

13. FISCAL AND ECONOMIC PLAN: 2011 UPDATE

Mandate

13.1 The Fiscal and Economic Plan sets out the objectives, strategy and plans in place to fulfil the Fiscal and Economic Policy Group's mandate which is:

'to oversee the development of long-term fiscal and economic strategy'

Plan Policy

13.2 The Fiscal and Economic Plan ('FEP') is drafted with the following politically endorsed working assumptions:

- sustainable economic growth is desirable and is to be pursued as a means of increasing the standard of living of Guernsey's residents and providing tax revenues to fund ever increasing demands for public services, in particular education, health and law and order;
- the principle that the private sector is the engine of economic growth;
- the public sector's role is to provide the necessary competitive fiscal and macroeconomic environment to enable the private sector to flourish;
- fiscal policy's prime objective is to promote long term economic growth; and
- the maintenance of a competitive position for Guernsey is an imperative for future economic success.

13.3 Thus the maintenance of this competitive position is best served by a continued conservative fiscal stance of the States (and internationally competitive tax position) and maintenance of Guernsey's reputation for being a well regulated, tax transparent jurisdiction together with measures to control inflation (and hence costs) and supply side³ measures that foster innovation and improve the productivity of both the workforce and companies. Finally, continued investment in key strategic infrastructure is essential to maintain Guernsey's competitive position.

13.4 The general objectives of the plan, first set out in 2009, are as follows:

- Long run fiscal balance: spending within constraints of the Fiscal Framework.
- Continuing OECD Tier One Status.

³ *'Supply side'* the side of the economy concerned with the production of goods and services, usually in reference to the factors of production such as labour, land etc (as opposed to *'demand side'* which is concerned with the demand for such goods and services.)

- Average economic growth of 2% or more per annum.
- Stable and low inflation: RPIX 3.0%.
- Continuing full employment.
- Skilled, flexible labour market.
- Diversified, broadly balanced economy.
- Well regulated, competitive domestic markets.
- Modern key strategic infrastructure, with public capital investment averaging 3% of GDP.

13.5 The final objective set out in 2009 is also retained but within the common terminology of the SSP is separately classified as a ‘specific’ objective, that is, in place until such time as the States returns to fiscal balance:

- Real term freeze on aggregate States revenue expenditure.

Underlining the critical nature of competitive fiscal position for Guernsey the following general objective is added to the plan:

- Maintenance of an internationally competitive fiscal regime.

Underling the importance of financial services and its regulation to Guernsey’s economy, the following general objective is also added to the plan:

- Maintenance of an internationally respected financial services regulatory regime: adopting and applying international standards.

Plans, projects and programmes to achieve objectives

- General Objective: Maintenance of an internationally competitive fiscal regime.

13.6 The most significant current ongoing project concerning the core objective of maintaining an international fiscally competitive regime is the corporate tax review. Commenced in late 2009, following reported concerns with the zero/10 regimes by the EU Code of Conduct Group on Business Taxation (the ‘Code Group’), the project is a review of the corporate tax regime to meet the following five objectives, namely that any revised corporate tax regime for Guernsey:

- must be “competitive”;
- must be “internationally acceptable”;
- must “promote a sustainable economy in Guernsey”;
- must be based on a simple, solid rationale (and not over-complicated);
- must give rise to other benefits such as double taxation agreements;

- 13.7 This project is under the political direction of the Chief Minister, Treasury and Resources Minister and Commerce and Employment Minister. A public consultation was conducted during the summer of 2010 and provisional feedback on that consultation was published in November, 2010.
- 13.8 As was communicated by the Chief Minister to the States in June, 2011, the five key criteria of the review remain unchanged. However, as was also communicated in that statement, the Code Group will formally assess the ‘rollback’ proposals⁴ of the Isle of Man and Jersey, whose corporate tax regimes were assessed as harmful in February, later this year. In addition, the territorial regime of Gibraltar will also be subject to informal assessment by the Code Group. Following conclusion of these Code Group assessments, it is anticipated there will then be sufficient clarity for an informed evaluation of options to be undertaken.
- General objective: Long run fiscal balance: spending within constraints of the Fiscal Framework
- 13.9 The project to initiate an annual independent report, in line with the fiscal framework strategy, was completed. An independent report on the States fiscal performance was published in December 2010 and another report will be published at the end of this year.
- 13.10 The SSP implicitly sets out a strategy, which if successfully achieved, returns the States revenue budget to balance by 2015/2016. The 2010 independent fiscal performance report highlighted various risk factors to achieving that position and also stated that this ‘balanced’ position was most likely cyclical and a ‘structural’ deficit position would remain. Alongside the results of the corporate tax review, the FEPG will be reviewing the projected fiscal position and any supplemental measures that may be required to achieve a structural balance and reporting through Policy Council in due course.
- Specific objective: Real term freeze on aggregate States revenue expenditure
- 13.11 Until such time as the States returns to balance, this objective remains of paramount importance. The States successfully achieved this objective in 2010 and with the 2010 deficit of £37.4m it is vital that this is again achieved in 2011 and beyond.
- General objective: Continuing OECD Tier One Status
- 13.12 Committing to tax transparency and ensuring the States continues to be viewed in the highest regard internationally is an ongoing programme across

⁴ ‘Rollback’ being a Code Group term, the Code Group report of June, 2011, specified this term as ‘a removal of any harmful effects’, ‘harmful effects’ meaning effects that are non compliant with the Code criteria (see Guernsey Corporate Tax Review, Fiscal and Economic Policy Group, June, 21st 2010).

numerous policy groups outside FEFG including the External Affairs Policy Group. Maintenance of the OECD, tier one status is just one measure of success. Guernsey continues to negotiate to expand its list of Tax Information Exchange Agreements. In February, the Global Forum on Transparency & Exchange of Information for Tax Purposes (“the Global Forum”) independently confirmed that Guernsey has not only followed through its 2002 commitment to observe the OECD principles on transparency and exchange of information for tax purposes, but has made substantive developments in expanding its exchange of information network.

13.13 Following a public consultation in 2010, the States approved the movement to automatic exchange of information, under the measures Guernsey adopted equivalent to the EU Savings Tax Directive, during the course of 2011. In January, the UK’s HMT classified Guernsey as a ‘category 1’ jurisdiction in determining penalties for offshore non-compliance⁵ (acknowledging the transparency of Guernsey’s regime).

- General objective: maintenance of an internationally respected financial services regulatory regime: adopting and applying international standards.

13.14 In January, the International Monetary Fund (‘IMF’) published six evaluation reports which recognised and commended the high standards of financial regulation, supervision and stability that Guernsey has developed. Given the importance of financial services to Guernsey’s economy it is vital that the regulatory regime should maintain and retain the international respect it currently enjoys.

13.15 The approach of the Guernsey Financial Services Commission (‘GFSC’) should be to encourage and enhance respect between government, regulator and industry, but not in any way to compromise the operational independence of the GFSC in the discharge of its regulatory functions. The GFSC should continue, as in the past and as appropriate, to work collaboratively with the financial services sector, recognising that the effective but proportionate enforcement of the regulatory and supervisory regimes for which the GFSC is responsible is now expected by the international community.

13.16 In November 2011, the Chief Minister wrote to the Chairman of the Commission clearly setting out the objectives for financial regulation in the discharge of its regulatory functions. In discharging its functions with a view to achieving these regulatory objectives, the GFSC is expected at all times to bear in mind the importance of the financial services sector to Guernsey, and so the economic benefit it brings, and the importance of the regulatory regime to Guernsey’s competitiveness.

⁵ Penalties for any offences carried out in category 1 regimes are no higher than prior to January 2011. Those carried out within territories classified as category 2 and category 3, are 1.5 and 2 times greater respectively, reflecting the UK’s view of the lesser transparency of territories in those categories.

- 13.17 Of necessity, these objectives are expressed in general terms, and are in no particular order.
- Maintaining financial stability in the regulated finance sector.
 - Managing risk to the financial system and maintaining market confidence.
 - Ensuring fair, efficient and transparent markets.
 - Protecting financial services' customers.
 - Countering financial crime and the financing of terrorism.
- 13.18 The FEFG was consulted on the terms of reference of the Independent Evaluation Review presently being conducted on behalf of the GFSC.
- General objective: Average economic growth of 2% or more per annum
- 13.19 This objective was set with reference to the recent historic average performance of Guernsey, and as such should be viewed as Guernsey's 'natural' growth rate. There is no specific project to achieve this objective which should be successfully delivered if the States achieves its other fiscal and economic objectives.
- General objective: Stable and low inflation: RPIX 3.0%
- 13.20 The project arrangements for the anti-inflation strategy have been partially completed: a target for inflation has been set. Inflation has been stable and around target since late 2008. The arrangements for the overseeing of competition remain under development. The Commerce and Employment Department has prepared a new service development bid to enable the implementation of the competition regime in Guernsey and this will be considered during the SSP debate. The costs of the implementation of the competition law have been reduced in last year's unsuccessful bid as a result of greater co-operation and joint working between the Office of Utility Regulation and the Jersey Competition and Regulatory Authority.
- General objective: Continuing full employment.
- 13.21 Achievement of this objective is predicated on ensuring sufficient aggregate demand in the economy and by successful implementation of return to work policies of the Social Policy Plan and by successful achievement of the following objective related to the labour market.
- General objective: Skilled, flexible labour market.
- 13.22 As reported in the FEP 2010, Commerce & Employment has been working with the Social Security and Education Departments together with industry, the College of Further Education and the GTA – University Centre in the preparation of a Skills Strategy for Guernsey. At the time of writing the three

political boards are now considering the Skills Strategy Development Group's report and its recommendations for the future ownership and governance arrangements to deliver the proposed actions.

- General objective: Diversified, broadly balanced economy.

13.23 Whilst Guernsey has a more broadly balanced economy than many similar sized competitor jurisdictions, this objective is viewed as important for both the economy at large and within the dominant financial services sector. This higher degree of diversification is believed to have been a key factor in the resilience and robustness displayed by the Guernsey economy during the recent global downturn. Diversification for diversification's sake is clearly not intended. Guernsey has scarce and limited land and labour resources and reallocation of resources from high to low value activities would both reduce Guernsey's overall economic output and reduce taxation revenues. What is sought is development of high value, low physical footprint activities that leverage Guernsey's existing expertise and skill set of its workforce.

13.24 Commerce & Employment is in the process of the development of an economic development strategy that will set out key projects and timelines to deliver the plan which will be reviewed by FEFG during the course of 2011. Commerce & Employment has various projects under development to broaden the revenue streams of the finance sector including the development, with Jersey of a Channel Islands Aircraft Registry, introduction of image rights legislation and the proposals for development of Foundations legislation.

- General objective: Well regulated, competitive domestic markets.

13.25 Commerce and Employment has completed its review of Guernsey's Utility regulation regime following a detailed report by the Regulatory Policy Institute and a wide ranging consultation with stakeholders. The Department's States Report is due to be debated by the States in the autumn. With respect to competition law, as noted earlier the Department has prepared a new service development bid to seek new funding in 2012 to ensure that Guernsey has well regulated, competitive domestic markets.

- General objective: Modern key strategic infrastructure, with public capital investment averaging 3% of GDP

13.26 The delivery of this objective is through States public investment, the Island Resource Plan for Infrastructure, and maintenance of a stable, competitive environment where infrastructure providers such as telecoms have business confidence and are faced with sufficient demand to continue to re-invest.

13.27 It is recognised that the current Fiscal and Economic plan makes neither specific mention of the issue of land use nor any indication of the required allocation for economic use. The new economic development strategy together with the Island Infrastructure Plan will seek to set out estimates and

parameters of projected requirements to be balanced against other competitive demands for this scarce resource. It is hoped that within this it will be able to provide estimates of future demand for various land/property types so that guidance of required future requirements can be quantified and set out in the plan in future years to assist the planning prioritisation process.