STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy C N K Parkinson
Seconded by: Deputy M M Lowe

Policy Council

Future Economic and Taxation Strategy

To amend the Propositions as follows:

1. By replacing "at 10%", in Proposition 2, with ", which, subject to Proposition 3, shall be charged at 10%".

2. By replacing Proposition 3 with:

"3. That the following profits shall continue to be subject to income tax at 20%:

a) the profits of specific banking activities realized by banks with total taxable profits exceeding £50 million per annum;

b) the profits of any regulated financial services company which elects to be taxed at 20%.".

3. By inserting the following Propositions immediately after Proposition 5:

"5A. That Guernsey and Alderney companies, other than regulated financial services companies, shall be subject to an Accumulated Earnings Tax at the rate of 20% in respect of taxable income which remains undistributed by the company on the third anniversary of the end of the accounting period in which that income was earned.

5B. That an individual who becomes non-resident for a period of less than 5 whole Years of Charge shall upon again becoming resident be subject to Income Tax at 20% in respect of distributions from Guernsey companies (including sale proceeds of shares in Guernsey companies, to the extent that these relate to undistributed profits) received during that period of non-residence.

5C. That rents relating to real property situated in Guernsey or Alderney will continue to be subject to Income Tax at 20%."

4. By inserting the following Proposition immediately after Proposition 7:

“7A. That the Income Tax Law be amended to make clear that dividends, interest, and royalties paid by Guernsey and Alderney companies to non-residents will become or remain exempt from Guernsey Income Tax.”

5. By replacing Proposition 9 with:

“9. That a Payroll Tax, at the rate of 7.5% of total payrolls, shall be introduced, payable by all employers except

(a) those whose income is subject to Guernsey Income Tax at the rate of 20%; and

(b) any company outside the regulated financial services sector which satisfies the Administrator that more than 80% of its share capital is beneficially owned by Guernsey or Alderney resident individuals.”

6. By deleting “half” and substituting “a quarter” in Proposition 11.

7. By inserting at the end of the words in Proposition 12: “, but only, in the case of life assurance policies, in respect of policies issued after the date on which the revision comes into force.”

8. By deleting Proposition 15 and renumbering Proposition 16 as “15”.

9. By adding the following Proposition:

“16. To authorise the Treasury and Resources Department to enter into discussions with Ministers and officials of the UK government to enable them to form a view as to which of the possible fiscal policies that might be adopted by Guernsey would command the support of the UK government at meetings of the Code of Conduct Group.”

EXPLANATORY NOTES TO DEPUTY C N K PARKINSON'S AMENDMENTS

1. To amend Proposition 2 in the PC proposals

Amendment consequential on 2, below.

2. To replace Proposition 3 in the PC Proposals

Under the principles of the EU Code of Conduct on Business Taxation, Guernsey can adopt a low or nil rate of Income Tax, if that rate is our general rate of tax. Higher rates of tax may be applied to defined groups of companies representing a minority of our economy. The ability to tax companies at a higher rate is therefore a 'scarce resource', which needs to be applied carefully to achieve the maximum effect. Taxing the regulated utilities at 20% would be a waste of this scarce resource because the States of Guernsey wholly owns two of the largest regulated utility companies in Guernsey, namely Guernsey Electricity and Guernsey Post, and therefore owns 100% of their profits. In effect the charge would only apply to telecoms companies, and then only to their regulated activities (eg not the profits of their retail outlets).

Under the amendments proposed, most locally-owned companies in the regulated financial services sector would elect to be taxed at 20% - because their profits will eventually be subject to 20% income tax in any case, and because they would avoid the Payroll Tax by making this election.

Some foreign-owned finance sector companies would also elect for 20% tax, eg because:

a) 7.5% of their payroll may be more than 20% of their taxable profit. Income Tax is only payable when a taxable profit has been generated, and, unlike a Payroll Tax, cannot convert a profit into a loss.

b) If the company is owned by non-residents, the owners may be entitled to double tax credits for any Guernsey Income Tax paid, but they will not obtain any credit for any Guernsey Payroll Tax paid. The problem here is that it may be a condition for obtaining relief in their home country that the payment of Guernsey Income Tax should be compulsory. Therefore, some parent companies may not obtain credit if their Guernsey subsidiary elects to pay Income Tax under 3 b). It may be possible to assist such parent groups in future if the categories of company subject to compulsory 20% Income Tax (ie 3 a)) are widened.

Jersey also proposes to allow financial services companies to elect to pay Income Tax (in their case at the rate of 10%) in order to benefit from partial reclaims of GST.

The Isle of Man allows any trading company to elect to pay 10% Income Tax to avoid being subject to its Distributable Profits Charge.

It is estimated that this amendment would produce additional tax of at least £3m per annum compared to the Policy Council proposal. Just as importantly, the proposal would result in a reduction in the deferral of income tax by locally owned financial services companies. The value of this deferral would otherwise be significant, given that it is proposed that regulated financial services companies should not be subject to the Accumulated Earnings Tax (see Proposition 5A).

The election would allow locally-owned financial services companies a simple method of opting out of the Payroll Tax, which would be administratively less cumbersome than applying “look through” rules for local ownership in this industry.

3.

- ***To insert new proposition 5A***

The policy proposed by Policy Council would allow wealthy investors to avoid, or defer indefinitely, paying Income Tax on the trading income of any company that they own. This would create an incentive to incorporate unincorporated businesses (there are 2,800 self-employed individuals in Guernsey) with the object of sheltering income from tax.

Guernsey resident shareholders consume Guernsey public services, just as employees and the self-employed do. There is no reason why they should not be expected to contribute to the cost of those services.

The profits of companies trading in Guernsey are currently subject to 20% Income Tax as they arise. The amendment would benefit shareholders by allowing them to retain trading profits within the company for up to three years (eg to fund fixed or circulating capital requirements) without paying tax, but would put a time-limit on the deferral.

Jersey is proposing to introduce both a “Deferred Distribution Charge” (an interest charge on the money saved by deferring payment of tax) and a “Deemed Distribution Charge” (which would treat the shareholder as if the company had distributed its profits three years after they were earned), to achieve the same purpose. The Accumulated Earnings Tax would be a simpler means to achieve the same end. Moreover, since the Tax would be paid by the company, the question of whether the shareholder has the resources to pay the tax would not arise.

The Isle of Man has a “Distributable Profits Charge” at the rate of 18%, applied to 55% of trading income and 100% of investment income which remains undistributed 9 months after the end of the accounting period in which the income is earned. Companies which have “distributing company status” (ie which distribute at least 55% of trading income and 100% of investment income, or which pay 10% income tax) are exempt from the DPC.

- ***To insert new Proposition 5B***

If this measure was not introduced, shareholders could avoid Guernsey tax by becoming non-resident for at least one tax year and taking a dividend from their company during the period of non-residence.

It will be noted that, under resolution 5, there would be effective anti-avoidance measures including deemed distribution rules (presumably covering sales of shares) to deal with cases of Guernsey residents attempting to take their shares of a company’s profits in the form of a non-taxable distribution.

- ***To insert new Proposition 5C***

There is no reason why rents from Guernsey real estate should not remain taxable in Guernsey. Jersey and the Isle of Man have corresponding rules (in the case of the Isle of Man, at a 10% rate of tax).

4. To insert new Proposition 7A

The finance industry will welcome this clarification, which largely confirms the existing position.

5. To replace Proposition 9

This amendment would transfer part of the cost of the “zero-ten” policy to the beneficiaries of that policy.

However it would leave Guernsey with a competitive fiscal regime, compared to its nearest competitors.

a) As compared with Jersey:

   i) Jersey proposes to introduce a “Regulation of Undertakings and Development Charge”, with an initial median value of £500 per employee (ie higher in some industries and lower in others – and presumably highest in the financial services industry).

   ii) In addition, Jersey’s employer social insurance contributions, at 6.5%, are 1% higher than Guernsey’s, and their upper earnings threshold (the maximum amount on which contributions are paid) is about £1,400 higher than Guernsey’s.

iii) Jersey will levy 10% income tax on the profits of banks, trust companies, collective investment fund functionaries, investment managers and brokers. Under the proposals in these amendments, collective investment fund functionaries, investment managers and brokers would suffer no income tax in Guernsey unless they elect so to do.

iv) Financial services companies in Jersey will be able to reclaim only a portion of the 3% GST that they suffer, unless they elect to pay 10% income tax.

v) Jersey has banned captive insurance companies, with effect from 1 January 2006.

b) In the Isle of Man:

i) the employer social insurance contribution is 12.8%, with no upper earnings threshold. Guernsey companies subject to the Payroll Tax would be paying 13% in total employer contributions and taxes up to the upper earnings threshold, and 7.5% over that amount.

ii) The Isle of Man will also levy 10% income tax on banking profits.

iii) Financial services companies suffer 17.5% VAT on their business expenses, which for most of them is an irrecoverable cost.

c) All non-finance sector businesses owned by Guernsey residents, and all finance sector businesses which elect to pay 20% Income Tax, would be exempt from the Payroll Tax. This would encourage local ownership of financial services businesses, and for some groups would convert what would otherwise be an ‘above the line’ business expense into a tax on profits which may be creditable against ‘home country’ tax.

The Payroll Tax would produce an estimated £40m, compared with the £22m which would be collected under Policy Council’s proposals regarding social security contributions.

See the Appendix for a comparison of the tax costs, for various sectors of the finance industry, of doing business in Guernsey under the proposed amendments, compared to doing business in Jersey or the Isle of Man. This shows that Guernsey will still be the cheapest jurisdiction in the Crown Dependencies for finance sector businesses, in tax terms, even if the Payroll Tax is adopted.

6. Amending Proposition 11

The original intention of the Contingency Reserve was to create a fund that would cover one half of the States Annual expenditure, in case of emergencies or prolonged economic down-turns. One half of today's States expenditure would be about £150 million, or three quarters of the current Contingency Reserve.

7. To add words to Proposition 12

Many life assurance policies are taken out in the context of an endowment mortgage scheme, as part of long term planning by individuals acquiring their home. They will have made their plans on the basis of the tax relief currently available for the premiums paid on such policies. It would be unfair to them to abolish that relief retro-actively.

8. Deleting Proposition 15

Proposition 15 is otiose if proposition 9 replaced as per 5 above.

9. Adding new Proposition 16

No ministerial level talks have been held to establish the limits of the Code of Conduct restrictions, from the viewpoint of the UK government. Considering that the Chairman of the Code of Conduct Group is a UK government minister, Dawn Primarolo, this is an omission which needs urgently to be rectified.

<u>Policy Council</u>
<u>Future Economic and Taxation Strategy</u>
Propositions as they would stand if the composite amendment moved by Deputy Parkinson were carried in its entirety.

1. That from 1st January, 2008, the basic rate of income tax on company profits shall be 0%.

2. That only a limited amount of regulated business (ie specific banking activities) shall be subject to income tax, *which, subject to Proposition 3, shall be charged* at 10%.

3. That the following profits shall continue to be subject to income tax at 20%:

> *a) the profits of specific banking activities realized by banks with total taxable profits exceeding £50 million per annum;*
>
> *b) the profits of any regulated financial services company which elects to be taxed at 20%.*

4. That resident individuals shall continue to pay income tax at 20% on assessable income.

5. That Guernsey resident shareholders shall be taxed at 20% on their distributed profits and on all rental and investment income but with effective anti-avoidance measures including deemed distribution in certain circumstances.

5A. That Guernsey and Alderney companies, other than regulated financial services companies, shall be subject to an Accumulated Earnings Tax at the rate of 20% in respect of taxable income which remains undistributed by the company on the third anniversary of the end of the accounting period in which that income was earned.

5B. That an individual who becomes non-resident for a period of less than 5 whole Years of Charge shall upon again becoming resident be subject to Income Tax at 20% in respect of distributions from Guernsey companies (including sale proceeds of shares in Guernsey companies, to the extent that these relate to undistributed profits) received during that period of non-residence.

5C. That rents relating to real property situated in Guernsey or Alderney will continue to be subject to Income Tax at 20%.

6. That individual taxpayers shall be liable to the standard rate on their investment and non-Guernsey trading income up to a defined income ceiling with a maximum tax payable of £250,000 on any individual’s income from such sources.

7. That “wealth taxes” such as inheritance and capital gains taxes shall not be introduced.

7A. That the Income Tax Law be clarified to make clear that dividends, interest, royalties and non-executive directors fees paid by Guernsey and Alderney companies to non-residents will become or remain exempt from Guernsey Income Tax.

8. That the rates of existing indirect taxes shall be increased, in particular duties on alcohol, tobacco and motoring, and Tax on Rateable Values, in line with the contents of that Report.

9. *That a Payroll Tax, at the rate of 7.5% of total payrolls, shall be introduced, payable by all employers except*

(a) those whose income is subject to Guernsey Income Tax at the rate of 20%; and

(b) any company outside the regulated financial services sector which satisfies the Administrator that more than 80% of its share capital is beneficially owned by Guernsey or Alderney resident individuals.

10. That General Revenue shall continue to fully fund the non-contributory elements of the present social security system (Family Allowances, Supplementary Benefit etc).

11. That up to *a quarter* of the Contingency Reserve (interest and capital) may be used to
fund the shortfall in public sector expenditure during a transitional phase.

12. That income tax relief on interest payable and life assurance policies shall be revised in accordance with the proposals set out in that Report, *but only, in the case of life assurance policies, in respect of policies issued after the date on which the revision comes into force*.

13. To direct the Treasury and Resources Department to investigate a system of goods and services tax, including that introduced by the States of Jersey, and to direct the preparation of the necessary enabling legislation.

14. To direct the Treasury and Resources Department to take account of the above proposals when bringing forward recommendations as part of that Department's 2007 and future Budget Reports.

15. -

15. To direct the preparation of such legislation as may be necessary to give effect to their above decisions.

16. To authorise the Treasury and Resources Department to enter into discussions with Ministers and officials of the UK government to enable them to form a view as to which of the possible fiscal policies that might be adopted by Guernsey would command the support of the UK government at meetings of the Code of Conduct Group.

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy J A B Gollop
Seconded by:

Policy Council

Future Economic and Taxation Strategy

To insert at the end of the words in Proposition 2 ", but all other business conducted by institutions which are licensed by the Financial Services Commission, other than domestic and offshore insurance business (including captive insurance), collective investment schemes, and treasury or referred business, shall be subject to income tax at 5%".

Explanatory Note

The types of regulated entities which would be taxed at 5% under this amendment include banks (excluding those specific banking activities identified by the Policy Council). fiduciaries, money brokers, stock brokers, insurance and captive insurance managers, and fund managers.

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy D de G De Lisle
Seconded by: Deputy

Policy Council

Future Economic and Taxation Strategy

In proposition 5:

To delete ‘their distributed profits’ and to insert in place ‘a full attribution basis’

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy J A B Gollop
Seconded by:

Policy Council

Future Economic and Taxation Strategy

In Proposition 6, to delete £250,000 and substitute "£200,000".

<u>STATES OF DELIBERATION</u>

28th June 2006

Billet d'État No. XI

<u>AMENDMENT</u>

Proposed by: Deputy R R Matthews
Seconded by: Deputy T M Le Pelley

<u>Policy Council</u>

<u>Future Economic and Taxation Strategy</u>

To insert at the end of the words in Proposition 8 ", except that taxes on motoring shall be increased by more than is indicated in that Report".

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy P J Roffey
Seconded by: Deputy J P Le Tocq

Policy Council

Future Economic and Taxation Strategy

In Proposition 9, to delete “£60,000” and substitute £100,000”.

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy P J Roffey
Seconded by: Deputy J P Le Tocq

Policy Council

Future Economic and Taxation Strategy

In Proposition 9, to delete “increasing the Upper Earnings Limit for employers, self-employed, non-employed and employees to the equivalent of £60,000” and substitute: “increasing the Upper Earnings Limit for employers to the equivalent of £100,000, and for self-employed, non-employed and employees to the equivalent of £60,000”.

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy J A B Gollop
Seconded by:

Policy Council

Future Economic and Taxation Strategy

In Proposition 9, to delete "increasing the Upper Earnings Limit for employers, self-employed, non-employed and employees to the equivalent of £60,000" and substitute: "increasing the Upper Earnings Limit for employers to the equivalent of £100,000, and for self-employed, non-employed and employees to the equivalent of £50,000".

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy D de G De Lisle
Seconded by: Deputy

Policy Council

Future Economic and Taxation Strategy

To insert a Proposition immediately before Proposition 11, as follows:

'**10A**. That public sector expenditure must be curtailed and, over the next five years, a maximum target figure of no more than the amount spent in 2005 in cash terms (i.e. £290m) for ongoing annual revenue expenditure and £15m for annual capital expenditure must be established and maintained'.

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy M H Dorey
Seconded by: Deputy

Policy Council

Future Economic and Taxation Strategy

In Proposition 11:

(a) to substitute "a quarter" for "half";

(b) to add at the end of the words ", and to direct the Treasury and Resources Department to bring forward recommendations to raise any additional revenue which is needed to ensure that only a quarter of the Contingency Reserve is so used".

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy D B Jones
Seconded by: Deputy M H Dorey

Policy Council

Future Economic and Taxation Strategy

To insert at the end of the words in Proposition 12:

“, except for the proposal at paragraph 76 concerning the maximum value of principal private dwelling mortgages eligible for interest relief; and to direct the Treasury and Resources and Housing Departments jointly to study the level and scope of the application of interest tax relief on mortgages for principal private residences and the likely effects on the housing market, and to report back to the States with their joint recommendations”.

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy J A B Gollop
Seconded by:

Policy Council

Future Economic and Taxation Strategy

To add at the end of the words in Proposition 12:

", save that persons not eligible for mortgage interest tax relief shall be allowed income tax relief on borrowings up to £40,000".

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy J A B Gollop
Seconded by:

Policy Council

Future Economic and Taxation Strategy

To replace Proposition 13 as follows:

"13. That, in principle, a Goods and Services Tax system shall be introduced after 2008, and to direct the Treasury and Resources Department to investigate a system of goods and services tax, including that introduced by the States of Jersey, (such an investigation to include appropriate exemptions from such a tax), and to direct the preparation of the necessary enabling legislation.".

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy R R Matthews
Seconded by:

Policy Council

Future Economic and Taxation Strategy

To insert the following additional Propositions immediately after Proposition 13:

“**13A** To direct the Treasury and Resources Department to investigate a system of taxation on import or registration of motor vehicles, graduated according to their size.

13B To direct the Treasury and Resources Department to investigate appropriate systems of taxation on luxury goods and services.”

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy C D Brock
Seconded by: Deputy S J Ogier

Policy Council

Future Economic and Taxation Strategy

To add a proposition as follows:

"17. To direct the Policy Council to afford a high degree of priority to the identification of initiatives (including possible public/private sector partnerships) which are favourable to the development and/or revival of economic sectors other than the financial services sector, and to bring before the States practical proposals which, to some degree, will redress the current imbalance in the Island's economic base.".

Explanatory Note

The current Policy Council proposals focus very much on ensuring the continued development and expansion of the Island's financial services sector and associated activities.

While there are some notable business successes in other economic sectors, these proposals (amended or otherwise) may well:

- generate once again (possibly significant) wage inflation,
- necessitate higher immigration levels, and
- increase property/land values beyond sustainable levels.

These conditions, to a greater or lesser extent, will create an environment which further undermines the ability of traditional/new alternative economic sectors to be in a position to make a positive contribution to Guernsey's economic growth.

If passed, this amendment will require the Policy Council proactively to 'intervene' in free market forces (as it has already done and is intending to do with the Financial Services Sector) and to come back to the States with a series of initiatives which act as stimuli for other economic sectors to be able to prosper in this Island.

STATES OF DELIBERATION

28th June 2006

Billet d'État No. XI

AMENDMENT

Proposed by: Deputy J A B Gollop
Seconded by:

Policy Council

Future Economic and Taxation Strategy

To insert an additional proposition 17:

“17. (a) To increase the rates of document duty to the following:

1.0% (20p per £20) of the value of the transaction where the value exceeds £150,000 but does not exceed £250,000;

2.0% (40p per £20) of the value of the transaction where the value exceeds £250,000 but does not exceed £400,000;

3.0% (60p per £20) of the value of the transaction where the value exceed £400,000.

An additional 2.0% shall also be payable on transactions which exceed £150,000 and the property concerned is listed on the “Open Market” Register.

(b) To prepare necessary legislation including anti-avoidance legislation pertaining to material change of ownership of Guernsey real property by company share transfer.”