It will have a significant benefit for individuals and families already paying high costs for the care of elderly relatives.**

Healthcare

31. During the first stage of our review the Social Security Minister announced that the impact of GST on doctors' fees and prescription charges would be absorbed by the Health Insurance Fund. We expressed concern that this approach might not be sustainable in the long run.
32. We welcomed the announcement by the Minister during the States debate in October 2007 that he would review the position regarding medical goods and services, including exemption for doctors, dentists and opticians.
33. We note that Schedule 5 Article 4 of the draft Law provides that goods and services provided by registered health professional will be exempt. We understand therefore that the following registered professional groups will be exempt :

- Doctors,
- Dentists,
- Opticians:
- Ambulance paramedics
- Biomedical scientists
- Chiropodists
- Chiropractors
- Clinical psychologists
- Clinical scientists
- Dietitians
- Midwives
- Nurses
- Occupational therapist
- Orthoptists
- Osteopaths
- Physiotherapists
- Psychotherapists
- Radiographers

Specialist community public health nurses
Speech and language therapists

34. The above list covers virtually all healthcare services. However we note that

Homeopathic treatment is not registered in Jersey and is therefore liable in theory to GST charges, but only if care was provided through a business with a turnover above the £300,000 GST-registration threshold.

Also not included in the above list, are a number of professionals including art therapists, prosthetists and orthotists and hearing aid dispensers. However, we believe that it is most likely that such professionals would be working within the public health services. If providing private healthcare, they would be liable to charge GST on their services only if they were involved in a business with a turnover above the £300,000 GST-registration threshold.

35. Goods and services provided by vets will not be exempt from GST.

Prescribed medicines

36. We note that under Schedule 6 article 3 prescribed medicines will be treated as zero-rated supplies. This will make little practical difference to consumers, as previously the Social Security Minister had undertaken to cover the costs of GST through the Health Insurance Scheme.

37. We note that non-prescription medicines and pharmaceutical products provided over the counter, such as pain relievers, cough medicines, vitamins and stop-smoking products, will still be subject to GST.

The Arts Trust

38. The Arts Trust in its submission to the GST consultation asked for special treatment under GST for the Arts and artists on the grounds that they provided an essential contribution towards quality of life and economic development. We did not support this view in our Interim Report but said that their concerns should be addressed by supportive strategic initiatives in conjunction with the Economic Development Department, rather than by exemption.

39. In response to this recommendation the Economic Development Department commented:

Jersey Arts Trust receives indirect financial support from the Economic Development Department each year as they are invited to organise the programme of street entertainment and other theatrical performances which are paid by this Department. The current budget for these activities stands at £50,000 p.a. As the majority of the funding for the Jersey Arts Trust is received from Education, Sport and Culture it would perhaps be inappropriate for us to comment on that. However,

we are aware of a number of diverse artistic activities which are flourishing within the Island, supported by the Arts Trust. There is no evidence to suggest that GST would have any great effect on these activities.

40. In the Summary of Responses to Public Consultation prepared by Crown Agents it was reported that *'the views of the Arts Trust remain under consideration.'* The Sub Panel asked the Treasury and Resources Minister on 2nd March for his current view. He responded that it might be possible to consider the underlying activities of the Arts Trust as a charity. However, he considered that it was appropriate that commercial productions taking place in premises provided by the Arts Trust would be liable to GST.
41. We understand that the GST Director will enter into further discussions with the Arts Trust in the near future.

Tourism

42. In its evidence to the Sub Panel the Jersey Hospitality Association argued for exemption for the industry as a whole on the grounds that it was an export industry and also separately for conference business. The Sub Panel did not support this proposal but recognised that the tourism industry might require further support from the Economic Development Department in terms of developing strategic initiatives
43. In response the Economic Development Department commented:

In general the exceptions for operators within the industry were not supported by the Department mainly because of the difficulties in administration. We also recognised the importance of tax being generated through spend within the tourism industry contributing to the overall States revenue stream.

The industry has for a long period of time been very well supported by government in Jersey through significant investment by the tourism department itself for marketing purposes and also in more recent years by the Tourism Development Fund. The Jersey Hospitality Association has benefited from a number of extremely favourable arrangements with the department including running the outsourced Bien V'nue scheme and the opportunity each year to publish a highly profitable advertising magazine.

It is clearly not possible to separate conference expenditure from other forms of tourism expenditure and therefore not possible to exempt the conference industry. As a result of the huge investment in hotels and other facilities within the island, we anticipate that conference tourism will continue to grow and not be affected by the implementation of GST at 3%.

Housing

44. For the Interim report we commissioned a study of the potential impact of GST on domestic housing. We accepted the Treasury's position that new build domestic

properties should be zero-rated but questioned the proposal to zero-rate extensions, improvements, maintenance and repair, as we felt that zero rating these items would have been inconsistent and unfair when the line was held so firmly against zero rating in general. **We welcome the fact that the Minister has accepted our recommendation.**

45. Article 51(2) specifies that refunds of GST will not be allowed on 'the alteration, conversion, enlargement, improvement, reconstruction or repair of an existing building' and 'the making of an extension'

46. We estimated that the potential revenue gain from applying GST to repairs and maintenance alone would be £0.6 million^[11]. The Minister said that this additional revenue will compensate for the revenue foregone through the exemption for charities.

47. We question one element of Article 51(2). We believe that conversion of a non-residential building (such as a barn) to residential use is the equivalent of new build and should have the same GST treatment. If GST is payable on the supply of goods relating to the conversion of an existing property we foresee the possibility that developers would find it more economical to demolish rather than take the trouble to convert the existing structure . **We therefore intend to seek an amendment to the draft law to delete the word 'conversion' from Article 51(2)(a).**

Issues identified in the Draft Law (P.37/2007)

48. In this section of the report we examine specific articles in the draft law. We highlight a number of provisions in the draft law where we have sought clarification. In certain cases, we have decided to seek an amendment to the draft legislation

Legal technical issues

49. The Minister advised the Sub Panel on 27th December 2006 that he was facing some legal technical issues made by the Attorney General on the drafting detail of the Law.

50. The Minister advised the Sub Panel in the public hearing on 2nd March 2007:

'The Attorney General was asked to take further advice, which he did.'

51. The Sub Panel subsequently discussed the issue in detail with the Attorney General in private session on 2nd March 2007.

52. As a consequence of the time taken to resolve this matter, progress on finalising the draft law was delayed for approximately four months and the projet was lodged on 6th March 2007, whereas lodging had previously been expected in the fourth quarter of 2006. The Law was then scheduled for debate in April with the introduction of the tax timed for the end of April 2008 allowing for a period of twelve months for educational and registration visits to take place.

53. The Minister acknowledged that this delay would lead to a loss in revenue from GST in the first year. Instead of a full year's revenue of £45 million, there would be a loss of approximately £15 million. He commented:

I am concerned that there has been tax loss and a time delay but I am more than reassured that we have a law which is fit for purpose. I should hate to find that I have got maybe not £15 million worth of revenue but £50 million or £500 million worth of revenue which I suddenly find has not been collected legally and I have a real problem in my hands. So it is an irritation, if you like, that the delay may have cost us £15 million but I am far more interested in getting a law, which is going to go on the statute book no doubt for many years to come, right to start with.

54. We find it disappointing that legal issues should have been raised at such a late stage in finalising the draft legislation and question why attention was not drawn to this matter at an earlier stage. We also question the length of time it took to resolve the issue once it was raised. Clearly this delay will cause a significant loss in revenue in the first year of the introduction of the new law. We do not accept that this delay was brought about by any other factor, such as the debate on exemptions or other changes to the design of the scheme.

55. We also find it disappointing that the Treasury's financial forecasts have until very recently continued to include a full year's revenue from GST in 2008, based on the assumption that the law would be introduced in January 2008.

General Rate of GST

56. Article 8(1) provides that GST shall be charged at 3%. Article 8(4) provides that the rate shall not be amended for a period of three years from the anniversary of the day on which article 8(1) comes into force. As a result of the delay to the introduction of GST as discussed above, we believe that the first practical occasion on which the Minister might propose any change in the rate of GST could be in the Budget debate in December 2011.
57. We are conscious that the States is in the midst of a period of budget restraint with considerable uncertainty surrounding the island's financial position over the next few years due to the 'Black Hole' created by the move to zero/ten taxation.
58. The Corporate Services Panel drew attention in 2006 to the problem of future revenue shortfalls in its report on the Financial Framework of the States Strategic Plan^[12]. The Panel asked the Treasury then to provide indicative figures for the period beyond the five year Strategic Plan. Forecasts for the years 2012 - 2015 showed a growing gap between income and expenditure with ongoing annual deficits of between £33 and £40 million^[13]. Far from balanced budgets over the five year period 2006 - 2011, which was the stated aim of the Minister, we feared that a structural deficit was developing in States finances.
59. In our Interim report^[14] we examined the implications of covering a potential shortfall of £35 million through increased GST revenues. We calculated that a rate of 6.3% would be required to achieve the revenue.
60. We asked the Minister, therefore, whether it would not be better in the long run to introduce GST at a higher rate immediately in order to address the deficit at an earlier stage, and to avoid the prospect of even more serious remedial action being required at a later date. Alternatively, we asked whether it would not be better for him to have the flexibility to vary the rate without waiting for three years to pass.
61. The Minister was unyielding in his response:
- I made a decision to propose the question of GST as a part-solution to a fiscal deficit of £80 to £100 million and the task given to the Crown Agents 2 years ago was to advise me on GST indications of raising that sort of level of money. The advice which I received, and which the States accepted, was that with a broad-based tax, GST, to raise that sum of money was a reasonable option. That was the advice at the time. That remains the advice and that remains the solution to that particular problem. So, yes, I think the 3 per cent is the correct rate and, yes, the problem is not going to change. That particular problem has not changed and the 3 per cent rate could be fixed for 3 years as far as I am concerned without compromising that problem at all. I think it is also a commitment that I have given, which the States have endorsed, and which I see no reason to vary or move away from.*
62. He assured the Sub Panel that despite difficulties being experienced in resolving shareholder provisions, Zero/ten would deliver the anticipated revenue:

What we are saying is there is a need to have shareholder provisions in Zero/Ten which are watertight which generate the levels of revenue that we are expecting to generate and those projections are still on target. How the Zero/Ten regulations are finally drafted in the law in respect of those shareholder provisions will cause us some concern. We have got to get them right but as soon as we get them right the level of revenue we are talking about is still within my estimate.

63. The Minister told the Corporate Services Panel^[15] that there were a number of reasons why he preferred to maintain the proposed rate for the full three years. In his view, the moratorium would encourage the States to be disciplined in its spending plans. He feared that higher States spending would have the effect of making businesses uncompetitive and would undermine economic growth. He said that the States faced constant pressures to increase spending on improved social provision; however, it was essential to curb spending to what the States could reasonably afford. Therefore he preferred to keep the door closed for the time being on any rate rise.
64. He went on to say that attempting to remove the three year moratorium on changing the rate of GST and vary the rate at an earlier stage would create complications in determining the correct levels of assistance to the Income Support scheme. It was likely also to re-open the debate on further exclusions. He felt that the priority should be to ensure that the scheme worked properly whatever the rate. The possibility of a higher rate of GST now would make this job harder.
65. Despite the confident assertions by the Chief Minister in announcing the provisional outturn figures for 2006 and the revised financial forecasts for the next few years^[16], we believe that there is every reason to remain cautious about the Island's financial position. We are aware of the urgent spending pressures already faced by the States - the funding of the Early Years Strategy is a case in point and we have already drawn attention to the need to address this problem as a matter of priority (See paragraph 28). By 2010 there may be further reasons why the Minister might consider a rise in the general rate of GST would be appropriate, even necessary.
66. We understand that the States will be in a much better position in 2009 to take stock of the effects of the Fiscal Strategy changes and the impact on States income. Nevertheless, we continue to have concerns about waiting for a full three years from the anniversary of the introduction of the tax before the Minister is permitted to make any proposal to the States to vary the general rate of GST.
67. Also, as stated above in paragraph 54, we are aware of the significant loss in future revenue in the first year of GST caused by the delay in debating the draft legislation. The four month delay in lodging the draft legislation may have further postponed in practical terms the date on which the Minister might deem it necessary to vary the general rate (to the Budget debate in December 2011). We recognise that this delay was caused by factors which required attention but we believe it may be unwise to similarly postpone the Minister's ability to vary the general rate.
- 68. Unlike GST the effects of Zero/ten and the creation of the 'Black Hole' will not be postponed. We believe that it may be in the best longer term interest of the Island not to limit the Minister's ability to respond to the fiscal circumstances which will**

arise following the introduction of zero/ten as part of his December 2010 (for 2011 fiscal year) budget planning process as was envisaged before the delays to the start of GST became apparent. We therefore intend to seek an amendment to Article 8(4) which will allow the Minister to propose an amendment to the GST rate at any time after 31st December 2010.

Parishes

69. The GST treatment of Parishes is covered under Part 4 of the GST Law - there are many references to Regulations under Article 20. This gives massive scope for "flexibility" should the need arise.

70. We understand that the introduction of GST will not have any significant effect on the current operation of Parish authorities or the services they provide. The following principles apply:

The Parishes will each register for GST and can therefore recover all GST charged on expenditure.

Parishes will be entitled to recover input GST on expenditure related to the provision of statutory goods and services, for example printing driving licences, collection of stray dogs.

Income from statutory licence functions will not be a taxable supply. It is expected that this would cover most Parish income, including rates.

71. The fees charged for residential care homes operated by the Parishes of St. Helier and St Brelade will be exempt on the same basis as other registered residential homes.

72. The fees for a nursery school operated by a Parish would be subject to the tax (irrespective of taxable turnover) because all Parishes will be registered.

73. Under the draft GST law refuse collection and road repair/maintenance are not excluded and as such would be potentially taxable. We understand, however, from the GST Director that refuse collection and road repair/maintenance are considered statutory obligations of the public sector. These services are provided either directly by the Parishes or, in many cases, by contracting the services to the private sector. In either case the Parishes would be entitled to recover any GST incurred on:

- (a) the purchase of materials, equipment or other assets (there would not be any GST on wages for employees); and
- (b) services provided by outside contractors, where the contractor is GST registered.

Powers of the Comptroller

74. Part Ten of the draft law deals with payment of taxes. Under a number of articles in this part, specified below, the Comptroller is given extensive discretionary powers to act by 'general direction'^[17].)

75. The Comptroller will have the power, for example:

- to refuse to repay input GST to a particular business or to all businesses.
- to impose conditions on a repayment,
- to issue directions as to how inputs are to be attributed to outputs.
- to make directions about matters such as when GST returns are to be made, what records must be kept, and the use of estimates.
- to order a business to pay its GST in advance.
- to demand not a pre-payment but security for future GST payments.

76. We noted that there has been a shift from the position in the consultation draft published in March 2006^[18] where it was intended for the States to set Regulations which would specify the circumstances in which the Comptroller's could exercise his powers.

77. Regulations would give the States responsibility for setting the parameters and guidelines which would restrict the Comptroller freedom to act. The effect of this shift then is to leave the Comptroller with a great deal of flexibility to decide on procedural matters. Although some of the points may appear relatively minor, we believed that some could be very disruptive for particular businesses, and we were concerned that the whole together might constitute an oppressive system.

78. The issues we have identified are set out in detail below. They have been discussed in detail with the GST Director. His responses are included.

Sub Panel comment	Response of GST Director
<p>Article 35(1)(b) gives the Comptroller the power to refuse to repay input GST to a particular business or to all businesses. The recovery of input GST is crucial to a GST system, and although the Comptroller needs to have powers to combat fraud, this power as currently drafted is unrestricted. (the taxpayer would be entitled to carry forward the GST credit to set off against future liabilities, but this could cause significant cashflow problems)</p>	<p>This relates to net credit i.e. net amount repayable on a GST return. The Comptroller may refuse to repay but he is still giving credit to the taxpayer either by open credit or reducing a current outstanding liability or against a future liability. It is perhaps also an Article for the future – when integrated ledgers are used it could be a taxpayer is due a repayment for GST and yet has an outstanding liability for other direct taxes [offsetting to protect the revenue].</p> <p>Each taxpayer is coded as either payment or repayment (the balance taken over a 12 month period). This power can be used when taxpayer (coded as payment) submits a repayment return – although the taxpayer can request a carry forward credit – this allows the Comptroller to direct a carry forward credit. It can also be used to stop small repayment amounts (which add to the administrative burden).</p>
<p>Article 35(3) is similar to the above. It</p>	<p>This is normally used to benefit the</p>

<p>allows the Comptroller to impose conditions on a repayment, with no restriction on when that power can be exercised.</p>	<p>taxpayer. It allows the Comptroller to repay a GST Credit submitted on a return that would look odd (no supplies made and / or only exempt supplies) but on conditions that would safeguard the revenue. This might be particularly useful in Jersey where the incidence of seasonal trade will be high.</p>
<p>Article 36(1). Businesses can only offset input GST (on their purchases) against the output GST due on their sales to the extent that the input GST is “attributable” to taxable sales. This section allows the Comptroller to issue “directions” as to how inputs are to be attributed to outputs. For a business with mixed taxable and exempt supplies this could reduce the amount of input GST that they can recover, and hence significantly affect their final GST liability.</p>	<p>Again this is meant to help the taxpayer. It will only apply to anyone that is partly exempt. Any input tax directly attributable to taxable outputs would be fully recoverable. Any input tax directly attributable to exempt outputs would not be recoverable. This article would allow simple methods for calculating the recoverable portion of any non attributable input tax.</p>
<p>Article 41(2) deals with input tax (whether domestic or imports) and covers the evidence required to claim input tax credit (retention of a supplier’s tax invoice or and import entry and other commercial evidence). Some of these matters could have a significant effect (e.g. whether GST returns and payments are due annually, quarterly or monthly), and so should perhaps be decided only by the States.</p>	
<p>Article 45(1) gives the Comptroller the power to order a business to pay its GST in advance. This could force a business to close if it cannot raise funds to do so. While this may be reasonable in some cases (for example where a business has previously defaulted), the law has no restrictions on when this power can be exercised.</p>	<p>This is intended to allow a taxpayer to pay a liability by instalment. Requiring advance payment or security is only applied in extreme cases – not just because someone has defaulted. “Phoenix syndrome” is an example – contrived insolvency.</p>
<p>Article 46 is similar to article 45(1). It gives the Comptroller power to demand not a pre-payment but security for future GST payments. Again, this could force a business to close, or prevent a new business from opening. In this case there is a condition that “the Comptroller thinks it necessary for the protection of GST revenue”, but this is very weak.</p>	<p>46(1) relates only to a GST credit (net repayment).</p> <p>46(2) is for the general security mentioned above.</p>

79. We have reviewed these provisions in comparison with international norms and have noted that the discretionary powers of the Comptroller are similar to those in the UK.

80. The Sub Panel was advised by the GST Director that, in his view, it was common in other jurisdictions to have these powers in Regulations [\[19\]](#).

81. We recognise that the powers of the Comptroller in each of the above cases will be subject to appeal to the Commissioners. In paragraphs 134 - 148 below we have sought to examine whether this is a sufficient safeguard by seeking evidence from those who currently use the Commissioners.

82. The GST Director advised us that the powers in P.37/2007 are in keeping with the wide powers in the Income Tax (Jersey) Law and the Customs and Excise (Jersey) Law as well as being probably rather less draconian than those in the UK VAT Act. Jersey Finance, however, contested this opinion believing that the draft law was over-prescriptive :

The existing approach and procedures available to the Comptroller in the event of non-compliance under the income tax code are based on principle, not prescription, with the Comptroller having sufficient powers to ensure compliance with the law whilst at the same time having discretion to exercise those powers in a pragmatic and flexible way.

We have particular concern with Failure to Comply (Part 14), Appeal (Part 16), and Offences (Part 17) of the draft law where in our view the provisions are out of step with the 'equivalent' provisions under the existing income tax code.

In order to minimise the cost of collection and to minimise the administrative burden for all business sectors, we believe that significant elements of the above parts could be removed and replaced with a much simplified set of general anti-avoidance enforcement and appeals principles and procedures which are consistent with existing Jersey jurisprudence.

83. The Treasury and Resources Minister told us that the intention of the draft law was to enable the Comptroller to act if necessary:

...it enables things to happen. It does not mean they must happen. I think Constables around the table will know that they have significant powers which they never use and, hopefully, never have to use and the fact that they have them very often deters people who might otherwise do things because they know that if they did them, then the Constable could use those powers. So, it is a sort of tensioner if you like, but all that this law does is it enables the Comptroller to do things if he has to.

84. The Minister was asked whether such far reaching powers were necessary in a small jurisdiction like Jersey: He said

I think you might not need the same degree of use of that power but I think having the power there is equally necessary in a larger or smaller jurisdiction. It is how you apply it and I think the parallel, if you like, the way that both Income Tax and Customs have applied their powers to date is such to indicate that in a small community like ours they do not need to be heavy handed. The powers are there but they are very rarely used to their full extent.

85. The Comptroller of Income Tax told us:

We apply the Income Tax Law in a reasonable, sensible, light touch manner. You can feel free to talk to any professional and I am sure they will all tell you that we do not apply the powers of the law in an oppressive manner or an onerous manner..... I anticipate exactly the same thing happening with the GST law.

86. Jersey Finance^[20] confirmed this view:

'The Jersey tax environment has been reasonably collaborative to date, and the experience of the members of the Fiscal Strategy Group on contentious issues is that it has generally been possible to negotiate the outcome with the Comptroller without resorting to a higher authority. This is a positive and practical approach and practitioners would hope that this would continue in the future.'

87. We have considered at some length whether it would be appropriate to seek to amend the articles quoted above in order to return to the position in the Consultation draft whereby the States would prescribe through Regulations boundaries to the discretion exercised by the Comptroller.

88. We have decided however that we will not seek to amend the draft law (except in the case of Article 41(2) - see paragraph 93) We recognise that a pragmatic, non-prescriptive approach has been the norm as regards the application of the Income Tax law and we have come to the conclusion, on the basis of the assurances given above that the Comptroller should continue to be allowed a broad degree of discretion in determining procedural matters. This is a finely balanced decision and we have opted for simplicity at this stage.

89. We recommend nevertheless that the assurances we have been given should be made explicit in guidance notes which we anticipate will be published regarding the operation of the law so that businesses are not left in any doubt about the overriding philosophy of the GST Department.

90. We also believe that it will be essential to review the operation of the GST after it has been allowed to bed down in, say, two or three years time. It will then be possible to take account of the experience of businesses in administering the tax. This review will be the responsibility of the Corporate Services Panel in the next life of the States after the elections in 2008.

91. In the case of Article 41(2) we believe that there is a matter of sufficient importance to be prescribed by the States. This article deals with a principle, rather than a procedural matter, under which the Comptroller could potentially turn what is meant to be a Goods and Services Tax into a pure sales tax with the consequent disadvantageous cascading effect. To the extent that a business holds market power and therefore the ability to pass on such a cascaded tax to its customers it could in addition have the effect in practice of turning a consumer tax into a business tax.

Power to enter and search premises

92. We note that under Article 7 of Schedule 8 an authorized person may enter business premises at any reasonable hour for the purposes of examining goods, services, records, devices and equipment or to take samples. We questioned whether this power introduced the impression of an adversarial or suspicious approach which was unlike the current style taken by Income Tax. Over-enthusiastic use of this power could alienate businesses whose co-operation was essential in the smooth operation of the scheme.
93. The Minister recognised that in a small island and with a high threshold for business registration it was unlikely that there would be many occasions on which it would be necessary to call on these powers:

Basically, Jersey businesses are law abiding. They are also in a small community where you can see what is going on. The likelihood of the sort of levels of VAT fraud which are occurring in the UK going on in Jersey is far more remote. So, yes, from that point of view you could say that you needed less legislation. What I would say is you need the same legislation but you would not need to apply it to the same degree because you have a far greater degree of compliance within the local community. I do not think it is a good idea not to have those powers. I think it is a good idea that we do not have to use those powers because we are a law abiding community.

94. The GST Director emphasised that the style which would be adopted was completely different from the early days of VAT in the United Kingdom:

The whole style has to be: "We are here as a service to support you, the businessman, to comply with your obligations. We will do everything that is possible to help you. If you do not then we have some measures which can be used." But the onus, the emphasis, is on a completely different and new relationship, one which is there to support and help.

95. We have looked at this power in other jurisdictions. We noted that UK VAT is similar – “an authorised person may at any reasonable time enter premises used in connection with the carrying on of a business”. New Zealand also seems to give a similar power to make unannounced visits. However Singapore restricts the power in two sensible ways. The officer must have:

reasonable cause to believe that an offence has been committed; and

reasonable grounds to believe that the delay needed to obtain a search warrant would cause the evidence to be removed.

- 96. We accept that it is necessary for the Comptroller to have the power to enter and search premises in reserve. We believe that the Singapore restrictions are sensible and intend to seek an amendment to the draft law accordingly.**

Benefits in Kind

97. Article 39 refers to goods or services for '*director's accommodation*'. We asked why this had been singled out. We were advised that all benefits in kind were treated in the same way. Article 39(3) was intended as a catch all. But this was a much greater problem at the Company/Director level and therefore required specific reference in the law. It was anticipated that 99% of registered GST taxpayers would be limited entities.
98. We also asked for clarification of the treatment of company cars when used in part for private purposes. It was explained that the full amount of input GST could only be recovered on company cars where the cars were used solely for business purposes. In most cases a reasonable apportionment in respect of tax payable for private use would be agreed between the business and the tax official.

Relief on sale of used cars^[21]

99. The Jersey Motor Trades Federation (JMTF) believes that it is essential to introduce a 'margin scheme' for used cars under which purchasers would not be required to pay GST on the full selling price. This would avoid double taxation in the supply chain. The Sub Panel Chairman met representatives of the JMTF on 22nd February 2007 to discuss the issues.
100. JMTF was initially advised by the GST Consultation Team that it was not considered necessary to introduce a margin scheme, with its associated administrative complexities, due to the low general rate of GST set at 3%. JMTF however believed that it was inevitable that the rate would soon rise above 3% and once GST reached 5% or above there would be a significant impact on the sale of used cars unless a margin scheme was in place. JMTF commissioned PKF to prepare a report on the need for a used car scheme.
101. JMTF argued that, without a margin scheme, the States would lose most of the expected revenue on used car sales. The current average gross margin on used cars is approximately £1,000 per unit. This applied across the board to all types of vehicle, there being no fixed percentage. This meant that the States would claim an average of £30 in GST per unit with a margin scheme. On a full turnover basis the States could expect to claim approximately £150 per unit on average (that is 15% of gross profit).
102. JMTF believed that, without a margin scheme in place, it was very likely that dealers would take steps to avoid paying the tax on their turnover - either by disaggregating their business to avoid the requirement for registration or by stopping used car sales. One large dealer made it clear that if a margin scheme was not established he would stop selling used cars as soon as GST was introduced and would act only as an agent. Thus the States would lose any form of revenue on sales.
103. JMTF recognised that a margin scheme appeared to be complex to administer. However, it was contended that, since the computer systems used by dealers were designed in the UK and therefore already set up to administer the scheme, it might actually be more onerous for the dealer not to have the scheme in place.

104. It was suggested that a retail scheme might be an attractive option to both car dealers and the GST office as it could reduce the administrative burden for both sides. However, it appeared that this would not stop large dealers from pulling out of the used car market. Furthermore, unless a blanket deal was achieved covering the entire motor trade, the benefits of a retail scheme would depend on the commercial leverage of individual companies. This could result in unfair disadvantage to smaller dealers.
105. The Treasury and Resources Minister told us that he had an open mind on the way the used car market would be treated. He had initially been advised that a margin scheme was unnecessary in Jersey but was prepared to listen to opposing points of view.
106. The GST Director advised us that the introduction of the scheme would be deferred pending clarification of proposals for environmental taxes which would replace VRD. It was important to look at the total picture of taxation of vehicles.
107. We understand that there may be a case for similar provision for the sale of other pre-owned goods, such as yachts, antiques, works of art, horses. However, in these case, we believe that most sales, with the possible exception of antiques, are conducted on a commission basis (with legal ownership transferred from consumer to consumer with the dealer taking a commission, as opposed to consumer to dealer to consumer), or likely in the main to be sold by unregistered businesses. In cases of difficulty the Comptroller and a business can always opt for a 'small retailers' scheme [\[22\]](#).
108. **We believe that the arguments in favour of a margin scheme for used cars, as presented in the report commissioned by the JMTF, are convincing. Furthermore, we believe that, if dealers were required to charge GST on the full selling price of a used car with no reference to a tax reclaim on its purchase they would struggle to pass on the entire cost to their customers due to the significant market power of private sellers of second hand cars. We, therefore, fully support the introduction of such a scheme for the used car market.**

Financial Services Industry

109. Part 12 of the draft law deals with the treatment of finance vehicles and the Financial Services Industry.
110. In the first part of our review we met representatives of the Fiscal Strategy Group of Jersey Finance to discuss their comments on the Treasury's GST Financial Services Discussion Paper [\[23\]](#). The following paragraphs contain a brief summary of the issues discussed in the public hearing on 7th September 2007.
111. The Fiscal Strategy Group (FSG) strongly recommended against applying the proposed ISS fee to all forms of trusts on the grounds that any fee would breach a long established principle that non-resident trusts are not subject to any form of taxation or charge.

112. The FSG was concerned about the potential yield from the ISS charge as there was uncertainty about the number of vehicles which might elect to pay the fee. Although the number of Jersey companies can be determined with the assistance of the Jersey Financial Services Commission the precise number of foreign incorporated companies is unknown. Estimates put the number between 50,000 and 150,000. The FSG believed that the current proposals, as contained in the Consultation paper could yield considerably in excess of the Minister's target of £5 - £10 million from the Financial Services Industry. They urged the Treasury to undertake further research and financial modelling before finalising the proposals.
113. Further issues regarding the **ISS status scheme**, were raised, in particular:
- the definition of an ISS (e.g. whether minor Jersey activities should be allowed)
 - level playing field between clients of banks and those of other service providers;
 - timing of payments of ISS fees (a single annual payment or on the anniversary of initial registration)
114. A number of issues were raised regarding the operation of the **presumptive scheme**, particularly:
- whether it was to be optional or compulsory;
 - the percentage of input GST that could be recovered;
 - fairness between different participants in the industry in setting that percentage.
115. The Sub Panel discussed the above issues with the GST Director. It was informed that banks with overseas clients could opt for either generic GST treatment, with the associated complicated administrative burden, or a partial refund scheme. Once the law had been introduced banks would be visited on an individual basis to assist in assessing their organisational structure and determining their best option.
116. The GST Director explained that it was difficult at this stage to make any meaningful projection for the potential yield from the ISS charge. In addition to the points raised by the FSG (see paragraph 114) application for ISS status by finance vehicles would be voluntary and would depend on assessment of the GST liability under individual circumstances.
117. **The FSG subsequently suggested to us that to reduce the uncertainty a survey sampling a proportion of financial services businesses in the Island might be undertaken. We will consider undertaking this proposal ourselves in the next stage of our review.**
118. The GST Director clarified that finance vehicles could apply for ISS status on a rolling application at any time during the year, rather than all application being made on a single fixed date. Annual re-applications would then be on the anniversary of the first application.
119. Trusts could apply for ISS status, subject to eligibility, in order to be granted end user relief if it was decided that this treatment would be beneficial to them. The ISS fee is not a compulsory tax, but a voluntary fee to avoid the trust being charged GST on its advisers' fees Trust companies could make a bulk application on behalf of the trusts

they administered.

120. The Sub Panel questioned whether a law firm carrying out only off-shore work could apply for the ISS status. We were informed that a company registered for GST could not also apply for the ISS status of a vehicle. This would be made clear in Regulations.

121. The Sub Panel invited the Fiscal Group to meet us for a second time in March 2007 to discuss the draft law (P.37/2007) once it was lodged and to consider whether their concerns had been addressed. However, it was agreed to defer this discussion pending further details of the treatment of the Financial Services Industry which would be prescribed in Regulations. **We intend to report on these discussions in the next stage of our review when we consider the proposed Regulations.**

De minimis limit on value of imports

122. A de minimis limit for the application of GST on the value of imports is to be defined in the Customs and Excise (Jersey) Law 1999. The application of this law to GST is covered in Article 69.

123. The Minister advised us^[24] that a value figure between £100 and £500 was still being considered. His principal interest was on the revenue yield as a comparison against administrative costs. No final decision had yet been made on this matter.

124. The Chamber of Commerce recognised the difficulty in its written submission to the GST Consultation Team^[25]:

It is important that a reasonable de minimis level is set for imported goods and the challenge will be to set an appropriate figure. An obvious level would be £100; however, we can see reasons why it is both too low and too high. Administratively it does not seem worth the effort to collect £3 of tax. On the other hand a large number of imports would still fall below this figure thereby disadvantaging on-island business.

125. In evidence to the Sub Panel, Mr. M. Lewis, a Director of B.G. Romerils^[26], said that he was seriously concerned at the potential impact on local retailers of setting a high de minimis level:

Government must not look at this solely from their position of 'tax take per item'. Local businesses are facing a difficult challenge from internet trading and offshore (United Kingdom and France) shopping where prices and choices are greater and more competitive. A high limit will only increase the pressure and I believe have a sizeable effect on our retail industry.The higher the limit the higher will be the loss of jobs in the Island.

126. Deputy S. Power^[27] drew attention to the difficulties which he believed Customs officials would face from increased internet-based freight and the potential for

evasion:

One of the things that I think will happen from 2008 is that there will be more freight coming into the Island off internet-based freight and there are a number of companies now -- there are a number of individuals and there are a number of companies now who have vans of various sizes who come in and come out on a daily basis as far as a semi-courier thing. I think that level of business will increase and I think there is an element out there of carriers who will operate on the basis that the actual manifest will show an internet-based import, that the manifest at the point of entry in Jersey will be different to the actual invoice price of the goods coming in. It will be completely different and I do not think from what I have read that we have the means to stop. At the moment we have 450,000 tons of freight coming in through the port or the airport every year and I think we inspect about 5 per cent of it.

- 127. We understand that setting the de minimis level for imports is a sensitive and difficult decision for the Minister. Nevertheless, we believe that a decision should be taken as soon as possible to enable businesses to plan accordingly. We also believe that the Minister must consider the needs of on-Island businesses as well as the Tax Office's costs. (i.e. it might be beneficial to collect uneconomic amounts of GST to avoid under-mining on-Island retailers)**

Unjust enrichment

128. We note that, under article 83(4), if a business has overpaid GST, the Comptroller is allowed to refuse to refund the overpayment if it would "unjustly enrich" the business.
129. We were advised by the GST Director that this provision stems from some exceedingly large claims in the UK after tribunal decisions have gone against the Commissioners. This clause is used where clearly the appellant cannot or has no intention of passing on the benefit of the refund to the customer(s). If the appellant repays the overpaid tax back to customers/clients there is not a problem.
130. This article gives the Comptroller a large degree of discretionary power on the repayment of GST when a tribunal decision has gone against him. We question the morality of this position. We concede, following the advice received in paragraph 131 above that there may be very rare circumstances when the Comptroller might legitimately use his discretion to limit repayments of GST to a successful appellant. We believe that there may be relatively many more cases where full repayment will be appropriate. We believe that the majority of appeals by businesses will occur as a result of the Comptroller's refusal to allow either the input tax that a business may be claiming or of the Comptroller's insistence that a business has understated its declared output GST on its sales. In these latter cases a business will already have passed on to his customers the lower GST charge and will have been penalised by the Comptroller's decision that will have led to the successful appeal.
- 131. We have concluded therefore that this is another area where a future review of GST should monitor the operation of the law in the light of experience.**

Appeals

132. Reference was made above (see paragraph 79 and following) to our concerns over the discretionary powers of the Comptroller and the ability of the appeals mechanism to provide an adequate safeguard.
133. Article 84 sets out the matters in respect of which an Appeal may be made to the Commissioners^[28] under part 6 of the Income Tax (Jersey) Law 1961.
134. We requested the views of the finance industry on the effectiveness, speed and costs of appeals to the Commissioners. The replies received confirm that the Commissioners perform a satisfactory role but some uncertainty was expressed whether the GST system could work alongside the current Income Tax system of appeals
135. Le Sueur Ireson & Co commented:
- We are not sure whether the Commissioners would be able to cope with the possible volume of work as, at present, there is a small group of people who form the Commissioners of Appeal and they only meet six times a year. It would therefore depend on the number of cases that may arise and we would have some concerns if the Commissioners of Appeal were to remain in the current format. It may require a panel to review the matter of returns and repayments of GST on a more frequent basis and we feel this matter should be reviewed.*
136. The Treasury Minister said that he did not expect a high volume of appeals in Jersey particularly in view of the high registration threshold which meant that there was a relatively small number of bodies involved in that aspect of the law.
137. The Minister accepted that it might be necessary to increase the number of meetings held per year^[29] to accommodate the different needs of GST appellants. It was suggested that, in order to achieve this, the number of Commissioners could be increased or the quorum reduced.
138. The GST Director said that there was no reason why there should be a separate Commission for GST - it was common practice throughout the world for a single body of Commissioners to adjudicate on tax matters. He said that his department would be trying to emphasise that there was 'a *perfectly sensible and reasonable internal mechanism for review*', which would avoid the need for appeal as far as possible.
139. While we have heard no criticism of the current Commission we share the concerns expressed above regarding the capacity of the Commission as currently constituted to undertake the increased workload which might be expected to occur with the introduction of GST. Although many issues may well be dealt with through an internal review mechanism, we believe that it is reasonable to anticipate a number of appeals in the early stages. It would be unfair to both the Commission and local business to allow a backlog of cases to build up. Income Tax is essentially backwards-

looking, so the impact on a business of a delayed appeal is minimised, but some aspects of the GST law could destroy a business unless an appeal could be heard almost immediately, particularly the requirements to pay in advance or give security if this were to be enforced (Article 45).

140. **We recommend therefore that early action be taken to strengthen the numbers in the Commission, and to provide training on the new GST law for all Commissioners.**

141. With regard to the appeals mechanism, we noted that under Article 86(2)(c) the Commissioners might refuse to hear an appeal unless the appellant had deposited the disputed GST (and any other GST due) with the Comptroller. We were concerned that this could seriously restrict a business' ability to appeal (particularly if, for example, the business was appealing against an order to pre-pay estimated future GST).

142. Jersey Finance's ^[30] comment on Article 86(2)(c) was as follows:

'The requirement that the taxpayer pay all contested GST before an appeal can be heard by the Commissioners is taken directly from the United Kingdom VAT Act 1994. However, while a United Kingdom VAT tribunal may alleviate this condition under certain circumstances prescribed by regulation, there is concern that the draft GST legislation does not appear to provide the Commissioners the same flexibility.'

143. Commenting on these concerns the GST Director said that the Commissioners in Jersey would not normally require payment of any tax in dispute. However, it was common practice to reserve this right in order to protect against frivolous cases.

144. Jersey Finance commented further on the appeals process:

It is important to point out that Article 86(3) sets out certain circumstances in which the Commissioners are prevented from hearing an appeal against certain directions made by the Comptroller. The right of appeal should not be limited, as far as possible.

145. The GST Director made it clear that the Commissioners would receive training to equip them for making appropriate judgements in respect of the new tax. He added:

Having looked at the commissioners appeal mechanism in Jersey, I would have said that it was far better than the equivalent VAT tribunal or tax tribunal in the UK. In all aspects it is a superior body.

146. **We welcome the assurance that the Commission of Appeals will continue to act in a manner which is consistent with existing Jersey principles and procedures. We recommend that this is made clear in the guidance notes and advice which the Department will be preparing for businesses over the coming year.**

Penalties

147. We noted that the penalties for offences under the GST law appeared to be considerably greater than those under the Income Tax (Jersey) Law 1961. We carried out some research into a comparison with other jurisdictions (see appendix). As can be seen from this table, GST penalties vary widely across the world. However two points stand out from Jersey's proposals:

The 15 year prison sentence for fraudulent evasion is far higher than the closest alternative; New Zealand has a maximum 5 year sentence, and Singapore a maximum of 7. UK VAT law does not impose prison sentences, although there is the ability to prosecute for general fraud which potentially carries a sentence of life imprisonment.

The offence of giving "recklessly" false information appears designed to sit halfway between an innocent mistake and fraud, and carries a corresponding sentence. However the sentence, of up to 5 years in prison, is almost as high as any other country's GST system has for *deliberate* fraud. New Zealand's GST law has a similar offence of "gross carelessness", for which there is no prison sentence.

148. The Treasury frequently cites New Zealand as an example of a good GST system; it may be suitable to also adopt their penalty provisions

149. The Comptroller explained why the penalties under the Income Tax law were purely monetary:

The vast majority of cases that we uncover are neglect and wilful default, which are handled administratively for a money settlement with penalties. The reason that we do not send people to jail is that we want them to carry on working in their business, generating income, which I can tax. If you send them to jail for 15 years, the State is paying for them to be in jail and I do not get any tax. It is purely monetary^[31].

150. We sought legal advice on this issue. We understand that the penalties under the Income Tax law are considered to be too low to deal with matters of fraud. As a result, fraudulent evasion of income tax would normally be prosecuted as fraud and not under the Income Tax law. (The maximum penalty for common law fraud is life imprisonment.) The opportunity was now being taken in the new draft GST legislation to set a severe deterrent against the possibility of a really massive GST fraud. Ultimately, it is for the court to distinguish between types of fraud and to decide the appropriate level of penalty.

151. **Following our research into comparisons with other jurisdictions, we have decided to lodge an amendment to Articles 88 and 89 to reduce the level of penalties.**

152. In addition we noted that article 88(2) states that a person would be guilty of an offence "...whether or not the particulars of that offence are known".

153. We were advised by the GST Director that this article was necessary because of some of the sophisticated measures now taken to fraudulently evade tax. He explained that the nature of the offence made it difficult to prove.

154. Under article 92(1), if a company commits an offence, as a result of “any neglect” by a director, manager or other officer, then that individual is personally liable. This seems to us too wide a power, and casually breaches the usual principle of limited liability. We suggest it would be more appropriate for personal liability to apply in the case of “gross negligence”, not mere “neglect”.

155. **We intend to lodge an amendment to article 92(1) accordingly.**

Display of retail prices

156. Article 94 enables the States to make provision by Regulations in respect of displaying retail prices. This article enables the States through forthcoming Regulations to determine whether retail prices should be marked on goods inclusively or exclusively of GST.

157. We have considered the report of the Trading Standards Officer to the Council of Ministers on this issue^[32]. He argues for inclusive pricing which would mirror the United Kingdom and most other countries with a VAT/GST regime. The alternative option is for *exclusive pricing* whereby the tax is added only at the till to the total bill amount (similar to the methods of paying the sales tax in USA and Canada). The Trading Standards Officer states:

‘Exclusive pricing would put Jersey out of step with price marking requirements legally enforceable throughout the European Union and many other countries throughout the world. Therefore, if the States do not legislate, there is the potential for consumer confusion where some traders include GST in their price displays and some do not. The majority of summer tourists come from the UK and the rest of Europe so are used to a price inclusive system, that is, “what you see is what you pay”.

158. We are aware that this issue has been the subject of much public discussion. The Chamber of Commerce considered the advantages and disadvantages of both options in its submission to the GST Consultation Team^[33]. The Chamber told us^[34] that, on balance, they preferred the exclusive option. They believed that it was important that the taxable element was clearly stated for the customer. This option would be the simplest option in terms of administration costs for businesses. Most importantly for the consumer it would reduce the risk of rounding up of prices.

159. We believe that the general public will be particularly concerned, in the early stages of the introduction of GST, with the perception that subtle increases in retail prices will be brought in under the guise of GST. Consumers would therefore prefer the price *exclusive* option as they will know precisely the amount of GST charged on their overall transaction. It seems to us likely that, once the initial impact of the tax has been felt, consumers will tend towards the price inclusive system. They will start to find the additional amount payable at the till rather irksome. At that point it would be appropriate to introduce Regulations to prescribe inclusive. The States will then be able to make a decision based on the facts and possibly changed circumstances prevailing at that time.

For example, after the initial inflationary effect of GST has diminished, there may be less public concern about the rounding up of prices on low priced items. We do not believe that a transitional phase will be confusing to the consumer - rather it will be reassuring.

160. We think therefore that, in the early stages of the introduction of GST, market forces should be allowed to determine whether or not prices are marked inclusively or exclusively. We note that the current draft of the legislation allows this situation to be prescribed under regulations and the States will therefore be in a position to address this matter when the regulations are lodged.

Taxpayer's Statements

161. Article 96 gives the Comptroller the right to use a taxpayer's statements in evidence even where this breaches a previous agreement not to prosecute.

162. We were advised that the ability to compound offences (settle out of court) was important but it was necessary to maintain certain precautions. The Comptroller must always reserve the right to take a case to court even if compounding was offered and accepted. Such cases must in the first instance be pursued as if the person involved was going to court – you must be able to demonstrate that an offence has been committed. Within certain rules the Comptroller can then offer compounding. If the person agrees and pays in full that was the end of the matter.

163. On the other hand, if the person agrees to compound but then reneges or defaults, the case is resurrected and taken to court. Any statements obtained during the investigation should have been obtained under Judges Rules / PACE and therefore admissible in court as evidence.

164. We thought that this article is potentially unfair, and damaging to trust between the Comptroller and taxpayer. It could also make investigations more difficult. It is useful for the Comptroller to make an offer to a taxpayer so that in return for a confession the taxpayer will be fined under the GST law but not prosecuted; this section makes such an offer impossible because it would not be binding.

165. We believe that this is another area where the operation of the law should be reviewed in the light of experience.

Rents

166. We note that Article 1(3)(c) of Schedule 6 makes a distinction between residential rentals (which are zero-rated) and holiday lets (taxable), by excluding rental of less than 3 months. We pointed out that this would create an anomaly for the lodging house sector (non-qualified residential accommodation) in that most licences are issued on the basis of a weekly rental which would bring them into the scope of the tax.

167. We understand that our recommendation that this article be amended has

been accepted by the Minister.

Resource implications for the Income Tax office

168. The Treasury Consultation paper published in March 2006 stated:

It is confidently anticipated that a simple, cost-effective system of GST is possible for Jersey, with administrative costs, including staff salaries, being in the region of only one per cent of the revenue yield. ^[35]

169. One per cent of revenue yield would amount to £450,000. We note however that the resources statement in P.37/2007 estimates that 10 staff will be needed in order to administer the tax at an approximately operating cost of £1 million per annum.

170. We acknowledge the importance of adequate staffing if the tax is to be administered efficiently. However, we were concerned that this latest calculation appears to be more than twice the confident statement made in 2006 on which most States members would have based their expectations of administration costs.

171. The GST Director explained that the 1% figure was normally a benchmark for an efficient and effective system that was mature – that is, one that has been implemented; stabilised and consolidated. The £1 million is a max operating budget that might be required in the first few years of the tax (before it is mature).

172. The 1% figure was also based on a simple GST (with max use of e-business etc). As a result of the changes so far (for example, margin schemes; group registrations; further exclusions – exempt and zero rate; treatment of charities; etc) we do not have the simple system envisaged in March 2006.

Appendix: Penalties – International Comparison

Jersey GST offence	Jersey GST	Closest international equivalent offences		
		Jersey Income Tax	UK VAT	Ne
Fraudulent evasion (s88)	15 years prison	£2,000 + 2x tax	1x VAT	
Give “recklessly” false information (s89)	5 years prison	£2,000 + 2x tax	15% of VAT	
Failure to charge GST or keep records (s40)	£5,000 max	n/a	£500	1st r
Late return & payment (s74)	£200 + 10% of GST	£2,000	First offence 2% of VAT, rising to 15%	1s
Failure to register (Sch1 p3(5))	£5,000	n/a	10-30% of VAT	1s

Notes:

Penalties are all maximums; actual penalties will usually be lower.

The definition of offences is different in different systems (for example New Zealand does not have a separate offence of giving “recklessly” false information), so the penalties will not exactly correspond.

There are also general penalties for fraud in all jurisdictions, potentially involving a prison sentence, but these are outside the VAT / GST law.

[1] HMRC Reference: Notice 701/1 see website <http://customs.hmrc.gov.uk/>

[2] See; 1999 United Kingdom Treasury Review of Charity Taxation; Deloitte: Charity VAT Survey, 2006. VAT for Charities - State of Play and Plans for the Future, Laszlo Kovacs EU Commissioner for Taxation and Customs, September 2005

[3] See website <http://www.ctrg.org.uk> for more information.

[4] Source: Treasury and Resources Minister at the public meeting held at Trinity Parish Hall, 6th September 2006.

[5] ‘The Jersey Law of Charities’, Jersey Law Commission Consultation Paper No.7(B) dated November 2006

[6] De La Salle College, Beaulieu and FCJ primary school

[7] Source: States Treasury

[8] A Working Group was established by the Council of Ministers in July 2006 to review early years provision for the 0-5 age range. This group reported to the Council in December 2007 in R.C.100/2006.

[9] Source: Jersey Childcare Trust

[10] R.C.100/2006

[11] Based on calculations using the Household Expenditure Survey 2006. We were unable to estimate a figure for alterations and extensions on the basis of Survey data but believe that the overall estimate of revenue yield would be significantly greater.

[12] Table 1 SR3/2006

[13] These forecasts were provided with an accompanying 'health warning'. The Minister told the Sub Panel: 'They are almost academic; they are sort of a mathematical extension to where we are now, rather than a realistic position.' Public hearing 18th May 2006

[14] Section 5.7 SR3/2006

[15] Private meeting dated 27th February 2007

[16] Information made public on 26th March 2007

[17] We understand that this is a form of 'quasi-legislation', applying generally and needing to be published See article 99(3)

[18] R28/2006

[19] Public hearing 2nd March page 12

[20] Letter dated 20th March 2007

[21] Article 52(3) enables provision to be made on the basis of the marginal value of a supply or of goods.

[22] allowable under article 43(1)

[23] Public hearing dated 7th September 2006

[24] Public hearing on 2nd March 2007

[25] Submission dated 21st June 2007

[26] Public hearing on 31st August 2006

[27] Written submission for the public hearing on 31st August 2006

[28] The Commissioners of Appeal are independent of the Income Tax Office. They are a body of professionals appointed for their experience in financial matters. There are currently eight Commissioners and a quorum of five is required to hear appeals.

[29] The Sub Panel was informed that typically a meeting of the Income Tax Commissioners was held every three months

[30] Letter dated 20th March 2007

[31] Public hearing 2nd March 2007

[32] Considered by the Council of Ministers on 22nd March 2007

[33] Submission dated 21st June 2006

[34] Public hearing dated 3rd August 2006

[35] R.28/2006