Jersey's value to Britain

2 July 2013

CAPITAL ECONOMICS

Evaluating the economic, financial and fiscal linkages between Jersey and the United Kingdom

Stronger together — A symbiotic relationship

- Jersey runs £½ billion trade surplus with global exports
- 100,000+ jobs in Britain supported by Jersey
- £118 billion of UK banks' funding from Jersey
- £½ trillion of foreign investment in UK comes via Jersey
- More British tax generated by Jersey than lost through it
- Globalisation means demand for offshores here to stay

Jersey's value to Britain

Evaluating the economic, financial and fiscal linkages between Jersey and the United Kingdom

A report by Capital Economics for Jersey Finance Limited

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FOREWORD
BY GEOFF COOK, JERSEY FINANCE

We commissioned this report from Capital Economics to assess the value of Jersey to the United Kingdom. We believed that Jersey is a benefit to the United Kingdom, but did not have the data to demonstrate it. For the first time, this report provides the evidence base, confirming that Jersey is an overwhelming benefit to the UK.

The report argues that Jersey provides vital liquidity to the UK economy, facilitates inward investment from around the world and consumes UK exports, all of which support UK jobs. It also provides evidence that our constitutional role plays an essential part in delivering those benefits: if Jersey, and the other Crown Dependencies, ceased to be international financial centres, much of the finance we mediate would no longer find its way to the UK economy.

The research also addresses, openly and honestly, other aspects of Jersey's relationship with the UK, and in particular, the perceived 'tax gap'—the belief that UK residents use the island to evade or avoid tax. This report demonstrates convincingly that a very small proportion of Jersey's business relates to private individuals domiciled in Britain. It does, however, accept that there may be some tax leakage, a small portion via tax evasion (illegal), but primarily through tax avoidance (legal tax planning but under significant scrutiny, with focus, quite rightly, on aggressive avoidance schemes). However, the possible losses from tax evasion and avoidance are far outweighed by the taxes generated through the activity in the UK supported by Jersey.

It cannot be reiterated enough that Jersey has no interest in fostering abusive tax practices or money laundering. The standards and regulations in the island have been judged by the International Monetary Fund and the OECD, both identifying Jersey as one of the best regulated jurisdictions in the world. We are thus happy to share the full report to demonstrate our commitment to openness and transparency in our relationships with the UK and the wider global community.

This report is the first of its kind and, as such, Capital Economics had to find original solutions to some of the issues that arose. We feel that their methods were fair and their assumptions appropriate, but as with all research of this nature there is room for healthy debate over methodologies employed and approaches taken. Therefore, as part of our commitment to transparency, details of the data and methodologies used can also be found in the report. Readers can thus judge for themselves the quality of its findings.

The Jersey finance industry is diverse, robust and exceptionally international in its focus. We have a global reputation for being well-regulated, open and transparent, key attributes for the current and continued success of our financial services sector. Its client base is growing ever more global and that only serves to help the United Kingdom. I sincerely hope this report will resonate with policymakers, businesses and individuals, helping them in understanding the importance of supporting and preserving a world class financial centre in Jersey.

Geoff Cook
Chief Executive Officer
Jersey Finance Limited

2 July 2013

CONTENTS

1 INTRODUCTION AND SUMMARY

Capital Economics has been commissioned by Jersey Finance Limited to research and report upon the economic, financial and fiscal linkages between Jersey and the United Kingdom, and to ascertain the extent to which the Channel Island is an overall benefit or cost to its neighbour's economy.

This report combines new and innovative analysis of existing information, statistics and research with the results from a major quantitative and qualitative research exercise conducted among a large and representative sample of senior executives in Jersey's financial and related businesses. The purpose of the exercise has been to provide first order estimates of the general scale and shape of the many ways in which the economies of Jersey and the United Kingdom are linked, so the results should be treated with the appropriate caution. This work goes further than any previous study and, importantly, provides a thorough review of the sources and uses of assets administered or managed by the island's banks, funds and trustees. It also provides seminal estimates of Jersey's trade position as well as the bailiwick's impact on the British government's coffers.

This introductory section sets out and summarises the report.

1.1 Austerity is the context

Since their high in 2009, average real household incomes in the United Kingdom have fallen by 3.8 per cent and have subsequently only recovered 1.5 of those percentage points.[1] Despite tough austerity measures, government debt remains high, at 73.5 per cent of national income, and its net borrowing for 2012/13 was £66.9 billion.[2] It is not unsurprising then that the attentions of both the political and media worlds have been drawn to people and organisations being seen as not taking their fair share of the nation's pain, especially those not paying their fair share of the tax burden.

The Times' revelations in June 2012 about comedian Jimmy Carr's tax affairs may not have been the first uncovering of an unpalatable tax avoidance scheme, but it did put offshore financial centres centre stage in a then exploding debate. The 'K2' scheme, in which Mr Carr was reportedly enrolled, used Jersey as its home for a tax mitigation vehicle that pushed British tax law to its elastic limit, if not beyond, and may now be described as 'aggressive' tax avoidance. And since then, we have seen a string of stories about the corporate tax bills of major multinational companies like Google

1 Source: Office for National Statistics website. Latest data are for third quarter of 2012.
2 Source: Office for National Statistics website. Figure is for eleven months; it excludes March 2013.

and Starbucks, where internal 'transfer pricing' regimes are apparently used to ensure that offshore subsidiaries accrue much of the groups' profits thus attracting lower tax charges – although, in these instances, the offshore jurisdictions often turn out to be countries like Switzerland and The Netherlands.

For politicians in Westminster, the issue of offshore financial centres is further vexed – as a number of them are dependencies or peculiars of the British Crown. Indeed, in December 2008, the then Chancellor, Alistair Darling, tasked Michael Foot, a former executive director for banking supervision at the Bank of England and managing director of the Financial Services Authority, to report on the potential risks faced by British offshore financial centres.[3] More recently, the National Audit Office examined the potential impact on public finances of the British Overseas Territories, which comprise fourteen dependent administrations across the Caribbean, the Mediterranean, and the South Atlantic, Indian and Pacific Oceans, as well as the Antarctic.[4]

The focus of this report, though, is Jersey – situated, along with the islands of the bailiwick of Guernsey, off the Normandy coast of France. These Channel Islands and the Irish Sea's Isle of Man have a unique relationship both with the British monarchy and the Westminster government as 'Crown Dependencies'. They are self-governing, self-legislating, self-administering and self-financing but are loyal to the British Crown, with their courts subject to the decisions of the Judicial Committee of The Privy Council. The London parliament has only limited jurisdiction over the islands, while the islanders have no representation there. By custom, Westminster only legislates for the islands with their consent, and the United Kingdom government's responsibilities are restricted to defending the dependencies, maintaining their international relations and providing them with consular and diplomatic services abroad – although there is extensive cooperation in many other areas.

1.2 Jersey as an offshore financial centre

Jersey's freedom to legislate and govern, and determine its own taxes, has allowed it to become established as a leading centre for international financial services — a so-called 'offshore financial centre'.

In Section 2, we consider the broader context within which offshore financial centres and Jersey in particular operate.

3 Michael Foot, *Final report of the independent review of British offshore financial centres* (HM Treasury, London), October 2009

4 National Audit Office, *Tax avoidance: tackling marketed avoidance schemes* (The Stationery Office, London), 21 November 2012

To understand offshore finance, it is essential to recognise the growing impact of globalisation – whereby trade between countries gets ever larger, people are more mobile and willing to relocate abroad, and capital flows are increasingly international. In a world like this, where national boundaries have ever decreasing significance to people and to businesses, it should come as no surprise that there is strong demand for services that facilitate efficient and secure cross-border transactions. Jersey and other offshore centres provide environments in which international business can be conducted without fear of double taxation, or legislative and administrative bias in favour of a 'home' counterparty. They often provide regulatory and supervisory regimes better tailored to the needs of their specific clientele, and can provide a safe haven for those carrying on business in unstable and risky countries. Jersey, in particular, has robust legislation for the creation of trusts and other asset and investment management and pooling vehicles, which makes it attractive to individuals, businesses and institutions with cross-border asset portfolios.

Notably, these drivers of offshore demand have little to do with evading or avoiding domestic taxation. There may be some offshore centres that provide secretive shelter from other jurisdictions' domestic taxes, but not Jersey (nor the other Crown Dependencies). Tough anti-money laundering laws and robust regulation make the bailiwick an ill-advised choice for would-be tax evaders – while efforts on both sides of the Channel mean that the scope for unwanted avoidance schemes to use the island is all but eliminated.

Jersey is a significant player in the offshore market although its footprint is nowhere near as large as the likes of Luxembourg, Switzerland or the Cayman Islands. Its scale is reflected in the mix of jobs and businesses found on the island. Financial and related businesses dominate, and account for a quarter of all jobs and two-fifths of economic activity. But this level of specialisation in a certain sector is not unusual in an economy with only 55,000 jobs; indeed, it would be quite typical among British local authorities of a similar size.

1.3 The economic linkages

In Section 3, we review the economic linkages between Jersey and the United Kingdom.

Although only fourteen miles off the French coast, the island's physical connections are mostly to southern Britain. The schedule of aeroplane flights in and out of Jersey airport is overwhelmed by British destinations. There are more ferry sailings to and from France than England, but almost all cargo and freight capacity goes north as does the majority of international telephone and digital traffic.

But these physical links to Britain mask a very different global pattern of trade conducted by the island's businesses. Through international trade, Jersey brings value into the sterling area from across the world and shares the spoils with the United Kingdom.

We estimate that Jersey ran an overall trade surplus broadly in the region of £0.6 billion in 2010, which is equivalent to sixteen per cent of its national output, and compares to the United Kingdom's trade deficit of two per cent for that year. Although there are tourism, agricultural and other revenues, export performance is dominated by financial services – with its trade conducted with many far flung markets as well as Britain and Europe. Indeed, the share of Jersey's non-sterling exports going to the higher growth emerging markets of Asia, South America and Africa compares favourably to Britain's recent achievements. But, as the island's imports come almost entirely from southern England initially, its balance with the United Kingdom alone is likely to be quite different. Indeed, we estimate that the island ran a trade deficit broadly in the region of £0.4 billion with it in 2010 – supporting 11,000 British jobs.

1.4 The financial linkages

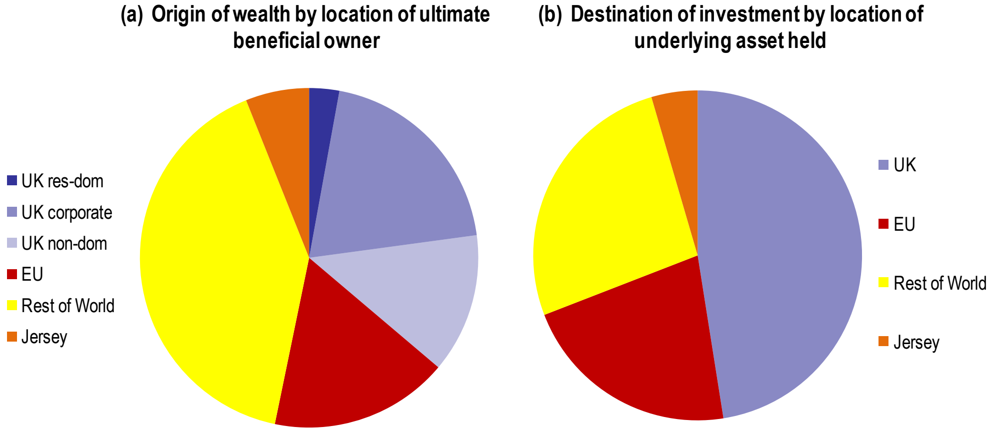
In Section 4, we consider the business conducted by Jersey as an international financial centre and explore its implications for the United Kingdom.

In addition to using extant data from regulatory, government and industry sources, we conducted a detailed quantitative survey and programme of in-depth interviews with banks, trust companies, fund administrators and managers, corporate service providers, legal practices and accountancies in Jersey – in order to capture new insight into who their ultimate customers are and who benefits from their activities. Our survey covered businesses employing two-thirds of all the island's finance workers, and is a robust and representative sample.

Overall, we estimate that Jersey is custodian of £1.2 trillion of wealth: £200 billion in banks; £400 billion in trusts established by private individuals; £400 billion in specialist structures for businesses and institutions; and £200 billion in administered or managed funds.

The sources of this wealth are truly international. We estimate that three quarters of it originates from ultimate beneficial owners (as depositors, investors and settlors) who are not domiciled in the United Kingdom – with North America, Asia Pacific and the Middle East all being major contributing regions. Over £150 billion are the foreign assets of individuals currently resident in Britain but not liable for tax there on their foreign source income, the so-called 'non-doms'. This makes Jersey a major conduit for non-dom foreign wealth, which has been a consistent plank of British policy for attracting wealth and talent under successive governments. (See Figure 1.)

Figure 1: Summary of sources and destination of Jersey managed wealth



Sources: Capital Economics' survey 2012/3

But the uses of these funds disproportionately benefit the United Kingdom. We estimate that almost one half of the combined value held in the stewardship of the island's trusts and other structures, funds and banks has been invested in assets located in Britain. By this, we mean ultimately located in Britain, and not assets with funding simply intermediated through the City of London. Overall, Jersey's financial services sector intermediates almost one pound in every twenty of investment by foreigners into the United Kingdom. This scale of investment could potentially support 112,000 British jobs.

Much of this investment into Britain depends upon the status of Jersey and the other Crown Dependencies. Jersey's practitioners believe that four-fifths of their business would leave the sterling zone if the Crown Dependencies didn't exist and relocate to other offshore centres. These other centres are unlikely to have the same affinity with the City of London and the United Kingdom as Jersey; their locus of operation could just as easily be New York, Hong Kong or Dubai.

Our survey also provides insight into the global nature of the different types of financial services activities undertaken on the island.

Jersey's banks largely service the needs of the expatriate 'mass affluent' and internationally footloose high net worth individuals, as well as associated corporate and institutional clients. They attract deposits and funding from across the globe. Almost three-fifths of the island's over £200 billion of banking funds come from deposits and other instruments ultimately provided by customers from beyond the European Union, while less than a quarter arise from the United Kingdom. There is, though, little lending business conducted from the island. Instead, the banks upstream the bulk of funds to their parent companies which are typically in London. The United Kingdom's banking sector is bolstered by almost £120 billion of funding received this way, which is equivalent to 1½ per cent of its total balance sheet or two-fifths of the overall customer funding gap. The up-streaming model brings real economic benefits to the United Kingdom, both through the extra liquidity it provides and through the revenue it generates from intermediation. Moreover, in recent years, the ability of the part-nationalised banks to secure funding through Jersey has eased the burden on British taxpayers.

The island's legislation allows for the creation of trusts and other asset holding vehicles. A variety of firms – from bank subsidiaries through legal practices to independent specialists – offer services to clients from across the world to assist in the establishment and operation of such entities. An estimated £400 billion of private individuals' assets and £450 billion of corporate and institutional assets have been settled in Jersey trusts or similar vehicles, with clients attracted by Jersey's tax neutrality, robust regulation of service providers, and well-established and tested legal framework. This is another of Jersey's highly international business activities. Two-fifths of the private individuals' assets come from United Kingdom non-doms, and a slightly larger share from beneficial owners who are residents of countries beyond the European Union – while over half of corporate and institutional assets are from outside the sterling area.

Jersey is also a centre for the investment funds industry, with almost £200 billion of net assets administered or, less often, managed there. Two fifths of the investment into Jersey funds comes from the United Kingdom. Over 40 per cent of investors are located outside the European Union, with one quarter of the total asset value originating in North America.

1.5 The fiscal linkages

In Section 5, we address the fiscal linkages between Jersey and the United Kingdom, especially supposed tax leakage.

The impression that some have that, because it is a 'dependency' of the Crown, Jersey is a drain on British public services is unfounded.

Whitehall is responsible for the island's defence and its representation to governments abroad, with Jersey's British passport holders also accessing consular support from the United Kingdom's embassies and consulates. The two governments have negotiated an appropriate contribution from Jersey for these services, which is paid in the form of a Territorial Army unit funded by the bailiwick. On a simple per capita calculation, the islanders' proportionate use of defence and foreign representation could be estimated to 'cost' British taxpayers in the region of £60 million per annum. But such an allocation of costs is only notional; even if the United Kingdom stopped defending and representing Jersey, it is unlikely to spend any less on its armed forces or diplomatic service.

In all other respects, the States of Jersey operate separately, and at their own expense – albeit often with close coordination with their British counterparts. Islanders fund their own health system. The island's schools, colleges and childcare provisions are all funded locally – while the tuition fees and maintenance costs for local young adults studying in British universities and colleges are borne entirely by the bailiwick. Jersey funds its own policing and jail. And, Jersey households watching television have to purchase the same license as those in Britain, in order to fund the BBC. It is also sometimes argued that the island benefits from an implicit insurance policy underwritten by the Westminster government under which it would bail-out the bailiwick if it got into severe trouble. But, no 'claim' has ever been made against such a 'policy' and it is unclear whether there is any real enforceable obligation on the United Kingdom to do so – or whether it is ever likely to be needed. This then begs the question whether an informal and unused guarantee is worth the paper it isn't written on.

The elephant in the room, though, is tax.

There is a widespread belief that Jersey, Guernsey and the Isle of Man are tax havens and are used by businesses and individuals both legally and illegally to reduce the tax they pay to British authorities. This belief appears to be based largely on impressions set during the Super Tax era of the 1970s and sporadic media exposés on the tax affairs of big companies and celebrities. The extent to which there are revenues rightfully due to the government that are leaking away has become a turbulent political issue in the current context of fiscal austerity.

There is little hard evidence about the actual scale of offshore tax abuse and almost no assessment whatsoever of the role of Jersey or the other Crown Dependencies. This lack of evidence should be no surprise in itself. Those involved in tax avoidance and, especially, evasion will have little desire to publicise the activity, and every interest in hiding it. Meanwhile, those trying to demonstrate the 'cleanliness' of their jurisdictions find it almost impossible to prove that little or no such activity takes place there because you can't prove an absence of something simply by failing to find it.

We can't and don't offer a watertight solution to this research conundrum. It can, though, be explored from different directions in order to draw meaningful conclusions about the envelope within which there may be leakage of what might otherwise be legitimate British tax revenues.

Little of Jersey's business relates to private individuals domiciled in Britain. Less than a tenth of bank deposits and only four per cent of private trust assets originate from them. The introduction of the European Union savings directive and tough anti-money laundering legislation in Jersey, combined with successive strengthening of the tax code in Britain, means that there is now limited scope for unlawful evasion of British taxes there.

In the 2013 Budget, HM Treasury estimate a combined benefit of £210 million per annum to the exchequer of the three new inter-governmental agreements with the Crown Dependencies. These agreements, based on the provisions of the United States' *Foreign Account Tax Compliance Act* ('FATCA'), provide for automatic information exchange between the three jurisdictions' tax authorities and HM Revenue and Customs, and ensure that the Jersey, Guernsey and Isle of Man-held interests of British taxpayers are reported fully.

Our own calculations, based on cautious assumptions and prior to the adoption of a new FATCA-type reporting regime, suggest that the maximum level of tax evasion plausibly facilitated through Jersey was £150 million per annum in 2011. The actual level was probably much lower.

Automatic information exchange will not necessarily banish all evasion of British tax from the island – but, given the States' tough anti-money laundering regulations and its criminalisation of the handling of the proceeds of tax evasion as well as the comprehensive coverage of the FATCA regulations, whatever will be left will likely be immaterial.

There is, though, the open question of tax avoidance, which may be defined as the lawful under payment of tax through means that are against the spirit of the law and/or intention of parliament.

HM Revenue and Customs' tax gap analysis suggests that nationally there is £2.9 billion of tax lost annually through avoidance of income tax, national insurance, capital gains tax, inheritance tax and stamp duty. Even on the basis of the most aggressive assumptions, we calculate that no more than £0.4 billion of this can be mediated through Jersey and, in all likelihood, it is much less. Furthermore, as a 2009 report commissioned from Deloitte by HM Treasury demonstrated, Jersey does not offer firms operating in the United Kingdom with meaningful opportunities to mitigate their corporation tax liability there.

Overall, we judge that, based on 2011 data, a maximum of £0.6 billion per annum of British taxes can leak through evasion or avoidance using Jersey vehicles – although, in all probability, the actual number is much lower.

Meanwhile, the Westminster government benefits from the taxes it levies on the jobs and economic activity stimulated in Britain through Jersey's financial and trade links. Indeed, the tax receipts from the Jersey-catalysed activity alone could be in the order of £2½ billion per annum – substantially outweighing any tax leakage.

1.6 Overall benefit of Jersey to the United Kingdom

In Section 6, we pull together the various strands of our research and make a tentative attempt to evaluate the overall benefit or cost of Jersey to the United Kingdom economy.

As with any exercise of this nature, there are margins of error. However, we have approached this task cautiously – and, where necessary, have given the benefit of the doubt in favour of Jersey being a cost to the United Kingdom.

Bringing these various factors together, we find that Jersey is a benefit to the United Kingdom economy, and on the basis of our broad calculations could be supporting in the order of 180,000 British jobs. (See Figure 2.)

Some may argue that, without Jersey or the other Crown Dependencies, the foreign investment, bank funding, etc currently routed via the islands would come to the United Kingdom regardless. This would be dangerous complacency.

The wide geographical spread of Jersey's client base means that it is attracting investment from businesses and individuals who wouldn't necessarily see the City of London as their first choice of financial centre. Around 30 per cent of the investment through Jersey originates from outside the London time zone, and would more likely have a locus around New York, Hong Kong or Dubai; this alone is worth an estimated 51,000 British jobs. Moreover, the results of our survey indicate that 84 per cent of the bailiwick's financial services business would be at risk of leaving the sterling zone if Jersey did not exist. This business (and the consequent investment) is likely to migrate to other offshore centres – and not London, and could cost the equivalent of around 150,000 British jobs.

With research of this nature, there is always room for healthy debate over the methodologies deployed and approaches taken. There are also, of course, margins of error associated with any survey results and consequent quantitative analysis. Nevertheless, taken together, the various strands of analysis point unquestionably to Jersey being a material overall and additional benefit to the United Kingdom economy.

Jersey and the United Kingdom are linked in a symbiotic relationship. One benefits and supports the other, and vice versa. And, what harms one will also harm the other.

Figure 2: Summary of Jersey's indicative impact on the United Kingdom economy

Indicative estimates of jobs supported in the United Kingdom, 2011	Gross	Net additional
Trade	11,200	2,700 - 7,400
£0.4 billion trade deficit with United Kingdom		
Banking (intermediation)	13,700	2,500 - 6,900
£120 billion of deposits upstreamed and intermediated in the United Kingdom		
Investment	111,800	34,400 - 93,900
£560 billion foreign investment in United Kingdom assets through Jersey		
Business referred	3,600	900 - 3,000
£230 million of business referred from Jersey to the United Kingdom		
Tax generated	51,600	13,900 - 39,000
£2½ billion United Kingdom tax generated from activity catalysed by Jersey		
Tax leakage	*(14,200)*	*(2,300)*
£0.6 billion maximum potential tax leakage through Jersey		
Provision of defence and foreign assistance	*(1,400)*	*(1,400)*
£60 million maximum pro-rata allocation of United Kingdom public spending to Jersey		
Total jobs supported in the United Kingdom	**176,300**	**50,700 - 146,500**

Source: Capital Economics

2 BACKGROUND AND CONTEXT

In this section, we examine the broader environment within which Jersey sits, in particular economic globalisation and the consequent growing role for offshore financial centres. Our key findings are:

- **Offshore centres have evolved to meet the needs of global businesses and internationally footloose individuals, and this demand looks set to grow**
- **Jersey is a significant offshore financial centre although smaller than the likes of Switzerland and the Cayman Islands**
- **Jersey's economy is concentrated in financial services, but this scale of specialisation in a single sector is not unusual for a geography of its size**

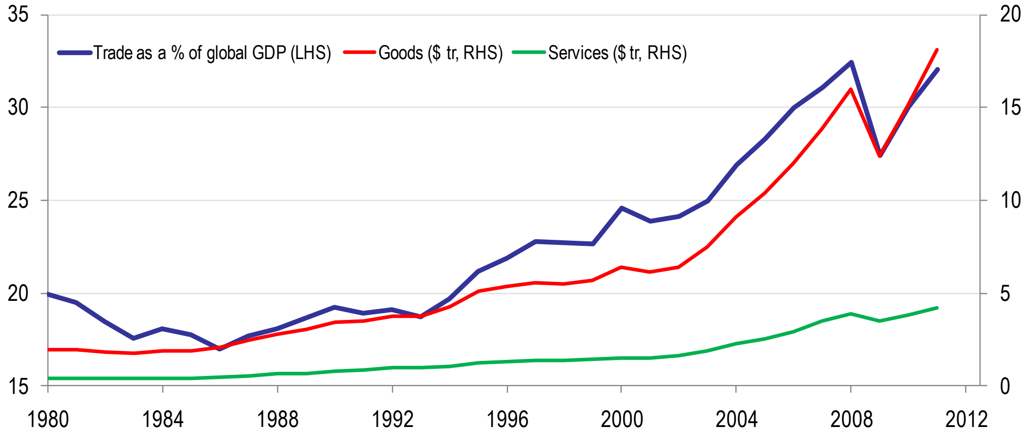
First, we discuss the trends in globalisation and how they have shaped a role for offshore financial centres. Second, we look at the nature and scale of offshore activity in Jersey and consider the island's economic structure.

2.1 Globalisation and offshore financial centres

Globalisation, or the economic interdependence of nation states, continues apace – despite the recent recessions in many major 'Western' economies and sharply slowed growth in emerging markets. International trade is increasing, while labour, enterprise and capital are all more mobile.

The value of goods and services traded between countries is growing at a much faster rate than the national economies themselves. Whereas world output grew by 5.9 per cent per annum over the past 30 years, cross-border trade has expanded by 7.5 per cent each year. Trade now accounts for 32 per cent of global gross domestic product, compared to 20 per cent 30 years earlier. (See Figure 3.) The current expansion of the so-called 'BRIC' countries, namely Brazil, Russia, India and China, has boosted trade, while the anticipated future growth in the Asia-Pacific region, South America and, eventually, Africa ensures the trend is set to continue for decades.

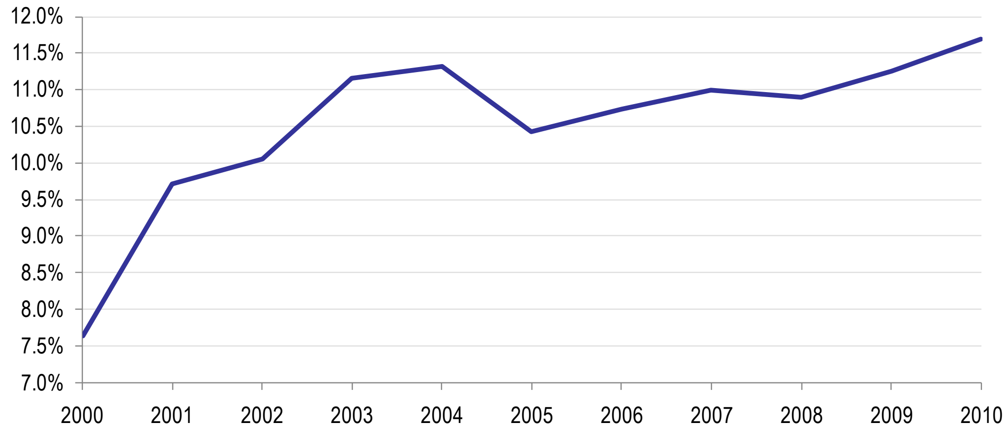
Figure 3: Comparison of world GDP and trade volumes



Source: International Monetary Fund, *World Economic Outlook*

People are increasingly mobile internationally. For developed countries who are members of the Organisation for Economic Cooperation and Development, the share of their population born outside their resident country has risen from 7½ per cent to almost twelve per cent in just a decade. (See Figure 4.) International migration is not a new phenomenon, but its scale is – especially for a peacetime period. Improved connectivity and greater affluence are key drivers, especially the improved connectivity of an increasingly affluent, mobile and eager 'middle class' in the newly emerging markets. But behind the trend are other factors including the growth in multinational businesses – which not only direct staff to a posting abroad but can create 'serial expatriates', who move between numerous foreign and home postings during their careers.

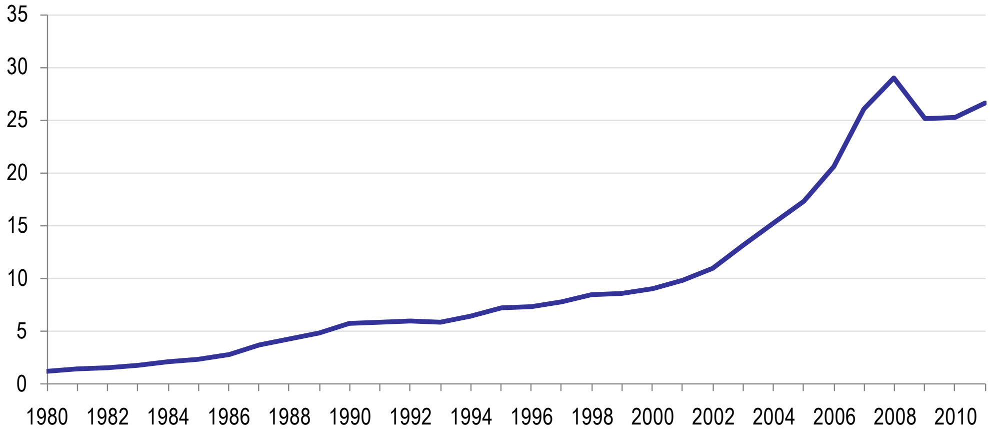
Figure 4: Share of OECD population born outside resident country



Source: Organisation for Economic Cooperation and Development

Likewise, capital also now flows more freely around the globe. Global external liabilities, a measure of the scale of cross-border lending and borrowing of internationally active banks, have risen from just over $1 trillion in 1980 to over $25 trillion in 2011. (See Figure 5.)

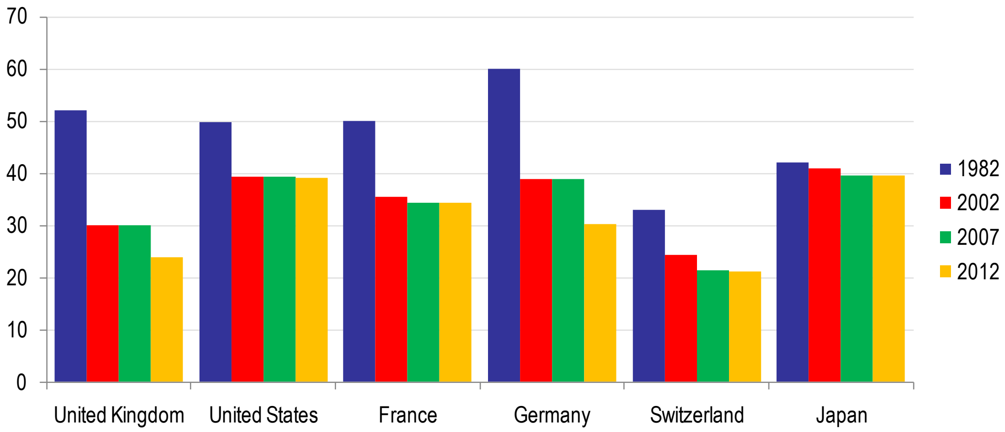
Figure 5: Global external liabilities ($ trillion)



Source: Bank for International Settlements

Indeed, increasingly footloose capital and growth in multinational companies have spurred tax competition between countries – with rates of corporate tax being driven down across major economies. (See Figure 6.)

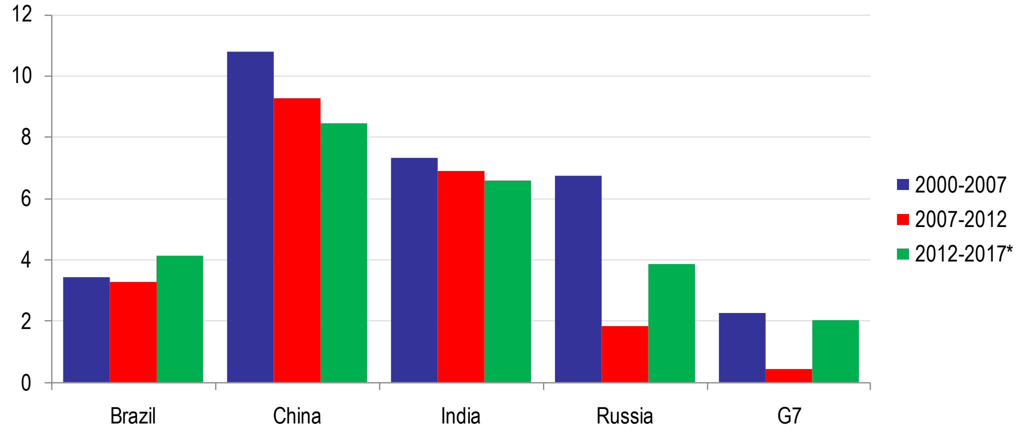
Figure 6: Overall corporate tax rates including national and sub-national headline corporate taxes (%)



Source: Organisation for Economic Cooperation and Development

Meanwhile, the shape of the global economy is changing – with the economic superpowers of the twentieth century being overtaken progressively by the BRIC countries and, in future, by other emerging market nations. (See Figure 7.) With this, a greater share of the world's wealth will be held by individuals and organisations from these regions.

Figure 7: Comparison of average annual rates of economic growth (%)



Source: International Monetary Fund, *World Economic Outlook*. * International Monetary Fund forecast

However, not all of these emerging higher growth countries are necessarily secure locations to conduct business or hold wealth. Such 'transitional' economies may not have stable governments. Or, the lack of an independent judiciary may call into doubt the consistency, reliability or enforceability of their legal codes – while, in some countries, property ownership rights remain poorly defined and defended, or the banks weakly regulated and poorly resourced. (See Figure 8.)

Figure 8: Exemplar results from the World Bank's 'Doing Business' report, 2012

	Ease of doing business ranking	Investor protection	Cost of starting business
	Ranking of selected countries (1=top, 185=bottom)	Investor protection index (0=lowest, 10=highest)	% of income per capita
Singapore	1	9.3	0.6
United States	4	8.3	1.4
United Kingdom	7	8.0	0.7
Australia	10	5.7	0.7
Japan	24	7.0	7.5
South Africa	39	8.0	0.3
China	91	5.0	2.1
Russian Federation	112	4.7	2.0
Brazil	130	5.3	4.8
India	132	6.0	49.8
Central African Republic	185	4.0	172.6

Source: International Finance Corporation, World Bank Group

In a world where national boundaries have ever decreasing significance to people and to businesses, it should come as no surprise that there is demand for services that facilitate efficient and secure cross-border transactions.

This is the context within which offshore financial centres operate. They have evolved to meet the needs of global businesses and internationally footloose individuals. These needs include resolving the complexities of the taxation of cross-border transactions – but are not limited to tax affairs alone.

Typically small self-governing jurisdictions, many offshore centres have developed consistent tax codes, legislation and financial regulations (and fostered appropriate expertise within local businesses) to deliver:

- **Jurisdictional neutrality** – The offshore centre provides a location that is independent of the home jurisdictions of the various counterparties where transactions can be conducted, whilst adding little or no additional cost. This can be important, for example, when forming joint venture vehicles between organisations from different countries, and maybe helpful when establishing a secondary market for the resale of assets and portfolios

- **Administrative convenience** – The offshore centre provides a neutral location for administrative tasks ensuring that the business or individual can remain footloose without risk of additional tax or other costs

- **Tax neutrality** – The offshore centre permits assets to be pooled, grown and/or distributed across borders without imposing any additional taxation. This is important, for example, when developing fund structures to attract international investors and/or to invest in a portfolio of assets across borders. It ensures that investors are not exposed to double taxation, and only pay taxes due to the authorities in their domicile

- **Regulatory specialisation** – The offshore centre is able to concentrate resources on regulating specific types of financial sector activity effectively, while larger countries have to spread regulatory resources across a wider range of activities. This bespoke regulation allows specific sectors locating in offshore centres to avoid the unintended inefficiencies of 'catch-all' regulation of larger jurisdictions

- **Country risk mitigation** – The offshore centre provides a safe haven, where assets can be kept protected from potential loss, damage or sequestration resulting from socio-political instability or delinquent legal, regulatory or enforcement institutions in a particular country

Some of the offshore centres may also be known for their domestic taxation regimes. Many offer a low tax environment for their residents and the businesses operating there. Low rates of tax on domestic incomes, profits and sales are achievable because of the levels of prosperity locally, which are supported by employment in higher value finance and related jobs. Meanwhile, some offshore centres also offer favourable tax rates to high net wealth immigrants. This is a policy deployed by some larger countries too, such as the United Kingdom with its 'non-dom regime'. (See Figure 9.)

Figure 9: The United Kingdom's 'non-dom' taxation regime

Individuals who are both resident and domiciled in the United Kingdom are liable to British taxation on their worldwide income and gains. However, those who are resident but not domiciled — the 'non-doms', who are typically high wealth immigrants — have only to pay taxes to HM Revenue and Customs on the foreign income and gains that they remit to the United Kingdom.

Since 2008, long term 'non-doms' wishing to retain their status beyond seven years have to pay £30,000 per annum and, since 2011, those wishing to stay beyond twelve years have to pay £50,000.

It would, of course, be naive to assert that offshore jurisdictions were and are always only used for the legitimate motives above. Some 'tax havens' have combined their sovereign or quasi-sovereign status with banking secrecy laws and weak anti-money laundering regulations. They have sometimes left open doors to individuals and organisations evading rightfully owed tax in their home or other countries, as well as those aggressively avoiding tax or hiding the proceeds of crime.

But not all offshore centres are secretive tax havens. Indeed, Jersey and its fellow Crown Dependencies have been at the forefront of international developments to improve banking transparency and clamp down on criminality, including tax evasion. For example, Jersey introduced its proceeds of crime legislation in 1999, which makes evading tax in other jurisdictions illegal, three years before the United Kingdom's *Proceeds of Crime Act 2002* and over a decade ahead of the Financial Action Task Force including tax evasion as a predicate offence in its 40 recommendations when they were revised in February 2012.

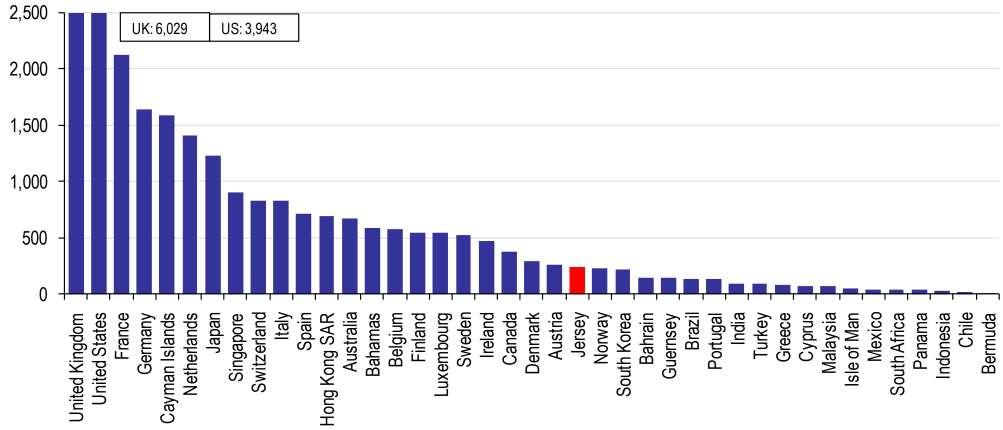
2.2 Jersey as an offshore financial centre

Although there may be debate and ambiguity over what precisely constitutes an offshore financial centre, Jersey is one of them.

The bailiwick is the most populous of the three Crown Dependencies, but is only one among a large number of low tax, tax neutral or offshore jurisdictions across the globe. From the Caribbean through the Mediterranean to the Indian and Pacific Oceans, self-governing and self-legislating islands and peninsulas offer specialist international financial, corporate and maritime services – as do the likes of Andorra, Liechtenstein, Luxembourg and Switzerland. Indeed, many larger economies, such as Belgium, Ireland, the Netherlands, the United Kingdom, and the United States, carry on substantial offshore or non-domestic banking, investment and corporate activity.

Data from the Basel/Bâle-based Bank for International Settlements gives an indication of the relative scale of Jersey's international financial activity against its peers. With an external position of around $240 billion, its international financial activity is roughly half that of Luxembourg and less than one third of Switzerland's. (See Figure 10.)

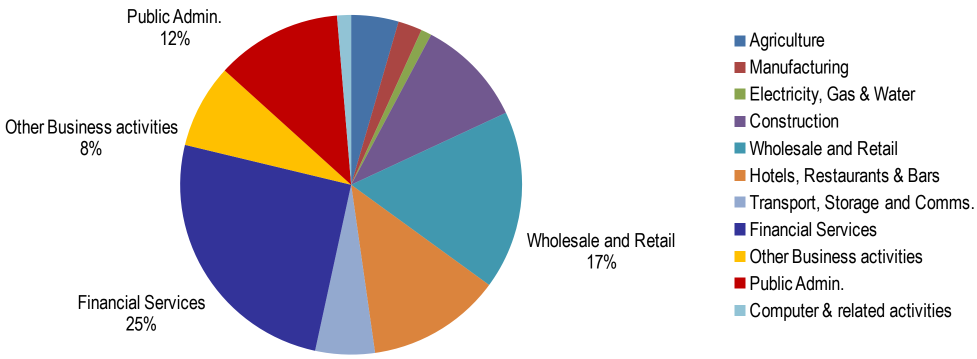
Figure 10: External liabilities of banks in all currencies vis-á-vis all sectors, December 2011 ($ billion)



Source: Bank for International Settlements

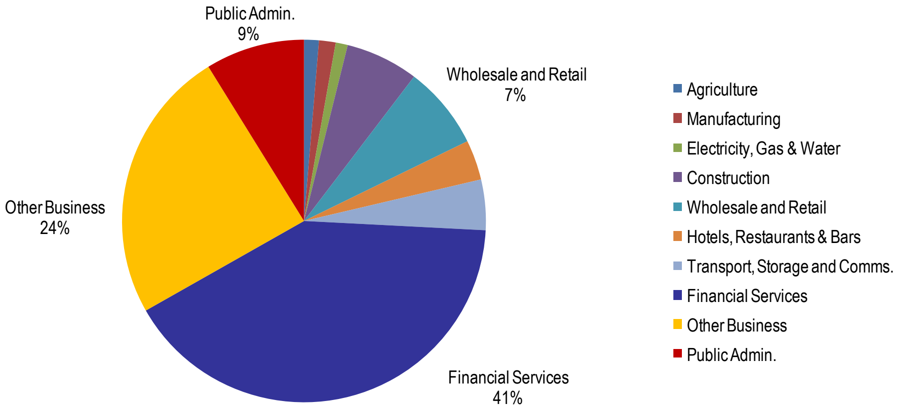
Jersey's focus on international finance is reflected in its labour market and economic activity statistics. Around one quarter of the island's jobs and two-fifths of its gross value added are accounted for by finance and related businesses. (See Figure 11 and Figure 12.)

Figure 11: Jersey's employment by industry, June 2012



Source: States of Jersey

Figure 12: Jersey's gross value added by industry, 2011



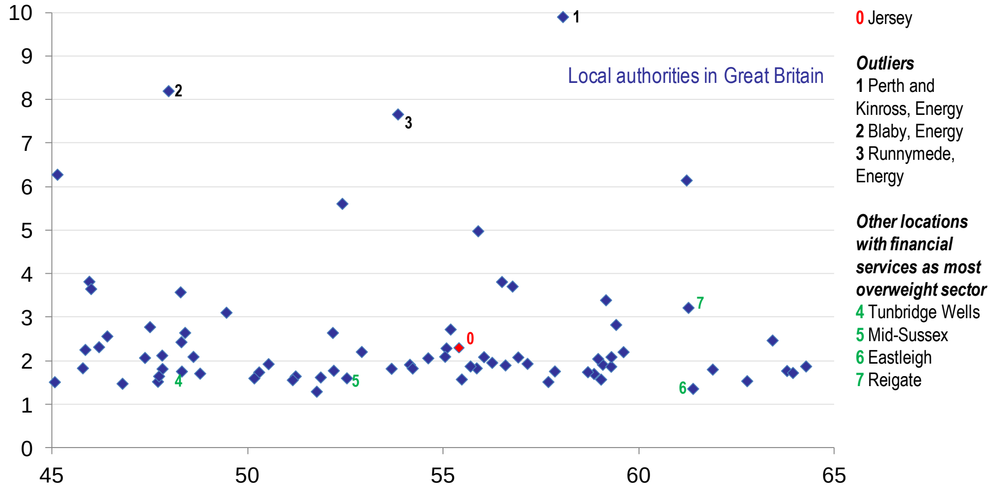
Source: States of Jersey

This specialisation in finance is over twice that found in Britain. The industry accounts for 25 per cent of jobs in Jersey and eleven per cent in the United Kingdom.[5]

Such concentration on a single sector is unremarkable for an economy squeezed onto a 45 square mile island. To illustrate this, we have examined the industrial structure of all local authorities in Great Britain with employment levels similar to Jersey. Although the island has 2½ times the United Kingdom's rate of employment in finance, this degree of specialisation is typical of authority areas of a similar size. This can be seen in Figure 13, which shows a variety of United Kingdom local authorities, plotted against the 'location quotient' for the sector in which they have the highest concentration of employment. The location quotient is a measure of how concentrated employment is in a particular sector relative to the national average. In this context, Jersey's location quotient (highlighted in red as point 0) is not exceptional for an administrative area of its size.

[5] Due to differences in data collection and reporting, the comparison is not on a precisely like-for-like basis.

Figure 13: Location quotient of most overweight sector (vertical), GB=1, and employment (horizontal) (thousands), 2011



Source: Capital Economics' analysis of labour statistics from States of Jersey and Office for National Statistics

3 ECONOMIC LINKAGES

In this section, we examine Jersey's real economic linkages with the rest of the world. Our key findings are:

- **Jersey's physical links, including scheduled airline flights, shipping routes and telecommunication connections, are predominantly with the United Kingdom**
- **Jersey runs an overall trade surplus of around £0.6 billion a year, but a trade deficit with the United Kingdom in the region of £0.4 billion**
- **Jersey's net trade supports over 11,000 jobs in the United Kingdom generating £½ billion of gross value added**

First, we outline Jersey's international air, sea and telecommunication connections. Second, we produce an indicative trade balance as well as broad estimates for exports and imports of goods and services and the impact that these have on the United Kingdom.

3.1 Jersey's connectivity

An examination of Jersey's transport and communications connections provides a good starting point for understanding its international economic linkages, and illustrates the dominance of the United Kingdom as the key physical trading partner.

The island's airport served almost three-quarters of a million passenger arrivals in 2011, and is set to host almost 400 outbound flights per week in the 2013 peak season. Jersey's air network is dominated by connections to the United Kingdom, and especially southern England. Indeed, many of Jersey's air links to Europe and the rest of the world are derived by connecting with flights from major British airports to the eventual destination. Direct flights to continental Europe account for just one-in-twenty peak season departures. (See Figure 14.)

Figure 14: Number of outbound flights per week, 2013 peak season, and passenger arrivals, 2011, in parentheses

Flights per week in peak season 2013 and (passenger arrivals 2011)					
United Kingdom (625,000)				**Crown Dependencies (77,000)**	
Aberdeen	1	Leeds Bradford	3	Guernsey	114
Belfast	3	Liverpool	7	Isle of Man	3
Birmingham	18	London City	11		
Bristol	16	London Gatwick	62	**Other destinations (33,000)**	
Cardiff	5	London Luton	4	Amsterdam	4
Doncaster sheffield	2	London Southend	16	Berlin	1
Durham Tees Valley	1	London Stansted	4	Cork	2
East Midlands	7	Manchester	7	Dublin	4
Edinburgh	4	Newcastle	3	Dussledorf	2
Exeter	13	Norwich	2	Geneva	1
Glasgow	4	Oxford	0	Paris Charles de Gaulle	4
Humberside	1	Southampton	47	Zurich	4
Inverness	1				
Total			**242**		**139**

Source: Capital Economics analysis of Jersey Airport, individual airline websites and Jersey Tourism statistics

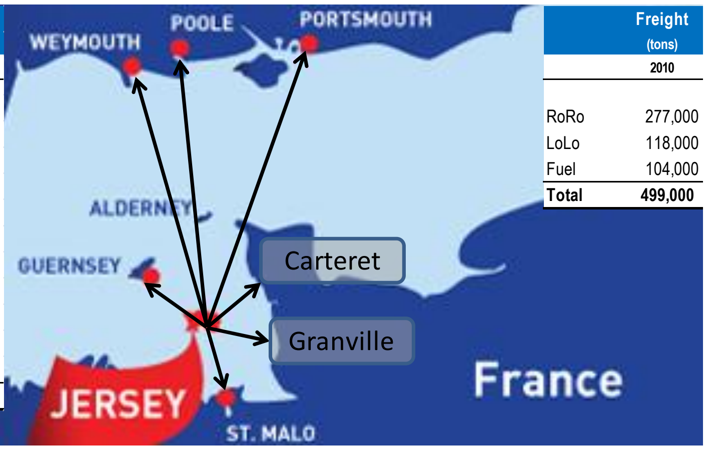
Jersey's seaborne connections are less biased towards the United Kingdom, which isn't surprising given the island's proximity to the French coast. The nineteen ferry sailings per week to Great Britain planned for the 2013 peak season compares to a schedule of 34 crossings to France. (See Figure 15.)

But the nature of the crossings varies.

Two of the French routes, to Carteret and to Granville, are passenger-only, while a fast 'roll-on-roll-off' catamaran ferry mostly serves St Malo. Although the latter can carry cars and vans, it has limited capacity for larger goods vehicles or freight. Meanwhile, a fast ro-ro catamaran operates between the Dorset ports and Jersey, and a conventional ro-ro ferry, with significant heavy goods vehicle capacity, runs from Portsmouth. In addition, there is a regular 'lift-on-lift-off' service for bulk freight from Southampton.

Figure 15: Passenger ferry routes to and from Jersey

	Sailings per week June, 2013	Passengers number 2010	Cars number 2010
UK	**19**	**190,000**	**59,000**
Poole	*13*		
Portsmouth	*6*		
France	**34**	**460,000**	**59,000**
St Malo	*20*		
Granville	*8*		
Carteret	*6*		
Other CI	**17**	**104,000**	**9,500**
Guernsey	*14*		
Sark	*3*		
Other		**1,500**	
Total	**70**	**755,500**	**127,500**



	Freight (tons) 2010
RoRo	277,000
LoLo	118,000
Fuel	104,000
Total	**499,000**

Source: Jersey Harbours' annual report 2010 and individual ferry operator websites

Patterns of telecommunications usage provide further clues to the island's cultural, social and economic links.

The dominance of the relationship with the United Kingdom is apparent. While 72 million minutes a year of outbound telephone calls are made from Jersey to its neighbour to the north of the English Channel, there are only 25 million minutes of talk with the other Channel Islands or the Isle of Man, and just three million minutes of conversation with France. Great Britain and Northern Ireland account for 62 per cent of the island's outbound voice traffic. Meanwhile, 50 per cent of Jersey mobile telephone users' 'roaming' minutes abroad are made from the United Kingdom, and 61 per cent of mobile minutes made by visitors while in Jersey are on calls to there. (See Figure 16.)

It is not easy to obtain data on the patterns of general data traffic to and from Jersey. However, information has been provided by two telecommunications companies on the 'private circuits' they operate linking specific businesses in Jersey to locations abroad with guaranteed, resilient and dedicated bandwidth on trunk fibre optic networks. Eighty five per cent of these high volume data links are to locations in the United Kingdom. Indeed, half are destined for the Docklands area of London, and a further quarter for somewhere else in London.[6] Quite literally, London and Jersey are hard wired together.

6 Information kindly provided to Capital Economics by Jersey Telecom and Cable & Wireless.

Figure 16: Different measures of international telephone usage

	Jersey's telecommunication connections		
	Outbound voice minutes, millions	Outbound roaming voice minutes, millions	Inbound roaming voice minutes, millions
United Kingdom	72.3	8.9	7.0
Other Crown Dependencies	24.8	3.5	3.0
Ireland	4.3	0.9	0.2
France	3.4	1.6	0.9
European financial centres	2.2	0.8	0.2
Rest of the EU	4.3	1.2	0.2
Russia and other Europe	1.0	0.2	0.0
Asia	1.1	0.2	0.0
Australasia	0.8	0.1	0.0
Africa	0.8	0.1	0.0
America	1.5	0.2	0.0
Other offshore financial centres	0.8	0.1	0.0
Total	**117.4**	**17.8**	**11.6**

Source: Jersey Telecom and Cable and Wireless

3.2 Balance of trade

Economic linkages between countries are typically explained and summarised in 'balance of trade accounts'. There are currently no such official accounts for Jersey, so we have constructed indicative accounts based on a variety of sources.[7]

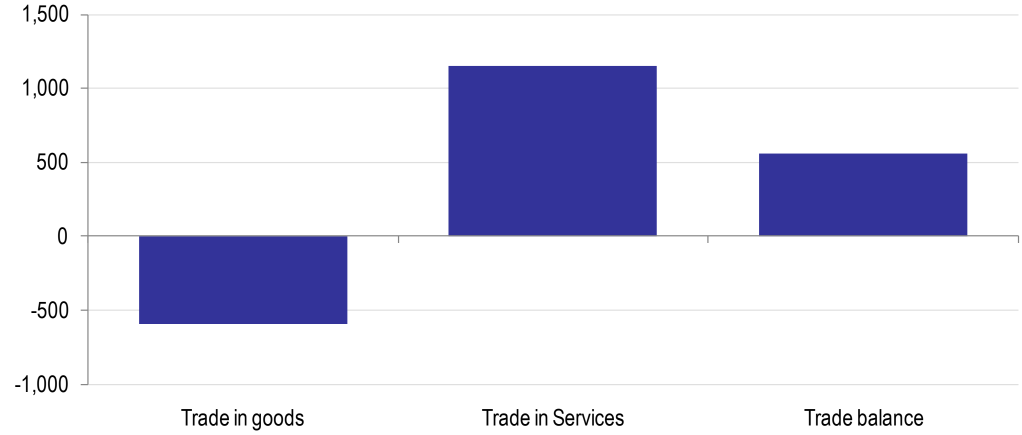
We estimate that Jersey ran an overall trade surplus in the order of £0.6 billion in 2010. We have calculated this by comparing official estimates of the island's gross value added with estimates of domestic consumption, business investment and government expenditure. The difference between these is the trade balance. (See Figure 17.)

Jersey's 2010 trade surplus is equivalent to sixteen per cent of national output, and compares to the United Kingdom's trade deficit for that year of two per cent. Of course, high export ratios are not uncommon among small jurisdictions but, against such peers, Jersey often appears to have less dependency on trade. By comparison, Ireland's trade surplus in 2010 was nineteen per cent of gross domestic product, Luxembourg's 24 per cent and Singapore 35 per cent.[8]

7 See Note 7.1 for further detail on methodology, but please note that the purpose of the exercise has been to provide first order estimates of the general scale and shape of trade between Jersey, the United Kingdom and elsewhere. Results should be treated with the appropriate caution.

8 Source: Capital Economics' analysis of Datastream.

Figure 17: Indicative estimate of Jersey's balance of trade, 2010 (£ million)



Source: Capital Economics' indicative estimates calculated using States of Jersey and Office for National Statistics statistics

Jersey's export performance compares favourably to the United Kingdom's.

The total value of exported goods and services is equivalent to 60 per cent of the island's total gross value added; for the United Kingdom, the comparable statistic is around 35 per cent. Meanwhile, Jersey has greater penetration of further afield higher growth markets, with 69 per cent of non-sterling exports destined for beyond the European Union. The United Kingdom's exports, on the other hand, are focussed closer to home, with roughly half of exports going to other countries within the European Union. (See Figure 18.)

Figure 18: Export profiles of Jersey and the United Kingdom, 2010

2010	UK	Jersey
Exports to outside sterling zone		
Total exports as share of GVA	34%	57%
Share of exports to outside sterling zone destined for the EU	47%	31%
Share of exports to outside sterling zone destined for elsewhere	53%	69%

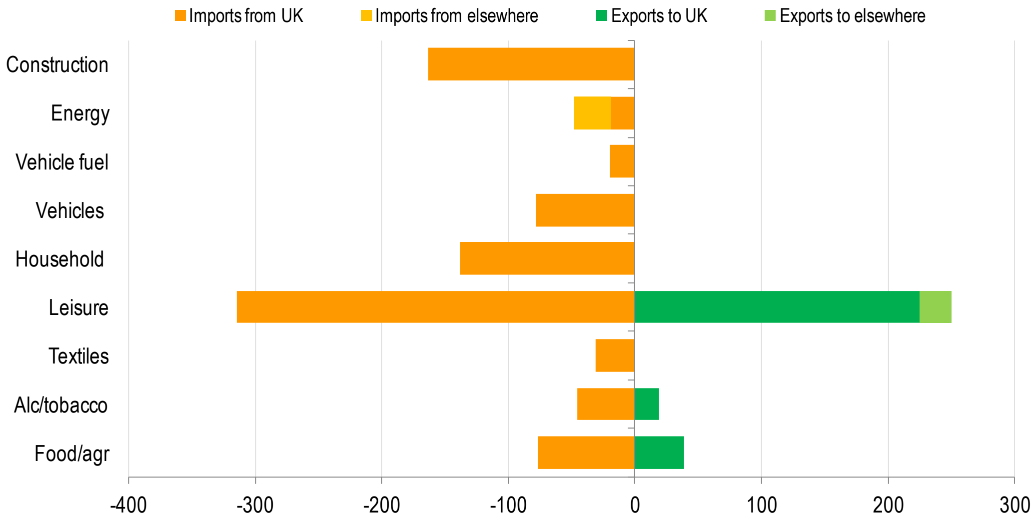
Sources: Capital Economics' analysis of Office for National Statistics trade statistics and Capital Economics' survey 2012/13

3.3 Trade in goods

Although running a trade surplus overall, we estimate that, for 2010, Jersey was a net importer of goods to the value of over £550 million.

This is unsurprising as there is little by way of manufacturing on the island and, although there is a notable agricultural industry and fishery, much of the food and drink that is consumed has to be imported. (See Figure 19.)

Figure 19: Indicative estimates of the trade in goods at port gate prices excluding duties and taxes, 2010 (£ million)



Source: Capital Economics' indicative estimates calculated using States of Jersey and Office for National Statistics data

Jersey has to import almost all goods consumed on the island – however there is no comprehensive recording of such flows.

It is possible to get a fix on the volume of imports of some goods from customs service information, especially records of duties paid – while surveys of households' and visitors' expenditure conducted by the States of Jersey provide estimates of local consumption of different products. Around 6,500 new cars and 50 million litres of vehicle fuel were brought onto the island in 2010, while import duty was paid that year on alcohol with a retail value of £70 million and cigarettes and tobacco products worth £20 million in the shops.[9] Meanwhile, around £280 million was spent in shops or online on household goods, clothing and footwear, which could easily account for imports in the region of £170 million.[10]

Given the lack of freight capacity to anywhere other than the United Kingdom, almost all of these imports will have been shipped in from the south coast of England or by air from British airports.

There are also some goods that are exported from the island.

An estimated £40 million of agricultural products were shipped out during 2010; these were predominantly but not exclusively potatoes. In addition, on-island purchases by foreign visitors of, say, alcoholic drinks count as exports,

9 Estimate based on volume and duty collected data kindly provided to Capital Economics by Jersey Customs and Immigration as well as Capital Economics' indicative estimates calculated using States of Jersey and Office for National Statistics data.

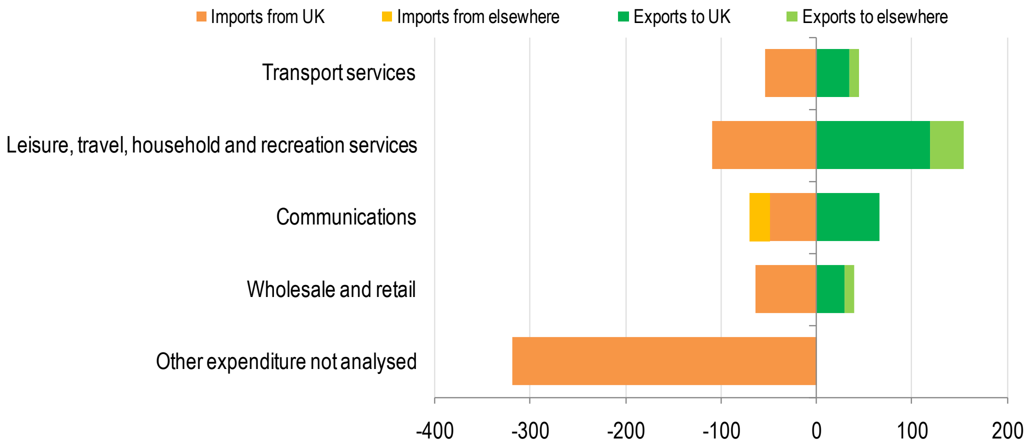
10 Capital Economics' indicative estimates calculated using States of Jersey and Office for National Statistics data. Note: import prices are wholesale prices at 'port gate' excluding any duties or sales taxes.

even if they are then consumed locally. Meanwhile, in the same year, a number of online retailers operated distribution facilities in Jersey to service the United Kingdom and, to a much lesser extent, other European markets. The bailiwick's international status then allowed these operations to benefit from the European Union's 'low value consignment relief', which permits member states to waive value added tax and duties on packages worth under €22 imported via the postal system from outside the bloc. We estimate that low value consignment relief exports could have been worth in the order of £250 million in 2010 (although there would have been a similar value on the import side of the balance sheet).[11] The United Kingdom government subsequently withdrew the waiver from imports from the Channel Islands – so these trade flows have now been curtailed.

3.4 Trade in services

The picture for the trade in services is somewhat different, where we estimate that Jersey ran a trade surplus with the rest of the world in the order of a £900 million in 2010. (See Figure 20 and Figure 21.)

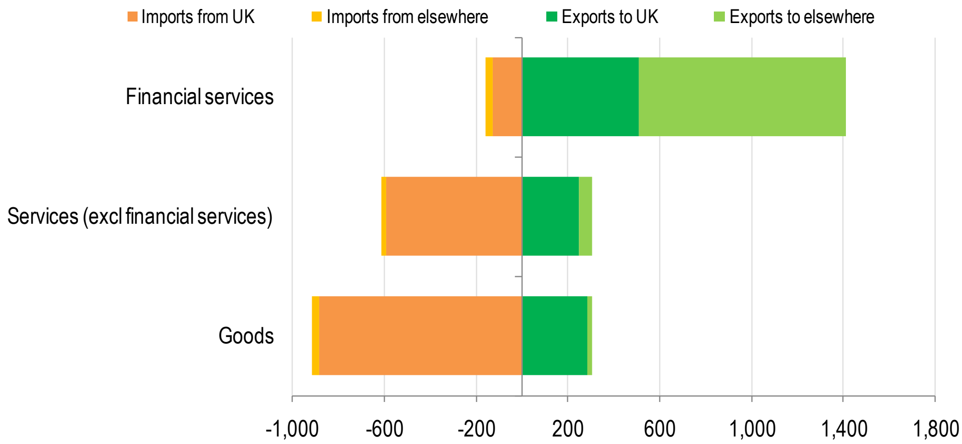
Figure 20: Indicative estimates of trade in services (excluding financial services) at export prices excluding duties and taxes, 2010 (£ million)



Source: Capital Economics' indicative estimates calculated using States of Jersey and Office for National Statistics data

11 Estimate based on mail volumes data kindly provided to Capital Economics by Jersey Post.

Figure 21: Indicative estimates of trade in services at export prices and goods at port gate prices excluding duties and taxes, 2010 (£ million)



Source: Capital Economics' indicative estimates calculated using States of Jersey and Office for National Statistics data

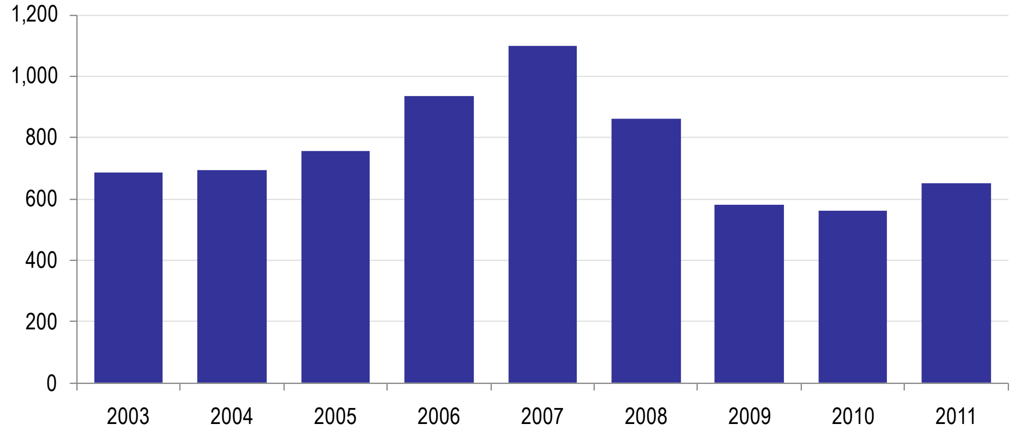
There are two key exports: financial services (broadly defined); and tourism.

With around 12,000 people employed on the island in banking, wealth management and related businesses in 2010, the sector generated an estimated £1.4 billion of gross value added.[12] Local demand, by Jersey residents and local businesses, for banking and finance probably amounted to something in the region of only £0.2 billion[13] – implying net exports worth £1.2 billion. This surplus in financial services underpins and dominates the island's overall trade balance – and, accordingly, the trade position likely varies with the fortunes of that key sector from one year to the next. (See Figure 22.)

12 Sources: States of Jersey's *Financial Institutions Survey 2011* and *GVA Report 2011*.

13 Source: Capital Economics' estimate calculated using States of Jersey's *Household Spending Survey 2009/10*.

Figure 22: Indicative estimates of the trend in balance of trade based on a stylised model, 2003-2011 (£ million)



Source: Capital Economics' indicative estimates calculated with States of Jersey and Office for National Statistics data

Turning to tourism, Jersey attracted 685,000 foreign visitors in 2010, who spent an estimated £230 million on the island – which, among others, boosted hotel and accommodation revenues by £110 million and pubs' and restaurants' takings by £50 million.[14] Conversely, Jersey residents travel abroad for work and pleasure, with their spending offsetting the local earnings from visitors. There are limited data on outbound travel and spending patterns, so it is not possible to draw any firm conclusions on the scale of tourism imports but it is likely that overall Jersey is a small net exporter of tourism. Two or more decades ago, tourism would likely have been a substantial net export for the island but budget airlines, more stable currencies and a growing British taste for more distant and exotic destinations has limited the export potential here.

There is two-way trade in other services too but, typically, Jersey is a net importer of services other than finance and tourism. For transport, for example, air services operating to the island are disproportionately crewed, fuelled, maintained and operated by firms off-island. Almost all electricity is supplied by a submarine interconnector from France. Meanwhile, there will likely be a trade deficit on healthcare and education, with Jersey residents making use of the United Kingdom's private healthcare facilities and their children attending British universities and colleges (often at the expense of States of Jersey coffers).

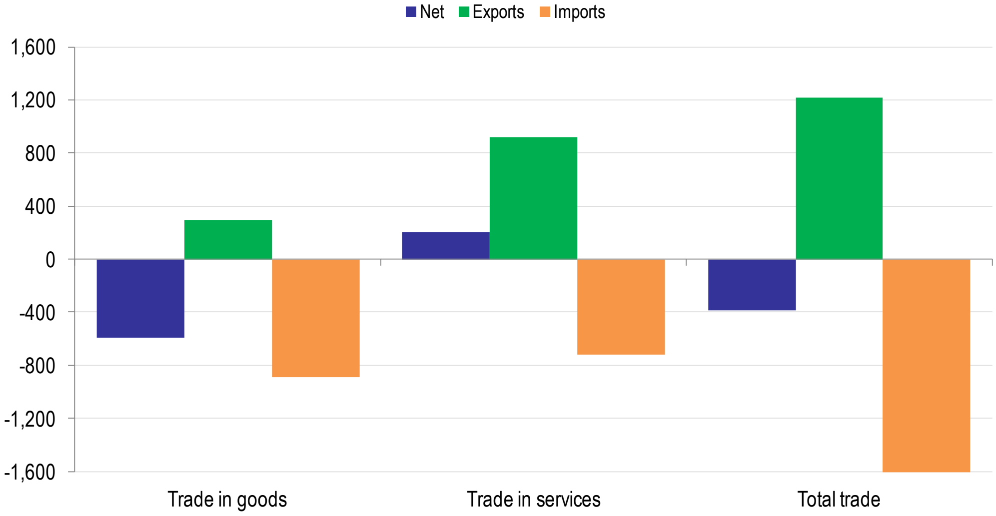
3.5 Trade with the United Kingdom

Although Jersey runs a trade surplus with the rest of the world overall, its balance with the United Kingdom alone is quite different.

14 Sources: Capital Economics' analysis of Jersey Tourism annual report 2010.

We estimate that the island imported in the region of £1.6 billion of goods and services from Great Britain and Northern Ireland in 2010, which was £0.4 billion more than it exported to there. (See Figure 23.)

Figure 23: Indicative estimate of Jersey's balance of trade with the United Kingdom, 2010 (£ million)



Source: Capital Economics' indicative estimates calculated using States of Jersey and Office for National Statistics data

This is explained by the variety of foreign markets served by the bailiwick's finance firms compared to the dominance of southern England among its sources of imports. An estimated 36 per cent of exports by such businesses are destined for the United Kingdom, while the remaining £900 million are exports to outside the sterling zone.[15]

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15 This is based on results from our survey of financial and business services firms in Jersey. (See Section 4.)

Figure 24: Indicative estimates of the impact of Jersey's trade on the United Kingdom's employment, 2010

	United Kingdom jobs supported	United Kingdom GVA generated
	Number	£ million
Estimate of British jobs supported by Jersey imports from the United Kingdom		
Greater South East	11,700	520
South West and the Midlands	6,900	300
Northern England	6,600	300
Wales, Scotland and Northern Ireland	4,300	210
United Kingdom	**29,600**	**1,300**
Estimate of British jobs supported by Jersey imports from the United Kingdom		
Less potential jobs foregone through United Kingdom imports from Jersey		
Greater South East	3,600	110
South West and the Midlands	2,900	110
Northern England	2,700	110
Wales, Scotland and Northern Ireland	1,800	80
United Kingdom	**11,200**	**400**
Estimate of British jobs supported by Jersey imports from the United Kingdom		
Less potential jobs foregone through United Kingdom imports from Jersey (excluding financial services)		
Greater South East	7,400	340
South West and the Midlands	4,500	200
Northern England	4,300	210
Wales, Scotland and Northern Ireland	2,900	150
United Kingdom	**19,300**	**900**

Source: Capital Economics' analysis of States of Jersey and Office for National Statistics statistics

To give some sense of scale, Jersey's imports of £1.6 billion could be sustaining around 30,000 jobs across England, Wales, Scotland and Northern Ireland, which is equivalent to the employment in a local authority the scale of Brentwood.[16] These calculations take account of the likelihood that many of the goods shipped from southern England are actually themselves imports to Britain from elsewhere in the world. (See Figure 24.)

On the reverse side, Jersey's exports may be taking away jobs that would have otherwise been sustained in the United Kingdom. Estimated exports of £1.2 billion could be costing 18,000 jobs in Britain – if one assumes that all the jobs would have otherwise been based there. But this is unlikely as much of what Jersey exports, especially in the financial services sector, cannot be produced onshore in Britain. Assuming that only non-financial services exports can replace British jobs, the number falls to 10,000.

Overall, we believe that Jersey runs a trade deficit with the United Kingdom, despite its positive trade balance with the rest of the world, and these net imports could be supporting in the region of 19,000 British jobs. In essence, the bailiwick brings value into the sterling area through trade, and shares the spoils with its larger currency zone partner.

16 Sources: Office for National Statistics' *Business Register and Employment Survey* and Office for National Statistics' input-output tables 2010. Indicative estimates calculated using official British data known as the 'input-output tables', which quantify how different sectors of the economy, as well as imports and exports, fit together.

4 FINANCIAL LINKAGES

In this section, we examine the financial sector in Jersey and its links with the rest of the world. Our key findings are:

- **Jersey's banks attract almost £150 billion of funding from markets outside the sterling zone, while they provide 1½ per cent of the funding of the whole United Kingdom banking sector**
- **Almost £400 billion of private assets are held in Jersey trusts, of which 94 per cent have been settled there by individuals resident outside the British Isles or by non-doms**
- **Two-fifths of all assets administered or managed across the whole of the island's financial and wealth management industry come from markets beyond the European Union**
- **Jersey is a conduit for almost £½ trillion of foreign investment into the United Kingdom, which is five per cent of the total stock of foreign owned assets in the country and could be supporting over 100,000 British jobs**

First, we reference the survey carried out to obtain relevant data for the subsequent analysis. Second, we examine the banking sub-sector, the nature of business conducted in Jersey and the location of the counterparties and underlying economic interests in banking transactions. Third, we do likewise for the island's trust and private wealth activities. Fourth, we similarly examine corporate and institutional asset vehicles. Fifth, we consider the funds administration and management sub-sector. Sixth, we review the activities of accounting, legal and other professional services firms in Jersey. Seventh, we produce a consolidated picture of the source, destination and beneficiaries of funds administered or managed in Jersey.

4.1 The survey

In order to better understand and more fully quantify the underlying financial relationships between Jersey and the United Kingdom, we conducted a survey of financial and professional services businesses on the island starting 5 November 2012 and ending 2 March 2013.

The survey sample was fully representative of the range of activities and types of firm. The sample of respondents covered businesses employing over

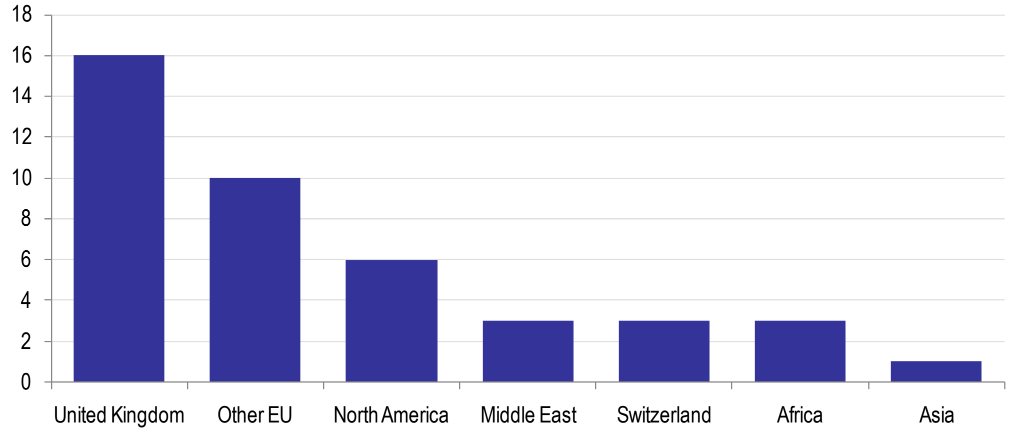
8,000 full time equivalents, which is two-thirds of total employment by the financial and related services sector in Jersey.[17]

4.2 Banking

Jersey is a substantial banking centre, with 42 deposit-taking licenses currently issued by the regulatory authority, the Jersey Financial Services Commission, and an estimated 4,850 people working in the sector. The international scale of the sector is demonstrated by statistics produced by the Bank for International Settlements, showing Jersey's external liabilities are comparable to those of countries like Austria, Norway or South Korea. (See Figure 10.)

Although the United Kingdom's retail clearing banks had a prior presence on the island, the origins of an international banking centre date back to the winter of 1961/2. The merchant bank Hill Samuel and Mayfair-headquartered private bank Kleinwort Benson established subsidiaries there then – in preparation for the repeal in 1962 of restrictive eighteenth century anti-usury laws. Today, Jersey's banks comprise everything from the branches and subsidiaries of the major British clearers through retail and private banks from a variety of countries worldwide to the treasury functions of major international finance houses. (See Figure 25.)

Figure 25: Jersey banking licenses by location of the ultimate parent of the holder, end 2011



Source: Jersey Financial Services Commission data published by Jersey Finance Limited

Although a wide range of banking activities are undertaken, the core of what most banks on the island do is one or more of:

17 See Note 7.2 for further detail on survey distribution and Note 7.3 for sample coverage and representativeness.

- **Retail personal banking** for the internationally mobile and expatriate 'mass affluent'

- **Private banking and wealth management** for internationally mobile and expatriate high net wealth individuals

- **Corporate banking** primarily serving the needs of the island's trust, funds and corporate services industries

Across all three of these activities, the emphasis is generally on deposit-taking rather than lending (although there are some notable exceptions).

4.2.1 Deposit taking and other bank liabilities

According to regulatory submissions, £163 billion of deposits were held by Jersey regulated banks at the end of 2011, of which £112 billion were 'customer deposits' with the rest being 'bank deposits'.[18]

The regulatory statistics suggest that almost half of deposits are from the sterling zone; 44 per cent were reported to be from a hotchpotch group of 'Jersey resident depositors', 'Jersey financial intermediaries', 'United Kingdom, Guernsey and Isle of Man depositors' and 'unallocated Jersey, UK etc.'.

We have used our survey and interviews to try and disentangle this, and determine the country of residence of the underlying economic interest in the deposits in Jersey banks. Importantly, we have sought to look through the deposits made by financial intermediaries, such as trust companies and law firms, to identify the true origins of all deposits. This has been done by combining data produced by the banks for our survey with those from the financial intermediaries themselves.[19]

We find that the sources of deposits in Jersey are spread across the globe. (See Figure 26.)

We have estimated the scale of Jersey's domestic banking market based on the size and affluence of the island's population and economy.[20] Less than one twentieth of banks' customer deposits are likely to have derived from the local population.

A further 34 per cent of customer deposits (including fiduciary deposits) have ultimate beneficial owners in the United Kingdom. Out of these, around £18 billion had been deposited by corporate and charitable organisations in

18 Source: Jersey Financial Services Commission, *Banking Statistics*.
19 See Note 7.4 for survey sample and treatment relating to banking respondents.
20 See Note 7.5 for methodology.

Britain, and a further £11 billion from individuals resident but not domiciled for tax purposes there i.e. the non-doms. The remaining £9 billion are deposits from private individuals who are not 'non-dom'.[21]

This leaves £70 billion that has come from elsewhere around the world. Almost £10 billion of customer deposits were sourced from beneficial owners in the Middle East in 2011; £9 billion from Africa; £5 billion each from Russia and North America; £4 billion from South America; £3 billion from China; and £2 billion from India – plus £13 billion from Switzerland.

The European Union as a whole, on the other hand, is the source of only £10 billion, which is less than ten per cent of all customer deposits.

Figure 26: Capital Economics' indicative estimate of the consolidated liabilities of the Jersey banks allocated to the country of residence of the underlying economic interest, 2011 (£ millions)

£ million, 2011	Liabilities				
	Customer deposits	As a share	Interbank deposits and other liabilities	Total liabilities	As a share
Jersey	**4,092**	**4%**	**5,824**	**9,916**	**5%**
United Kingdom	**38,430**	**34%**	**9,767**	**48,197**	**24%**
Private non-dom	11,298	10%	0	11,298	6%
Private not non-dom	9,368	8%	0	9,368	5%
Corporate	17,763	16%	9,767	27,530	13%
EU	**10,440**	**9%**	**17,185**	**27,625**	**14%**
Non-EU world	**59,236**	**53%**	**58,994**	**118,230**	**58%**
of which					
Guernsey	354	0%	14,947	15,301	8%
Switzerland	12,926	12%	1,124	14,051	7%
Russia	5,498	5%	385	5,883	3%
North America	5,401	5%	31,217	36,618	18%
South America	4,088	4%	5,211	9,299	5%
Middle East	9,521	8%	542	10,063	5%
Africa	9,424	8%	93	9,518	5%
China	2,936	3%	615	3,551	2%
India	2,513	2%	615	3,127	2%
Other Asia Pacific	6,575	6%	2,454	9,029	4%
Total	**112,198**	**100%**	**91,770**	**203,968**	**100%**

Sources: Capital Economics' survey 2012/3 and Jersey Financial Services Commission data

Customer deposits are not the only source of funding for banks. They accounted for around 55 per cent of the funding of Jersey's banking balance sheet in 2011.[22] The remaining £92 billion of other liabilities included around £30 billion of interbank deposits and £60 billion of issued debt, equity and other instruments. (See Figure 26.)

21 See Note 7.6 for an analysis of the sources of deposits reported as from United Kingdom private individuals who are not non-doms.

22 This includes our estimate of fiduciary deposits, and is not comparable directly with Jersey Financial Services Commission statistics.

Looking at all of the £204 billion of bank liabilities combined, less than a quarter derive from the United Kingdom – while more than three in every five pounds of Jersey bank funding arose in the world beyond the European Union.

The bulk of this bank funding would not have come to the sterling area if it wasn't for Jersey and the other Crown Dependencies' unique status.[23] Respondents to the survey estimate that, if the Crown Dependencies didn't exist, 63 per cent of their current business would be conducted outside the United Kingdom – with the majority of the business going to other non-sterling offshore financial centres.

4.2.2 Up-streaming, and other bank assets

The majority of funding collected by banks in Jersey is 'up-streamed' to their parents' operations which, more often than not, are in London. Over two-thirds of funding is utilised this way by parent banks to support their balance sheets. (See Figure 27.)

Figure 27: Capital Economics' indicative estimate of the consolidated assets of the Jersey banks allocated to the country of residence of the underlying economic interest, 2011 (£ millions)

£ million, 2011	Assets						
	Up-streaming	As a share	Inter-bank loans	Customer loans	Other assets	Total	As a share
Jersey	**587**	**0%**	**1,091**	**10,985**	**15,035**	**27,699**	**14%**
United Kingdom	**117,545**	**84%**	**1,327**	**8,131**	**8,829**	**135,833**	**67%**
Private non-dom	-	-	-	2,090	0	2,090	1%
Private not non-dom	-	-	-	2,376	2	2,378	1%
Corporate	117,545	84%	1,327	3,664	8,826	131,364	64%
EU	**2,395**	**2%**	**46**	**2,661**	**0**	**5,101**	**3%**
Non-EU world	**18,753**	**13%**	**1,317**	**4,367**	**10,898**	**35,335**	**17%**
of which							
Guernsey	5,595	4%	561	796	622	7,574	4%
Switzerland	8,061	6%	517	679	0	9,257	5%
Russia	0	0%	0	15	0	15	0%
North America	0	0%	207	695	14	917	0%
South America	0	0%	0	136	0	136	0%
Middle East	102	0%	0	1,689	0	1,791	1%
Africa	0	0%	0	289	0	289	0%
China	0	0%	0	46	0	46	0%
India	0	0%	0	23	0	23	0%
Other Asia Pacific	4,996	4%	32	894	616	6,536	3%
Total	**139,281**	**100%**	**3,781**	**26,144**	**34,762**	**203,968**	**100%**

Sources: Capital Economics' survey 2012/3 and Jersey Financial Services Commission data. Note: 'Up-streaming' is 'Funding of group companies' as per Jersey Financial Services Commission reporting.

We estimate that British banks had £118 billion of their balance sheets funded through these intra-group transfers from Jersey. This is not a trivial amount; it amounts to 1½ per cent of the total liabilities of monetary financial institutions

23 See Note 7.7 for more detail on estimates of the significance of Jersey and the Crown Dependencies' status for the levels of business conducted on the island.

in the United Kingdom and could be supporting around 14,000 jobs in Britain's banking sector.[24] (See Figure 28.)

To the extent that this is funding the balance sheets of the part-nationalised banks, there is also a direct benefit to British taxpayers.

Figure 28: Estimated up-streaming by Jersey banks into the United Kingdom with comparator statistics, 2011 (£ millions)

£ million, 2011	Up-streaming into the UK		
	Total	by non-UK	by UK non-doms
Total Value	117,545	89,770	6,511
as share of:			
Total UK liabilities	1.4%	1.1%	0.1%
Total non-resident liabilities	3.7%	2.8%	0.2%
Total sterling deposits	3.8%	2.9%	0.2%
Total sterling time deposits	7.8%	5.9%	0.4%
Total UK Quantitative easing	31.3%	23.9%	1.7%
Total UK banks' customer funding gap	42.0%	32.1%	2.3%

Sources: Capital Economics' survey 2012/3 and Bank of England statistics

In addition to up-streaming, Jersey banks' assets include £26 billion of outstanding loans to customers, £4 billion of outstanding inter-bank loans and £35 billion of other instruments. Even with all these are added together, the geographical distribution of total assets remains dominated by the United Kingdom; two-thirds of the island's bank assets are there. (See Figure 27.)

4.2.3 Auxiliary banking activities

Jersey's banks undertake a range of other activities for their customers – most of which are auxiliary to the island's wealth management and fiduciary industries.

Our survey captured data on three such lines of business: 'broking and trading'; 'custodian services'; and 'discretionary management' – from a sample of eight organisations that reported on them. Across the sample, these activities generated £48 million of revenues in 2011. (See Figure 29.)

24 See Note 7.8 for calculation of the estimate for the number of jobs supported.

Figure 29: Revenues from auxiliary banking activities reported by respondents to survey by location of customer, 2011 (£ millions)

Revenue £ million, 2011	Broking and trading	Custodian services	Discretionary management	Broking and trading	Custodian services	Discretionary management
Jersey	**8.8**	**4.4**	**9.1**	**44%**	**33%**	**61%**
United Kingdom	**3.5**	**3.8**	**1.8**	**18%**	**29%**	**12%**
EU	**1.0**	**2.4**	**1.6**	**5%**	**18%**	**11%**
Non-EU world	**6.7**	**2.6**	**2.5**	**33%**	**20%**	**17%**
Switzerland	0.1	0.0	0.0	0%	0%	0%
Russia	0.2	0.2	0.2	1%	1%	1%
North America	0.5	0.7	0.2	3%	5%	2%
South America	3.0	2.2	1.0	15%	17%	7%
Middle East	0.0	0.0	0.0	0%	0%	0%
Africa	0.1	0.1	0.0	1%	1%	0%
China	0.4	0.1	0.1	2%	1%	0%
India	0.6	0.4	0.1	3%	3%	1%
Total	**20.0**	**13.2**	**14.9**	**100%**	**100%**	**100%**

Sources: Capital Economics' survey 2012/3.

Much of this business derives locally: over two-fifths for broking and trading; a third for custodian services; and three-fifths for discretionary management. But little of this Jersey-based demand is likely to be truly domestic; instead, it will be the banks servicing the needs of trust, funds, wealth management and corporate services firms in Jersey. The clients of these firms are global (as we show elsewhere in this report).

The United Kingdom accounts for £9 million of the sample's revenues, which is nineteen per cent of the total. Other European Union countries account for a further ten per cent. Like deposit-taking, Jersey's auxiliary banking services are a global business.

4.3 Trusts and private wealth

Trusts are legal instruments under which one person can transfer the legal ownership of all or part of their assets to a second, while ensuring that the assets remain for their benefit or the benefit of some other third party.[25] With origins that date back to the English medieval crusades, the formation of trusts is almost exclusively associated with common law jurisdictions, which are typically Commonwealth or other countries with a strong historical connection to Britain.

25 The parties are typically referred to as 'settlor', 'trustee' and 'beneficiary' respectively.

Trusts can be established and enforced under Jersey law, and the courts there have jurisdiction over such agreements that are made on the island regardless of whether the parties or the assets are located abroad. As such, there is appeal to asset-owners residing in countries where the law is based on a civil code and the facilities of a trust may not be accessible.

Jersey has been administering trusts for international clients at least since the 1920s, and it has become a significant industry in its own right. Just as in the United Kingdom, there is no registration of individual trusts with authorities – so there is no locus for the collation of statistics on how many of them are in existence. However, unlike Britain, there is regulation of certain types of trust businesses on the island; the Jersey Financial Services Commission reports that 885 entities currently regulated for such purposes.[26]

Official statistics suggest that 3,800 people were employed in the sub-sector in 2011, earning a total of £230 million in wages and salaries, conducting business with £550 million of turnover and creating £110 million of profit for the island.[27]

Although once focussed on simple trusts for British families, the emphasis of the island's industry today has almost completely shifted to high value and more complex structures for international families, and the establishment of 'virtual' family offices for ultra high net worth individuals and estates. Trusts are deployed in a variety of circumstances, but the common uses of a Jersey vehicle include:

- **Succession and estate planning.** An offshore Jersey trust can be used to by-pass certain cumbersome probate processes and harsh succession laws in other countries. This is particularly relevant for individuals residing in countries where the law does not respect the will of the deceased or where there are forced heirship rules

- **Preservation of wealth.** Trusts may be used to preserve the continuity of ownership of particular assets, such as a business, within a family

- **Asset protection.** A Jersey trust can be used to secure assets at risk of expropriation or confiscation by an unstable or hostile regime. This is particularly relevant for individuals with international assets, but who wish to continue residing in a volatile home country

26 Source: Jersey Financial Services Commission.

27 Source: States of Jersey's *Financial Institutions Survey 2011*. We have, however, made some adjustments to the official data to account for fund administration activities being included within this sub-sector in the official statistics. For the purposes of our survey we have attempted to reallocate these activities to the fund administration and management sub-sector. The adjusted figures suggest employment of 3,110, total employment costs of £170 million and £430 million of revenues. (See Figure 46.)

- **Confidentiality**. A Jersey trust can be used to preserve the confidentiality of the ultimate beneficial owners of assets. This can be valuable on occasions such as when there is a risk of criminality or extortion resulting from release of such information, or when family circumstances or matrimonial proceedings dictate. Clearly, confidentiality is also valuable when trying to hide assets not declared for tax – but this would be ill-advised in Jersey given the jurisdiction's tough anti-money laundering legislation, which originates from the *Proceeds of Crime (Jersey) Law 1999* and treats any funds obtained through the evasion of tax in another jurisdiction as a proceed of crime. Moreover, through the island's trust statutes and its regulation of trust and company service providers, all trustees must know who the settlor and the beneficiaries of a trust are. Provisions exist to enable the authorities to obtain such information and exchange it with law enforcement authorities in other countries

- **Operating within exchange controls.** A Jersey trust may be helpful for owners of international assets who reside in a country with exchange control regulations, but do not want their global wealth embroiled in them

In addition, trusts may also be used to **minimise or defer taxes** on the assets and on the income and gains arising from them where local tax codes permit. Jersey trusts are tax neutral for international clients and there is no capital gains tax in Jersey or any stamp duty upon the creation of a trust and the execution of any trust instrument.[28] In practice, though, the opportunities for United Kingdom resident taxpayers to avoid British taxes through offshore trusts nowadays are scant. Tough legislation on both sides of the Channel and active enforcement means that there are few legitimate ways to use offshore trusts as a shelter from British tax, while Jersey's criminal code makes it a dangerous location to try to evade tax. Nevertheless, the use of trusts for tax mitigation remains.

Jersey trusts are often utilised by United Kingdom non-doms not wishing to remit their global income and gains into Britain – while an offshore trust is a practical way to manage the family wealth for settlors who move from one country to another, changing their country of tax residence and, sometimes, their nationality.

28 Although trustees are strictly liable to Jersey income tax in respect of all income arising to them in that capacity, by long standing published concessions from the Comptroller of Income Tax non-Jersey source income and Jersey bank deposit interest are exempt where the settlor or originator of the trust and any beneficiaries of the trust are not residents of the island.

There are no data collected officially or by the industry on the scale of assets under the stewardship of Jersey trustees – nor are there comprehensive statistics on the settlors or beneficiaries. Our survey helps plug these gaps.[29]

Figure 30: Indicative estimate of the value of assets held in Jersey trusts settled by private individuals by residence of ultimate settlor and beneficiary, and location of assets*, 2011 (£ millions)

Net Asset Value, £ million, 2011	Settlors		Beneficiaries		Assets*	
		As share		As share		As share
Jersey	**8,163**	**2%**	**4,056**	**1%**	**12,920**	**3%**
United Kingdom	**174,016**	**44%**	**177,618**	**45%**	**192,859**	**49%**
of which Res Non-Dom	156,378	40%	134,792	34%	-	-
EU	**40,693**	**10%**	**47,584**	**12%**	**73,760**	**19%**
Non-EU world	**168,321**	**43%**	**161,936**	**41%**	**111,655**	**29%**
of which						
Switzerland	7,895	2%	8,094	2%	6,919	2%
Russia	15,478	4%	8,171	2%	20,451	5%
North America	8,580	2%	6,525	2%	4,034	1%
South America	1,691	0%	1,536	0%	10,886	3%
Middle East	14,728	4%	38,044	10%	23,137	6%
Africa	30,971	8%	18,853	5%	19,982	5%
China	1,016	0%	1,510	0%	-	0%
India	6,381	2%	4,519	1%	8,727	2%
Other Asia Pacific	54,650	14%	48,049	12%	11,533	3%
Total	**391,193**	**100%**	**391,193**	**100%**	**391,193**	**100%**

Sources: Capital Economics' survey 2012/3 scaled up by turnover from the sample to reflect the whole Jersey industry
* Note: Data on location of assets includes assets in trusts and special purpose vehicles settled by corporate or institutional clients.

Considering only those with private individuals and families as ultimate settlors, we estimate that assets valued in the region of £0.4 trillion are held in such vehicles. (See Figure 30.)

Over two-fifths of assets held relate to settlors resident in the United Kingdom – but, of these, 90 per cent are not domiciled there for tax purposes; an estimated £160 billion of non-dom private assets are held in Jersey trusts. The remaining assets have settlors from across the globe: eight per cent from other European Union nations; eight per cent from Africa; four per cent each from Russia and the Middle East; and between £5 and 10 billion each from North America, Switzerland and India.

Analysing the survey by ultimate beneficiary, the results are similar. The location of the beneficiaries of private trusts is closely aligned to the location of the settlor. The only notable difference is that the share of resident and domiciled beneficiaries from the United Kingdom is slightly higher than that for the settlors.

The geographic distribution of the assets held shows a disproportionate benefit to the United Kingdom. Although only a small share of the assets

29 See Note 7.9 for further details of survey sample and treatment.

originates from those that are resident and domiciled in the United Kingdom, one half of the assets are located there.

4.4 Corporate and institutional asset vehicles

Trusts are also used for corporate and institutional purposes, as are a range of other asset-holding special purpose vehicles and companies that can be established in Jersey. Such vehicles can be established efficiently on the island, and their costs are readily controllable given the bailiwick's low and predictable tax regime.

There are a number of differences between the legislation either side of the English Channel which makes Jersey especially attractive for corporate and institutional settlors. For example, unlike the United Kingdom, Jersey law permits the establishment of 'non-charitable purpose trusts'. These have a variety of uses, normally in connection with commercial transactions where there is a need for an independent third party to hold funds or assets.

Similarly, Jersey law does not limit the duration of trusts, whereas there are restrictions under United Kingdom law. This makes the bailiwick a more practicable jurisdiction within which to manage long-living assets, for example. Deloitte, in a study for a HM Treasury review, report:

> 'We are aware of government contracts which have included within their terms the need to ring fence assets within a trust of 100 years' duration (to protect them from being diverted into other projects). A UK trust cannot exceed a stated period longer than 80 years, and English law does not fully recognise trusts which have been established for a defined general purpose, where there is no clearly identifiable class of beneficiaries who can enforce the trust. Accordingly, companies bidding for such contracts are obliged to set up non-UK trusts (typically in Jersey) but which are UK tax resident.'[30]

The uses of trusts and other special purpose vehicles are wide-ranging but include: sheltering assets from a company's other risks; collective investment of capital; issuing and repackaging of securities such as asset backed securities, mortgage backed securities, collateralised bond obligations, collateralised loan obligations and collateralised debt obligations; inter-creditor agreements; pension, employee share option and executive incentive schemes; collection and securing of sinking funds; provision of security and guarantees; divestment of debt obligations; private investment funds;

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30 Deloitte, *Understanding corporate usage of British Crown Dependencies and Overseas Territories: A report to the Independent Review of British Offshore Financial Centres* (HM Treasury, London), September 2009. p48

catastrophe bonds and insurance risk securitisation; quasi-charitable trusts and foundations; and voting trusts.

There is significant overlap between the firms in Jersey that carry on trust business for private individuals and those that service corporate and institutional clients.

We estimate that, in 2011, assets from corporate and institutional settlors with a value in the region of £½ trillion were held in Jersey trusts and special purpose vehicles.[31] Of this, around one-third ultimately originates from the United Kingdom and another third from the rest of the European Union. Our survey respondents also report significant use of these vehicles by Middle Eastern and North American clients (five and six per cent respectively). (See Figure 31.)

As with the private trust business, the location of the beneficial owners closely matches the location of the settlors.

Figure 31: Indicative estimate of the value of assets settled by corporate or institutional clients in Jersey trusts or similar vehicles by residence of ultimate settlor and beneficiary, and location of assets*, 2011 (£ millions)

Net Asset Value, £ million, 2011	Settlors		Beneficiaries		Assets*	
		As share		As share		As share
Jersey	**57,972**	**13%**	**63,100**	**14%**	**14,829**	**3%**
United Kingdom	**149,237**	**33%**	**148,789**	**33%**	**221,366**	**49%**
EU	**121,131**	**27%**	**114,467**	**25%**	**84,662**	**19%**
Non-EU world	**120,677**	**27%**	**122,660**	**27%**	**128,159**	**29%**
of which						
Switzerland	25	0%	2,953	1%	7,942	2%
Russia	6,220	1%	6,764	2%	23,474	5%
North America	26,231	6%	28,421	6%	4,630	1%
South America	3	0%	6	0%	12,496	3%
Middle East	20,802	5%	14,131	3%	26,557	6%
Africa	535	0%	586	0%	22,936	5%
China	0	0%	0	0%	0	0%
India	1,693	0%	1,847	0%	10,017	2%
Other Asia Pacific	17,915	4%	19,487	4%	13,238	3%
Total	**449,017**	**100%**	**449,017**	**100%**	**449,017**	**100%**

Sources: Capital Economics' survey 2012/3 scaled up by turnover from the sample to reflect the whole Jersey industry
* Note: Data on location of assets includes assets in trusts settled by private individuals.

Almost all of Jersey's trust and other asset vehicle business are dependent on the island's special international status, and would leave the sterling area if the Crown Dependencies did not exist.[32] Respondents to the survey estimate that, if the Crown Dependencies didn't exist, 89 per cent of their current

31 By and large, we have not sought to examine the trusts, corporate services and SPV market by type or purpose of vehicle, but instead we have focussed on the important distinction between private individuals and institutions as clients. However, see Note 7.10 for further details of trusts and vehicles established as part of the process of rewarding, incentivising and sharing risk with employees.

32 See Note 7.7 for more detail.

corporate and individual trust and asset vehicle business would be conducted outside the United Kingdom – with the majority of the business going to other non-sterling offshore financial centres.

4.5 Funds administration and management

Jersey is a centre for the administration and, to a lesser extent, management of investment funds.

The island's tax neutrality attracts fund promoters who can establish vehicles there that can pool contributions from investors in different countries without them risking being taxed twice, and then accumulate returns from global assets and distribute them back to investors across borders with the same confidence. In addition, the jurisdiction has focussed energy on creating a robust regulatory and legal environment for funds, which not only provides comfort to investors but is also more finely attuned to the needs of specific types of promoter. Jersey offers a full spectrum of fund regulation, from highly regulated so-called 'recognized' funds which may be offered widely to the general public through to un-marketed expert funds which may opt out of regulation if they fulfil stringent criteria. There is also a wide choice of legal vehicle in which funds can operate; they may be established as unit trusts, limited partnerships, separate limited partnerships, incorporated limited partnerships, companies, protected cell companies or incorporated cell companies. In most cases, funds may be open ended or of finite term.

According to official statistics, the island's fund industry employed 460 people in 2011, turned over £170 million and generated £80 million of added value.[33]

There are reliable data published on the scale, nature and geographical spread of funds administered or managed in Jersey. Jersey Financial Services Commission publishes data on the net asset value of funds regulated in the jurisdiction regardless of whether they are domiciled there; but it does not provide information on either asset or investor locations, nor does it report on unregulated business.[34] The *Lipper Fund Encyclopaedia* provides detailed fund-by-fund information on domicile, asset class and asset location by broad area – but offers no insight into the investors.[35] The International Monetary Fund conducts and publishes the *Coordinated Portfolio Investment Survey*, which

33 Source: States of Jersey's *Financial Institutions Survey 2011*. The official data relate to fund and some other wealth 'management', but not fund 'administration' (which is included with trust and corporate business). We have made some crude adjustments to the official data, and believe that a redefined 'fund administration and management' sub-sector was worth more like 1,100 jobs, £290 million turnover and £170 million of gross value added in 2011. (See Figure 46.)

34 Source: Jersey Financial Services Commission.

35 Source: *The Lipper Fund Encyclopaedia*.

provides data on the location of assets and investors, but only for Jersey domiciled and regulated funds and only for a selection of asset classes.[36] (See Figure 32.)

Figure 32: Comparison of data sources for fund activity in Jersey

2011	Total in CE sample	Total in JFSC data	Total in IMF data	Total in Lipper data
		(a)	(b)	(b) (c)
Fund assets (£ m)	141,450	193,590	97,511	172,764
Capital survey penetration		73%	145%	82%
Location of assets	Yes	Partial data	Yes	Partial data
Location of investors	Yes	No	Yes	No

Sources: Capital Economics' survey 2012/13, Jersey Financial Services Commission, International Monetary Fund and the *Lipper Fund Encyclopaedia*

Notes: (a) Based on the average of four quarters. (b) An exchange rate of $1.5 to £1 is assumed. (c) This figure includes only funds administered and/or managed in Jersey; the full survey captures a wider range of funds.

We have used our survey to better understand the geographical distribution of investors and assets across a sample the covers regulated, unregulated, domiciled and non-domiciled funds.[37]

We find that two fifths of the investment into Jersey funds comes from the United Kingdom. Over 40 per cent of investors are located outside the European Union, with one quarter of the total asset value originating in North America. Investment from inside the European Union accounts for the remainder. (See Figure 33.)

Unlike the trust and corporate vehicles business, the bulk of investment (53 per cent) from funds administered in Jersey is channelled into assets in the European Union. The exception is property, where investment into the United Kingdom dominates.

36 Source: International Monetary Fund, *Coordinated Portfolio Investment Survey*.

37 See Note 7.11 for further detail on survey sample and treatment.

Figure 33: Indicative estimate of the net value of funds' assets by location of ultimate investors and assets, 2011 (£ million)

Net Asset Value £ million, 2011	Investors			Assets	
	Total 'immediate investors'	Total 'ultimate investors'	As share of total	Total	Of which: Property
Jersey	**6,336**	**234**	**0%**	**0%**	**0%**
United Kingdom	**71,287**	**77,500**	**40%**	**20%**	**78%**
of which Res Non-Dom	7	7	0%	0%	0%
EU	**33,302**	**32,843**	**17%**	**53%**	**7%**
Non-EU world	**82,664**	**83,013**	**43%**	**27%**	**15%**
Switzerland	19,103	19,844	10%	1%	0%
Russia	201	8	0%	0%	0%
North America	43,701	46,822	24%	7%	0%
South America	11	14	0%	0%	0%
Middle East	3,646	5,433	3%	0%	0%
Africa	861	2,038	1%	2%	0%
China	1,979	2,172	1%	0%	0%
India	4	123	0%	0%	0%
Total	**193,590**	**193,590**	**100%**	**100%**	**100%**

Sources: Capital Economics' survey 2012/3

The majority of Jersey's funds' activity would not have come to the sterling area if it wasn't for Jersey and the other Crown Dependencies' unique status.[38] Respondents to the survey estimate that, if the Crown Dependencies didn't exist, 60 per cent of their current business would be conducted outside the United Kingdom – with almost all of the business going to other non-sterling offshore financial centres.

4.6 Accounting, legal and other professional services

Jersey is host to a range of accountancy and legal firms providing support and advisory services to the finance industry.

According to official statistics for 2011, the professional services sub-sector employed 2,700 workers on the island, turned over £330 million and generated £100 million of profits.[39] Our survey helps to better understand the nature of these businesses' clients, and the scale of the assets over which they advise.[40] (See Figure 34.)

Our sample of eleven professional service companies in Jersey, which account for just over half of the sub-sector's employment and turnover, advised on over £200 billion worth of assets in 2011. The majority of 'initial clients', that is the entity or individual that is commissions directly the practice, were reported to be from Jersey. This suggests that the bulk of the business is

38 See Note 7.7 for more detail.

39 Source: States of Jersey, *Financial Institutions Survey*.

40 See Note 7.12 for further details of survey sample and treatment.

providing services for intermediaries registered in Jersey. For example, a fund administration firm commissions an accountancy practice to do the books for one of their funds.

The geographic profile of the 'ultimate client', which is the ultimate beneficial owner of the asset, is different, and more closely matches the results we have found in the fund and trust sub-sectors. Using the fund example above, this would refer to the investor into the fund, which may be managed in London or elsewhere, and is administered in Jersey. Our results suggest that nearly 50 per cent of the clients are from the United Kingdom. A further third are located in the world beyond the European Union, with North America being the largest share.

Figure 34: The value of assets advised on by the professional services firms responding to the survey, by location of client, 2011 (£ million)

Net Asset Value £ million, 2011				
	Immediate Client	Ultimate Client	Immediate Client	Ultimate Client
Jersey	**126,981**	**20,297**	**60%**	**10%**
United Kingdom	**65,910**	**101,076**	**31%**	**47%**
EU	**3,208**	**17,578**	**2%**	**8%**
Non-EU world	**17,210**	**74,358**	**8%**	**35%**
Switzerland	1,684	12,816	1%	6%
Russia	0	5,557	0%	3%
North America	6,767	29,294	3%	14%
South America	0	2,133	0%	1%
Middle East	699	7,527	0%	4%
Africa	0	4,071	0%	2%
China	0	1,181	0%	1%
India	0	1,473	0%	1%
Total	**213,309**	**213,309**	**100%**	**100%**

Source: Capital Economics' survey 2012/13

4.7 Overall sources, location and beneficiaries of Jersey-held assets

Overall, we estimate that three quarters of the combined value held in the stewardship of Jersey's trusts, special purpose vehicles, funds and banks originated from ultimate beneficial owners who are not domiciled in the United Kingdom.[41] (See Figure 35.)

[41] This has been calculated by combining assets held in Jersey trusts and SPVs with those managed or administered in funds, plus the cash and other liabilities held in the banks. In some respects, it may appear overly simplistic to summarise the breadth of Jersey's financial services' activity into

Figure 35: Indicative estimate of the value of assets held, administered or managed in Jersey by location of ultimate contributor, settlor, investor or depositor, 2011 (£ million)

Net Asset Value, £ million, 2011	Banks			Trusts, funds and other corporate vehicles				All	
	Customer deposits	Interbank deposits and other liabilities	Banks Total	Private trust assets by settlors	Corporate and institutional vehicles by settlor	Funds by investor	Less trust etc. assets held as cash on	Total	As share
Jersey	**4,092**	**5,824**	**9,916**	**8,163**	**57,972**	**234**	**4,629**	**71,655**	**6%**
United Kingdom	**38,430**	**9,767**	**48,197**	**174,016**	**149,237**	**77,500**	**22,628**	**426,322**	**36%**
Private non-dom	11,298	0	11,298	156,378	-	7	10,946	156,737	13%
Private not non-dom	9,368	0	9,368	17,638	-	8,124	1,235	33,896	3%
Corporate or other institutions	17,763	9,767	27,530		149,237	69,369	10,447	235,689	20%
EU	**10,440**	**17,185**	**27,625**	**40,693**	**121,131**	**32,843**	**11,328**	**210,965**	**18%**
Non-EU world	**59,236**	**58,994**	**118,230**	**168,321**	**120,677**	**83,013**	**20,230**	**470,011**	**40%**
of which									
Switzerland	12,926	1,124	14,051	7,895	25	19,844	554	41,261	3%
Russia	5,498	385	5,883	15,478	6,220	8	1,519	26,070	2%
North America	5,401	31,217	36,618	8,580	26,231	46,822	2,437	115,814	10%
South America	4,088	5,211	9,299	1,691	3	14	119	10,888	1%
Middle East	9,521	542	10,063	14,728	20,802	5,433	2,487	48,539	4%
Africa	9,424	93	9,518	30,971	535	2,038	2,205	40,856	3%
China	2,936	615	3,551	1,016	0	2,172	71	6,668	1%
India	2,513	615	3,127	6,381	1,693	123	565	10,760	1%
Other Asia Pacific	6,575	2,454	9,029	54,650	17,915	6,531	5,080	83,044	7%
Total	**112,198**	**91,770**	**203,968**	**391,193**	**449,017**	**193,590**	**58,815**	**1,178,953**	**100%**

Sources: Capital Economics' survey 2012/3

The sources of Jersey's business are far and wide.

An estimated two fifths of the combined value of assets managed was sourced from markets beyond the European Union with North America, Asia Pacific and the Middle East all being major contributing regions. Seventeen per cent derived from ultimate underlying clients in the continental bloc and six per cent from Jersey. Thirteen per cent (over £150 billion) originated from non-doms resident in Britain but not liable for tax there on their foreign income – making Jersey a major conduit for non-dom foreign wealth.[42] Just under one quarter of all assets originated from British domiciled entities or individuals — of which 21 percentage points were corporate or institutional clients.

Britain benefits disproportionately from the investments made by those managing their wealth through Jersey. Almost half of the combined value held in the stewardship of the island's trusts, special purpose vehicles, funds and banks has been invested in assets located in the United Kingdom. (See Figure 36.)

a single measure. Indeed, there is a degree of comparing apples with pears in the computation. But, nevertheless, it does provide a meaningful overall picture across the different sub-sectors.

42 See Note 7.14 for estimates of the number of non-dom clients serviced by Jersey firms.

Figure 36: Indicative estimates of the value of assets held, administered or managed in Jersey by location of underlying asset held, 2011 (£ million)

Net Asset Value £ million, 2011	Banks	Trusts, funds, etc.			All	
	Bank outstanding assets	Trust assets	Fund assets	Less trust assets held on deposit	Total	As share of total
Jersey	**27,699**	**27,749**	**2**	**1,942**	**53,508**	**5%**
United Kingdom	**135,833**	**414,225**	**38,832**	**28,996**	**559,895**	**47%**
Private non-dom	2,090	-	146	-	2,237	0%
Private not non-dom	2,378	-	166	-	2,545	0%
Corporate or other institutions	131,364	-	9,195	-	140,559	12%
EU	**5,101**	**158,422**	**102,657**	**11,090**	**255,091**	**22%**
Non-EU world	**35,335**	**239,814**	**52,098**	**16,787**	**310,460**	**26%**
Switzerland	7,574	14,861	1,352	1,040	22,747	2%
Russia	9,257	43,925	763	3,075	50,870	4%
North America	15	8,664	12,823	606	20,895	2%
South America	917	23,382	280	1,637	22,942	2%
Middle East	136	49,695	8	3,479	46,360	4%
Africa	1,791	42,919	3,525	3,004	45,230	4%
China	289	0	225	0	513	0%
India	46	18,745	638	1,312	18,117	2%
Total	**203,968**	**840,210**	**193,590**	**58,815**	**1,178,953**	**100%**

Sources: Capital Economics' survey 2012/3

Moreover, a disproportionate share of the benefit of the assets accrues to United Kingdom domiciled residents, companies or institutions. They accounted for a third of the combined value of bank assets, trust and special purpose vehicle assets by beneficiary, or funds' investors. (See Figure 37.)

Figure 37: Indicative estimates of the value of assets held, administered or managed in Jersey by location of ultimate beneficiary, 2011 (£ million)

Net Asset Value £ million, 2011	Banks	Trusts, funds and other corporate vehicles					
	Banks outstanding assets	Private trust assets by beneficiary	Corporate and institutional vehicles	Funds by investor	Less trust assets held on deposit	Total	As share
Jersey	**27,699**	**4,056**	**63,100**	**234**	**4,701**	**90,388**	**8%**
United Kingdom	**135,833**	**177,618**	**148,789**	**77,500**	**22,848**	**516,891**	**44%**
Private non-dom	2,090	134,792	-	7	9,435	127,454	11%
Private not non-dom	2,378	42,826	-	8,124	2,998	50,330	4%
Corporate or other institutions	131,364	-	148,789	69,369	10,415	339,107	29%
EU	**5,101**	**47,584**	**114,467**	**32,843**	**11,344**	**188,652**	**16%**
Non-EU world	**35,335**	**161,936**	**122,660**	**83,013**	**19,922**	**383,022**	**32%**
of which							
Switzerland	9,257	8,094	2,953	19,844	773	39,375	3%
Russia	15	8,171	6,764	8	1,045	13,912	1%
North America	917	6,525	28,421	46,822	2,446	80,238	7%
South America	136	1,536	6	14	108	1,584	0%
Middle East	1,791	38,044	14,131	5,433	3,652	55,747	5%
Africa	289	18,853	586	2,038	1,361	20,404	2%
China	46	1,510	0	2,172	106	3,622	0%
India	23	4,519	1,847	123	446	6,067	1%
Other Asia Pacific	6,536	48,049	19,487	6,531	4,728	75,876	6%
Total	**203,968**	**391,193**	**449,017**	**193,590**	**58,815**	**1,178,953**	**100%**

Sources: Capital Economics' survey 2012/3

In total, through a combination of banks' up-streaming and investment from trusts, corporate vehicles and funds, Jersey facilitates foreign investment into the United Kingdom to the tune of £½ trillion. This represents nearly five per cent of the United Kingdom's total stock of foreign owned assets. (See Figure 38.)

Figure 38: Indicative estimates of the investment in United Kingdom assets by foreigners and non-doms mediated by Jersey vehicles, 2011 (£ million)

Net Asset Value, £ million, 2011	Investment in UK assets by foreigners and non-doms mediated by Jersey				
	by private trusts	by corporate and other non-private vehicles	by funds	by banks	**Total**
Total value	184,164	147,792	23,288	111,260	**466,504**
as share of:					
UK stock of foreign owned assets (a)	1.8%	1.4%	0.2%	1.1%	**4.6%**

Source: Capital Economics' survey 2012/3 and Office for National Statistics
Note: (a) Data on the gross international investment position are only available for 2010.

Estimating the impact this investment has on the United Kingdom economy is complex given that there is a vast array of underlying assets that are represented. This makes a bottom-up estimate near impossible.

To provide a simple illustration of the possible impact, we can instead take a 'top-down' approach. UK Trade and Investment publishes research that estimates the total number of direct jobs secured or created by foreign direct investment.[43] Given that we know the proportion of total United Kingdom foreign investment that Jersey is responsible for and how foreign direct investment relates to overall inward investment, we can scale that number to arrive at an estimate of Jersey's contribution to overall foreign investment. Once the indirect and induced impacts are included, we arrive at a figure of approximately 112,000 jobs supported and £5.7 billion of gross value added.[44]

In addition, there is an often symbiotic relationship between financial services firms in Jersey and their counterparts in the City of London. Using results from the survey, an estimated £230 million of business, worth say another 3,600 British jobs, was referred in 2011 from the island to London firms.

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43 http://news.bis.gov.uk/Press-Releases/Jobs-boost-as-UK-attracts-increased-overseas-investment-67d9d.aspx

44 Details of the calculation can be found in Note 7.13.

5 FISCAL LINKAGES

In this section, we examine the fiscal linkages between Jersey and the United Kingdom. Our key findings are:

- **Jersey is almost entirely self-sufficient, with it benefitting only from the United Kingdom's defence and foreign representation activities to which it makes an agreed contribution**

- **No more than £150 million per annum of taxes are currently evaded using Jersey but the new information exchange regime should stop practically all of this. Meanwhile, a maximum of £½ billion per annum could be leaked through tax avoidance**

- **Jersey is the catalyst for significant economic activity in the United Kingdom, which itself generates tax revenues for Whitehall. Our broad estimates of the scale this activity suggest HMRC receive in the order of £2½ billion per annum of revenue from such business**

First, we discuss to what degree Jersey receives fiscal support from the United Kingdom. Second, we discuss the potential for tax leakage for the United Kingdom via Jersey. Third, we discuss the amount of tax generated in the United Kingdom by activity mediated in Jersey.

5.1 Public services

Possibly given its status as a 'dependency', there is an often held view that Jersey is supported by the British taxpayer in terms of public services.

The United Kingdom government on behalf of the Crown is responsible for the defence of the Channel Islands. In addition, islanders are represented to governments abroad by the Foreign and Commonwealth Office, and Jersey passport holders are able to access consular support from United Kingdom embassies and consulates.

There is an agreement between the two governments about how and how much the bailiwick should contribute to the cost of these services.[45] Jersey's agreed contribution comes in the form of its funding for the Jersey Field Squadron, which is a unit of the British armed services' Territorial Army. In

[45] See: The Ministry of Justice Crown Dependencies Branch, *Background briefing on the Crown Dependencies: Jersey, Guernsey and the Isles of Man* (Ministry of Justice, London).

2011, the island's government spent £1.1 million on it.[46] At around £12 per person per annum, this is proportionately lower than the United Kingdom government's total spend on defence, which is around £600 per capita each year.[47] Add to this, a per capita proportionate share of Whitehall's entire £2.2 billion budget for foreign consular and diplomatic operations in 2011 – and, on a simple *pro rata* basis, Jersey receives a benefit of around £60 million per year from Whitehall defence and foreign office spending. But this allocation of costs is in most relevant respects notional; in reality, this money would still be spent if the United Kingdom gave up its military and representation obligations to the island.

In all other respects, the States of Jersey operate separately, and at their own expense – albeit often with close coordination with their British counterparts.

Islanders fund their own health system – although there are reciprocal arrangements so that British visitors to Jersey and Jersey visitors to the United Kingdom can each access local healthcare free of charge.[48] The island's schools, colleges and childcare provisions are all funded locally – while the tuition fees and maintenance costs for local young adults studying in British universities and colleges are borne entirely in the bailiwick.[49] Jersey funds its own policing. It also finances a prison service at a cost of £11 million per annum, although some prisoners maybe held in British jails but at the expense of the States government.[50]

The Crown Dependencies are part of common television licensing arrangements with the United Kingdom, and Jersey households are obliged legally to purchase a license in order to watch broadcast television or stream it live online. BBC outputs are available on island, including Channel Islands' television news and a Jersey local radio station.

The States of Jersey also accrue revenues from the hereditary estate of the Crown on the island. Initially this revenue was to be paid to HM Treasury; however, the Jersey and Guernsey (Financial Provisions) Act 1947 stipulated that a sum equal to that paid into the exchequer will be paid out of the United Kingdom government's consolidated fund to the States of Jersey. We do not believe that the sums involved are significant in the context of this report.

It is also argued that the island benefits from an implicit insurance policy underwritten by the Westminster government under which it would bail-out the bailiwick if it got into severe trouble. This may well be true and, if so, it does have a value to the island. However, the terms of any such insurance

46 Source: States of Jersey, *Annex to Annual Business Plan 2011*.

47 Source: States of Jersey, Institute for Fiscal Studies and Office for National Statistics.

48 Source: States of Jersey website.

49 Source: Capital Economics' review of the States of Jersey website.

50 Source: States of Jersey, *Annex to Annual Business Plan 2011*, HM Treasury, *Public Expenditure Statistical Analysis 2012*, and Office for National Statistics.

policy are at best opaque. London has intervened directly in the Caribbean, but in dependencies where stable self-government hasn't been established or where there has been a major natural disaster. (Indeed, such interventions have extended to locations beyond Overseas Territories or even the Commonwealth.) Jersey has never received such support.

Overall, there is a net benefit to Jersey in the region of £60 million per annum, predominantly through the provision of defence by the United Kingdom in excess of Jersey's contribution.

5.2 Tax leakage

There is a widespread belief that Jersey, Guernsey and the Isle of Man are tax havens and are used by businesses and individuals both legally and illegally to reduce the tax they pay to British authorities. This belief appears to be based largely on impressions set during the Super Tax era of the 1970s and sporadic media exposés on the tax affairs of big companies and celebrities. But the extent to which there are revenues rightfully due to the government that are leaking away has become a turbulent political issue in the current context of fiscal austerity.

There is however little hard evidence about the actual scale of offshore tax abuse and almost no assessment whatsoever of the role of Jersey or the other Crown Dependencies.[51] This lack of evidence should be no surprise in itself. Those involved in tax avoidance and, especially, evasion will have little desire to publicise the activity, and every interest in hiding it. Meanwhile, those trying to demonstrate the 'cleanliness' of their jurisdictions find it almost impossible to prove that little or no such activity takes place there because you can't prove an absence of something simply by failing to find it.

We can't and don't offer a watertight solution to this research conundrum. It can, though, be explored from different directions in order to draw meaningful conclusions about the envelope within which there may be leakage of what might otherwise be legitimate British tax revenues.

5.2.1 Defining tax leakage

Even defining 'tax leakage' is problematic.

HM Revenue and Customs provide a useful typology. 'Evasion' is the illegal and wilful underpayment of tax; 'avoidance' is the lawful under payment of

51 HM Revenue and Customs produced initial estimates of the loss of tax from interest income and undeclared capital in Crown Dependencies' banks in 2005. These predate the implementation of the European Union savings directive and, therefore, are redundant now.

tax through means that are against the spirit of the law and/or intention of Parliament; while 'tax planning' utilises tax reliefs as per the letter of the law and as intended by the policymakers.

At one end, any tax lost through evasion is clearly a leakage of revenues that should have rightfully accrued to the British exchequer. At the other, tax planning shouldn't be viewed as a leakage at all – as it is fully consistent with the letter of the law and the intention of the law-makers. The difficulties are with legal tax avoidance.

Tax authorities will seek to identify avoidance methods and may subsequently tighten the tax code and guidance to eliminate them. In some cases, the courts may be deployed to judge on the appropriate interpretation of legislation. But, as tax has been avoided legally, can the exchequer really assert that it should have rightfully been theirs? As such, is it a tax leakage at all? Moreover, the line between avoidance and tax planning is poorly specified. The exact group of entities a relief was meant to benefit may not be well articulated or the intention of a law made by a previous government may not chime with the current political agenda or public mood. What was once a tax relief intended by government can quickly become an avoidance scheme as the political agenda changes.

These are more than issues of linguistics. They are matters of moral and political judgement – and, as such, make their investigation as part of an objective economics study troublesome.

5.2.2 Quantifying tax leakage

To make some sense of the issues, we focus first on the United Kingdom government's own work in the field.

In the 2013 Budget, HM Treasury make their own estimates of the benefits to the exchequer of the three new inter-governmental agreements with the Crown Dependencies, which will provide for automatic information exchange between tax authorities and ensure that the Jersey-held interests of British taxpayers are reported fully to the HM Revenue and Customs.[52] They estimate that these new FATCA-type arrangements will yield the British government an average of £210 million per annum in revenues from otherwise evaded taxes over the coming five years. Jersey will represent only a fraction of this – with Guernsey and the Isle of Man also impacted. (See Figure 39.)

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52 Source: HM Treasury, *Budget 2013* (London), March 2013.

Figure 39: Estimated increase in tax revenues yielding from FATCA-type arrangements with the Crown Dependencies

£ millions	2013-14	2014-15	2015-16	2016-17	2017-18
Revenues	80	240	325	235	170

Source: HM Treasury, Budget 2013

The HM Treasury analysis is consistent with our own calculations, based on scenario modelling using the results of the survey. Even on cautious assumptions, we estimate that the maximum level of tax evasion plausibly facilitated through Jersey (prior to FATCA) was £150 million per annum. The actual level is probably much lower.

Automatic information exchange will not necessarily banish all evasion of British tax from the island – but, given the States' tough anti-money laundering regulations and its criminalisation of the handling of the proceeds of tax evasion as well as the comprehensive coverage of the FATCA regulations, whatever will be left will likely be immaterial.

The new regime should not, though, have an impact on the lawful activities of British taxpayers on the island – which leaves open the question of the scale of tax avoidance.

HM Treasury provide insight here too. As part of the preparatory work for and published alongside Michael Foot's 2009 report, Deloitte conducted research into the use of the Crown Dependencies and the Overseas Territories by companies wanting to reduce their British corporation tax liabilities.[53] The accountancy practice concluded that: "the element of the UK tax gap potentially attributable to tax avoidance by companies .... is estimated to be up to £2.0 billion. ..... Avoidance through the CDs and OTs would in turn be an unidentified component of this".[54] This leaves little scope for any significant value of avoidance mediated through Jersey.

We concur. By and large, Jersey does not offer firms operating in the United Kingdom with meaningful opportunities to mitigate their corporation tax liability.[55] But there are liabilities to other British taxes that may be reduced through the lawful use of Jersey vehicles.

HM Revenue and Customs' tax gap analysis suggests that nationally there is £2.9 billion of tax lost annually through avoidance of income tax, national

53 Michael Foot, *Final report of the independent review of British offshore financial centres* (HM Treasury, London), October 2009.

54 Deloitte, *Understanding Corporate Usage of British Crown Dependencies and Overseas Territories: A Report to the Independent Review of British Offshore Financial Centres* (HM Treasury, London), 23 September 2009.

55 See Note 7.16 for an explanation of our view.

insurance, capital gains tax, inheritance tax and stamp duty.[56] Even on the basis of the most aggressive assumptions, we calculate that no more than £0.4 billion of this can be mediated through Jersey and, in all likelihood, it is much less. This is consistent with 'bottom-up' calculations using the results from the survey, which show a maximum avoidance of £0.5 billion per annum of British taxes based on the current tax code.[57]

5.3 Tax revenues generated for the United Kingdom

There are also tax revenues that are generated for the British exchequer because of Jersey.

We have reported on the probable shape of Jersey's trade in goods and services, and have estimated that the bailiwick is likely to be running a trade deficit with the United Kingdom which we estimate to be in the order of £0.4 billion per annum. We have also shown that the intermediation of assets and investment in the United Kingdom via Jersey creates jobs and business activity in Britain.

These Jersey-dependent activities and jobs will yield tax revenues for the British exchequer. Using our indicative estimates of the scale of jobs supported in Britain, we calculate that these Jersey-catalysed tax revenues could be in the order of £2.3 billion per annum.[58] (See Figure 40.)

56 See Note 7.15 for details of the HMRC analysis and our calculations of the maximum probable contribution of Jersey to the tax gap. HMRC's values for stamp duty and inheritance tax include all estimated tax losses including but not exclusively avoidance.

57 See Note 7.16 for details of the 'bottom up' calculation of the likely range of tax leakage.

58 Note: (1) Total employment taxes are assessed using the 2011/12 tax liability on the average salary, which is then multiplied by the number of jobs. (2) Corporation tax is assessed, applying the 2011 corporation tax rate, based on the gross operating surplus calculated using the Office for National Statistics input-output tables. (3) Calculations exclude United Kingdom exchequer revenues from air passenger duties paid on flights between the United Kingdom and Jersey, and any taxes generated by business that is brought attracted to the United Kingdom as a result of proximity to Jersey.

Figure 40: Indicative estimates of the tax generated in the United Kingdom from activity catalysed by Jersey

£ millions, 2011	Gross							Net additional
	Exports	*Less imports*	*Less provision of defence and foreign assistance*	Banking (intermediation)	Investment in the UK	Business referals	Total	Considering the two counterfactual scenarios
Employment taxes								
Jobs (number)	29,600	*18,400*	*1,400*	13,666	111,800	3,600	138,866	
Tax[(a)]	**283**	***176***	***13***	**201**	**1,069**	**53**	**1,416**	**400-1,100**
Corporation tax								
Gross operating surplus[(c)]	468	*291*	*22*	664	2,340	175	3,333	
Tax[(b)]	**122**	***76***	***6***	**173**	**608**	**45**	**867**	**200-600**
Total tax (£m)	**405**	**252**	**19**	**374**	**1,677**	**98**	**2,283**	**600-1,700**

Sources: Capital Economics' survey 2012/13

Notes: (a) Taxes include income tax, and employees' and employers' national insurance contributions. (b) Assumes 26 per cent corporation tax. Whilst not all gross operating surpluses will see corporation tax applied, businesses will also generate business rates and value added tax receipts not captured separately here. (c) Calculated from Office for National Statistics input-output tables.

Much of the tax benefit yields directly from Jersey's self-governing status. If the Crown Dependencies were to offer the same tax and regulatory environment as the United Kingdom, the level of tax generated for the exchequer would fall to somewhere in the range of £0.7 to £1.8 billion per annum, meaning Jersey's net additional contribution to the United Kingdom public purse is between £0.6 and £1.7 billion.[59]

59 See Note 7.7 for explanation of counterfactual calculations.

6 JERSEY'S OVERALL IMPACT ON THE BRITISH ECONOMY

In this section, we examine the overall impact, positive and negative, of Jersey on the United Kingdom economy. Our key findings are:

- **Accounting for tax leakage and other net losses, Jersey supports an estimated 180,000 British jobs and adds £9 billion to the United Kingdom economy**
- **If Jersey didn't exist, much of this benefit to the United Kingdom would be lost**

First, we bring together the analyses in previous sections to assess the overall net impact of Jersey on the United Kingdom economy. Second, we consider the extent to which this impact depends on Jersey or whether it would occur regardless.

Do the benefits that Jersey brings to the United Kingdom economy outweigh the costs that it imposes? This report (and the research underpinning it) attempts to bring together the evidence needed, that was previously lacking, to provide a serious, informed and educated answer.

6.1 Jersey's overall benefit

We have examined the likely scale and shape of trade patterns, and uncovered a probable overall trade surplus for Jersey, which we estimate to be in the region of £0.6 billion – but a trade deficit, of around £0.4 billion, with Britain. In other words, the bailiwick is generating income from afar but is spending it on British goods and services, supporting in the order of 11,000 British jobs. (See Section 3.)

We have investigated the linkages between the finance and investment industries either side of the Channel. Jersey accounts for an estimated 1½ per cent of the funding of the balance sheet of the United Kingdom's whole banking sector, which likely supports around 14,000 jobs in British banks alone. Adding in the island's trusts, funds and special purpose vehicles, it is the conduit for almost five per cent of all foreign investment into Britain, potentially supporting well in excess of a further 112,000 jobs in the economy generally. Jersey firms also refer around £230 million of business to their counterparts in the City of London each year, which should support in the order of another 4,000 jobs. (See Section 4.)

And, we have addressed the relationship in terms of public expenditure and taxation. (See Section 5.)

Although Jersey may be a dependency of the Crown, it is not a drain on British public services. The bailiwick benefits from Whitehall expenditure on defence and diplomatic services. Its share of these costs amounts to no more than £60 million annually – or the equivalent of 1,400 British jobs.[60] Otherwise, the island is self-sufficient.

Meanwhile, Jersey's offshore status is used by some businesses and individuals to lawfully and legitimately reduce their liability for tax in the United Kingdom. Some of this may extend into what HM Revenue and Customs might consider tax avoidance, which is lawful tax minimisation that is not necessarily within the spirit of the law. The opportunities for doing so appear limited nowadays. We concur with the overall tenor of the British government's own analyses – and calculate that any tax leakage through avoidance methods is unlikely to be more than £480 million per annum and is probably far lower. In addition, some may attempt to use the island to evade British taxes unlawfully. But the bailiwick's tough anti-money laundering legislation, the absence of bank secrecy laws and its robust implementation of the European Union saving directive mean that anyone would be ill-advised to carry on such business there. Again, in line with HM Treasury, we estimate that tax lost through evasion is no more than £150 million per annum currently – and most of that should be routed with the implementation automatic information exchange as per the recent inter-governmental agreement. Overall, the maximum tax leakage of £630 million per annum may cost the equivalent of up to 14,000 British jobs.[61]

But Jersey also provides a substantial tax benefit to the exchequer. The economic activity in the United Kingdom supported by funds from Jersey's banks, trusts, funds and special purpose vehicles, as well as the island's trade, is itself generating jobs, incomes and profits that are liable to British taxes. Given our previous estimates for the jobs supported, we calculate that around £2.4 billion of United Kingdom tax revenues may accrue from these linkages with Jersey.

Bringing these various factors together, we find that Jersey provides an estimated overall benefit to the United Kingdom economy to the order of 180,000 jobs and £9 billion per annum of economic activity. (See Figure 41.)

60 Jobs are calculated by assuming that the £60 million benefit would otherwise have been spent within the United Kingdom. By using the Office for National Statistics input-output tables this spending can be translated into jobs supported.

61 Jobs are calculated by assuming that the £630 million of lost tax would otherwise have been spent within the United Kingdom. By using the Office for National Statistics input-output tables this spending can be translated into jobs supported.

6.2 Jersey's net additional benefit

We have identified a significant overall benefit accruing to the United Kingdom economy because of its linkages with Jersey, but how much of this is actually dependent on the island? How much of it would occur regardless?

As well as sizing the overall or 'gross' benefit of Jersey to the United Kingdom, we have also considered the island's 'additionality', or its net impact, by considering and comparing against counterfactual scenarios where Jersey does not exist.

Some may argue that, without Jersey or the other Crown Dependencies, the foreign investment, bank funding, etc currently routed via the islands would come to the United Kingdom regardless. This would be dangerous complacency.

It is an advantage that Jersey attracts investors from across the globe – but this also means they are less wedded to the British Isles or to the sterling area. Fifteen per cent of the foreign investment into the United Kingdom mediated through Jersey comes from investors in the Americas, who could quite easily channel their funds via the offshore centres in the Caribbean to the likely eventual benefit of New York. A further nine per cent originates from Asia and Australasia, where Hong Kong, Shanghai and Tokyo offer greater convenience and relevance. Meanwhile, a further seven per cent has a locus nearer Zurich or Dubai, than London.[62] In total, the business in Jersey that comes from beyond the London time zone is worth the equivalent of 51,000 British jobs on our calculations. (See Figure 41.)

The respondents to our survey report that 84 per cent of the island's financial services business would be at risk of leaving the sterling zone if Jersey did not exist. This business, and the consequent investment, is likely to migrate to other offshore centres and not to London. We estimate this could cost almost 150,000 British jobs calculated on a consistent basis. (See Figure 41.)

Although there are uncertainties with research of this nature and margins of error associated with each of the component calculations, overall the various strands of analysis point unquestionably towards Jersey being a material net benefit to the United Kingdom economy. Jersey and the United Kingdom are linked in a symbiotic relationship. The one benefits and supports the other, and vice versa. And, what harms one will also harm the other.

62 See Note 7.7 for calculations.

Figure 41: Indicative estimate of the impact of Jersey on the United Kingdom economy, 2011

£ millions and number of jobs, 2011	Gross impact on United Kingdom		Net additional impact on United Kingdom (against a scenario where Jersey doesn't exist)			
			(Based on survey responses)		(Based on time-zone of client)	
	Jobs	GVA	Jobs	GVA	Jobs	GVA
Exports to Jersey[(a)]	29,600	1,300	13,700	600	5,000	200
Less imports from Jersey	18,400	900	6,300	300	2,300	100
Less provision of defence and foreign assistance	1,400	60	1,400	60	1,400	60
Banking (intermediation services)	13,700	1,300	6,900	600	2,500	200
Investment in the UK intermediated by Jersey	111,800	5,700	93,900	4,800	34,400	1,800
Tax generated	51,600	2,400	39,000	1,800	13,900	700
Less tax leakage [(b)(c)]	14,200	700	2,300	100	2,300	100
Business referrals	3,600	200	3,000	200	900	50
Total	**176,300**	**9,240**	**146,500**	**7,540**	**50,700**	**2,690**

Sources: Capital Economics' survey 2012/13

Notes: The additional impact scenarios net out the activity which would remain in the United Kingdom even if Jersey didn't exist (which for the purposes of this analysis is defined as Jersey having a tax code and legislation identical to that of the United Kingdom. The gross impact figures exclude this. (a) In calculating the net impact we assume that the potential loss of assets corresponds to a loss of business for the financial sector and overall imports in proportion to the financial sector's share of the Jersey economy. Exports are also treated in the same way; as it is assumed that the exports of the financial services to the United Kingdom are reliant on the underlying asset being in Jersey. However they are reduced in line with financial services' share of exports to the United Kingdom as opposed to share in the overall economy. (b) The tax leakage figures used to generate employment here are the maximum generated by our bottom up estimate. (c) In considering how much of the tax leakage is additional the counterfactual differs from the calculation of activity. Here where firms indicated that a proportion of business would leave the island we assume that it would go to avoid tax elsewhere and so only the amount of remaining activity on the island is net additional. Under the time zone analysis, we posit that if United Kingdom residents were using Jersey solely for evasion/avoidance, then they would simply move to another offshore jurisdiction, however we factor in the inertia suggested by our survey response to question of where assets would go if tax and legislation with the United Kingdom.

7 NOTES ON METHODOLOGY AND CALCULATIONS

7.1 Estimating the balance of trade

This note outlines calculations made to estimate Jersey's indicative balance of trade in goods and services.

An overall balance of trade figure is estimated using data on domestic production and domestic demand from a variety of sources. It is computed using the well-known national accounting identity:

Y = C + I + G +(X-M)
And: (X-M) = Y-(C+I+G)

Where: Y is national income; C is consumption; I is investment; G is government; X is exports; and M is imports.

(See Figure 42.)

The trade balances for specific groups of goods and services are calculated by deducting estimated domestic demand from estimated domestic production, using relevant States of Jersey statistics where possible. The analysis is conducted for 34 expenditure groups, which bridge the official output and expenditure reports. (See Figure 43.)

Exports, imports and flows between the Jersey and the United Kingdom are based on relevant specific data where available. Otherwise, they are judgemental values constrained within a model set to yield the values calculated for the various balances above. (See Figure 44.)

Figure 42: Domestic components of gross value added, 2010 (£ million)

£ million, current prices	2010	Notes and sources
GVA		
Gross Value Added	3,555	States of Jersey GVA report 2010.
Less Owner-occupiers imputed rent	388	Data from States of Jersey statistics department.
~ Total GVA	**3,167**	
Domestic components of GVA		
Households' consumption	1,597	Jersey Household Spending Report 2009/10.
less duty and GST	*-95*	States of Jersey Accounts 2010 and Customs and Immigration.
Business investment	466	Calculated using UK ratio of investment to GVA. States of Jersey GVA report 2010 and Office for National Statistics Input-Output tables.
Government current purchases	570	Estimate from the operating cost statement of States of Jersey Annual Accounts 2010. Excludes benefit payments, FX movements, changes in pension liabilities and depreciation.
Government capital expenditure	68	Estimate from States of Jersey Annual Accounts 2010.
Total domestic components of GVA	**2,606**	
Balance of trade	**561**	

Sources: Capital Economics' indicative estimates calculated using States of Jersey and Office for National Statistics statistics

Figure 43: Capital Economics' aggregation of expenditure groups

Capital Economics' aggregation of expenditure groups

1. Food and agricultural goods
2. Alcohol and tobacco
3. Clothing, footwear and textile goods
4. Electricity
5. Other fuel for properties
6. Other utilities
7. Construction
8. Other housing costs
9. Electrical and electronic goods
10. Household goods (other)
11. Medical and Health Services
12. Pharmaceutical and medical products
13. Motor vehicles
14. Vehicle fuel
15. Other personal transport costs
16. Land transport services
17. Air
18. Sea
19. Communications
20. Recreation, cultural and household services
21. Recreation and cultural goods
22. Package holidays
23. Education
24. Higher and further education
25. Other public services
26. Insurance and financial services
27. Wholesale and retail
28. Housing Costs
29. Rent
30. Interest and endowment payments
31. Professional services
32. Other manufactured goods and materials
33. Other vehicles and transport equipment
34. Other business and personal services

Source: Capital Economics' analysis of States of Jersey's household spending survey and *Standard Industrial Classification 2007*

Figure 44: Notes on trade calculations

	Exports		Imports	
	Value	Destination	Value	Destination
Trade in goods				
Food and agricultural goods	Based on published agricultural export values. We believe this is a conservative estimate.	All exports attributed to the UK	Calculated as residual to sum to balance	All attributed to the UK
Alcohol and tobacco	Estimated using Jersey Tourism tourist expenditure data	All exports attributed to the UK	Calculated as residual to sum to balance	All attributed to the UK
Clothing, footwear and textile goods	No exports identified		Calculated as residual to sum to balance	All attributed to the UK
Leisure, travel and recreation goods	Based on data provided by Jersey post on online retailing business	90% attributed to the UK	Calculated as residual to sum to balance	All attributed to the UK
Household and other goods	No exports identified		Calculated as residual to sum to balance	All attributed to the UK
Vehicles and transport equipment	No exports identified		Calculated as residual to sum to balance	All attributed to the UK
Vehicle fuel	No exports identified		Calculated as residual to sum to balance	All attributed to the UK
Electricity, other fuel and utilities	No exports identified		Calculated as residual to sum to balance	Estimate 60% from France, 40% from UK
Construction	No exports identified		Calculated as residual to sum to	All attributed to the UK
Trade in services				
Transport services	Estimated using Jersey Tourism tourist expenditure data and States of Jersey's financial account 2010	Estimated using Jersey Tourism data.	Calculated as residual to sum to balance	All attributed to the UK
Leisure, travel, household and recreation services	Estimated using Jersey Tourism tourist expenditure data	Estimated using Jersey Tourism report. UK 77%.	Calculated as residual to sum to balance	All attributed to the UK
IT and Communications	Calculated as residual to sum to balance	All attributed to the UK	Estimated from Capital Economics' survey and data provided by Jersey Post	Estimated from Capital Economics' survey and data provided by Jersey Post
Financial and professional services	Calculated as residual to sum to balance	Estimated from Capital Economics' survey	Estimated from Capital Economics' survey	Estimated from Capital Economics' survey
Wholesale and retail	Estimated using Jersey Tourisms tourist expenditure data	Estimated using Jersey Tourism tourist expenditure	Calculated as residual to sum to balance	All attributed to the UK
Other expenditure not analysed	No exports identified		Calculated as residual to sum to balance	All attributed to the UK

Sources: Capital Economics' survey 2012/13 and Capital Economics' analysis of official statistics in Jersey and the United Kingdom

7.2 Survey distribution

This note outlines the distribution of the Capital Economics' survey questionnaire.

Detailed questionnaires were issued to 31 of the largest financial and business sector firms in Jersey. Shorter questionnaires, tailored to the specific industry of the respondent, were issued electronically to a wider pool of 101 smaller firms. Interviews were conducted with senior managers in the firms responding to the full survey before, during and after completion in order to address any difficulties and to clarify and validate results. Some post-completion surveys with respondents to the smaller surveys were also conducted. The individual responses contain highly sensitive business information and are confidential; they have been seen by the Capital Economics team only.

Of the 31 longer questionnaires issued, three were not returned and two extra were completed where firms initially identified as a single respondent actually had additional separate subsidiaries for which it was not appropriate to provide a consolidated response; 22 of the shorter surveys were also returned.

7.3 Survey sample coverage and representativeness

This note discusses the depth and quality of the responses received to the Capital Economics' survey.

Fifty two separate completed questionnaires covering the activities of 70 different legal entities were received by Capital Economics. These represent the full breadth of activities conducted by the island's financial services sector, as well as a wide range of companies of different sizes, business models and nationalities. (See Figure 45.) In addition, multiple interviews were conducted with the senior executives of almost all of the responding organisations in order to check, test and validate their submissions.

Figure 45: Number of responses to the Capital Economics' survey and the number of legal entities covered

	Respondents by main activity		Respondents by sub-sector	
	Number of submissions	Number of entities covered	Number of submissions	Number of entities covered
	(a) (b) (c)	(c)	(a) (b) (d) (e) (f)	(d) (e) (f)
Banking	13	19	15	20
Off balance sheet banking	-	-	8	8
Funds	13	16	16	16
Trusts	18	23	19	23
Corporate and institutional vehicles	-	-	16	18
Professional services	10	12	11	13
Total	**52**	**70**	**52**	**70**

Source: Capital Economics' survey 2012/3

Notes: (a) Two submissions were split in order to be consistent with official data and so appear twice. (b) Some submissions contained consolidated data for more than one entity. (c) Entities that undertake wealth management activities as a main activity are counted under funds, which is to ensure consistency with official statistics. (d) Entities that undertake wealth management activities are counted under off balance sheet banking or banking. (e) Entities that undertake both private trust business and corporate trust of company business will be counted in both trusts and corporate and institutional vehicles. (f) Some firms recorded entities they were answering for at the beginning of the survey, but did not go on to answer the questions relating to that entity and so were not counted as having entered a submission for that entity.

Overall, the respondents to the survey reported that the organisations for which they were supplying information employed over 8,000 full time equivalents, which is around two-thirds of the number of jobs recorded in the entire sector by the States of Jersey's statisticians. The respondents also reported an aggregate annual turnover of £1.6 billion, which is roughly three-quarters of the sector total estimated officially. (See Figure 46.)

Figure 46: Metrics to assess the coverage of the Capital Economics' survey

2011	Employment (thousand, FTE)			
	Total in sample	Number of responses	Total in Jersey	Survey penetration
			(a) (b)	
Banking	3,924	12	4,850	81%
Funds	1,023	13	1,130	91%
Trusts & Company administration	1,814	18	3,110	58%
Professional services	1,369	10	2,710	51%
Total	**8,129**	**53**	**12,090**	**67%**

2011	Turnover (£millions)			
	Total in sample	Number of responses	Total in Jersey	Survey penetration
			(a) (c)	
Banking	1,116	13	1,110	101%
Funds	162	12	291	56%
Trusts & Company administration	224	18	429	52%
Professional services	170	10	330	52%
Total	**1,672**	**53**	**2,160**	**77%**

Sources: Capital Economics' survey 2012/3 and States of Jersey's Financial Institutions Survey

Notes: (a) 'Total in Jersey' is based on States of Jersey Financial Institutions Survey statistics, but amended as advised to reflect the categories the Capital Economics survey uses. (b) Total employment exceeds the sum of the column owing to the exclusion of the 'other' category found in the official statistics. (c) Total turnover in banking exceeds official statistics, which is probably the result of definitional and timing differences between the Capital Economics' survey and the official statistics.

Not all respondents to the survey provided details of their profits or the value of their employee compensation. Those that did accounted for roughly half and three-fifths of the industry's totals respectively, as estimated by the States' statistics office. (See Figure 47.)

Figure 47: Further metrics to assess the coverage of the Capital Economics' survey

2011	Profit (£millions)			
	Total in sample	Number of responses	Total in Jersey (a)	Survey penetration
Banking	428	12	841	51%
Funds	23	8	71	33%
Trusts & Company administration	31	12	83	38%
Professional services	48	9	101	48%
Total	**531**	**41**	**1,096**	**48%**

2011	Employee compensation (£ millions)			
	Total in sample	Number of responses	Total in Jersey (a)	Survey penetration
Banking	226	11	340	67%
Funds	41	11	101	41%
Trusts & Company administration	81	15	169	48%
Professional services	70	10	120	58%
Total	**418**	**47**	**730**	**57%**

Sources: Capital Economics' survey 2012/3 and States of Jersey's Financial Institutions Survey

Notes: (a) 'Total in Jersey' is based on States of Jersey Financial Institutions Survey statistics, but amended as advised to reflect the categories the Capital survey uses.

7.4 Banking sample

This note describes the coverage of the responses to the banking sections of the Capital Economics' survey.

In all, fifteen responses to the banking section of the survey, covering twenty separate legal entities, were received. The responses provide information on banking activities, and eight offer details of auxiliary banking activities (such as broking and trading, discretionary management and custodian services). Our banking sample covers an estimated four-fifths of on-island employment in the sub-sector, with a combined balance sheet worth £152 billion in 2011.

Survey results have been scaled up to the totals reported by the JFSC. However, we have adjusted their data in line with the purposes of this study. The regulatory data include details of all banks that are licensed by the island's authorities. This includes one bank, which, although technically headquartered in Jersey, has almost no operational presence there. This bank, which has a sizeable balance sheet worth around £29 billion in 2011 derived from activities outside Europe, is excluded from the analysis. Meanwhile, the official statistics identify £57 billion of total liabilities as 'bank deposits'. Some of these represent the placing on deposit of funds by banks with other banks (often intra-group) strictly on their own accounts. Others include fiduciary deposits which are effectively the placing of private deposits via an intermediary. Where these have been identified they have been treated as private individual deposits and allocated to the country of residence of the underlying private depositor. (See Figure 48.)

Figure 48: Capital Economics' adjustments to JFSC banking statistics, 2011

£ million, 2011	Liabilities				Assets				
	Customer deposits	Bank deposits	Other Liabilities	Total	Up-Streaming	Inter-bank Loans	Customer loans	Other assets	Total
JFSC	**111,980**	**51,494**	**69,635**	**233,109**	**159,180**	**4,321**	**29,879**	**39,728**	**233,108**
Adjustment for bank with minimal operational presence [(a)]	*-a* [1]	*-a* [2]	*-a* [3]	*-a* [4]	*-a* [5]	*-a* [6]	*-a* [7]	*-a* [8]	*-a* [9]
Adjustment for Swiss fiduciary deposits [(a)]	*+b*	*-b*							
Capital Economics	**112,198**	**31,397**	**60,373**	**203,968**	**139,281**	**3,781**	**26,144**	**34,762**	**203,967**

Sources: Capital Economics' survey 2012/3 and Jersey Financial Services Commission data

Note: (a) Sensitive information has been redacted.

The raw results are shown in Figure 49.

Figure 49: Raw survey responses - banking section

£ million, 2011	Customer deposits	As a share	Interbank deposits and other	Total liabilities	As a share	Up-streaming	Inter-bank loans	Customer loans	Other assets	Total	As a share
Jersey	22,981	29%	4,490	27,470	18%	486	22	5,963	11,057	17,528	12%
United Kingdom	14,335	18%	7,456	21,791	14%	97,388	27	2,403	6,493	106,310	70%
Private non-dom	*4,034*	*5%*	-	*4,034*	*3%*	-	-	*441*	*0*	*441*	*0%*
Private not non-dom	*6,241*	*8%*	-	*6,241*	*4%*	-	-	*879*	*2*	*881*	*1%*
Corporate	*4,060*	*5%*	*7,456*	*11,516*	*8%*	*97,388*	*27*	*1,083*	*6,491*	*104,988*	*69%*
Guernsey & IoM	2,770	3%	11,287	14,057	9%	4,635	11	357	458	5,461	4%
Other offshore	4,118	5%	9,750	13,867	9%	0	0	586	5,492	6,078	4%
Europe	13,837	17%	6,613	20,450	13%	8,663	11	597	1,602	10,873	7%
Rest of World	22,166	28%	31,872	54,038	36%	4,223	5	802	463	5,493	4%
Total	**80,206**	**100%**	**71,467**	**151,673**	**100%**	**115,396**	**76**	**10,708**	**25,564**	**151,743**	**100%**

Sources: Capital Economics' survey 2012/13

7.5 Domestic banking activity

This note explains the calculations made to estimate the level of banking activity generated by domestic Jersey and Guernsey based clients.

Banking survey respondents reported a high proportion of deposits originating from Jersey, some £23 million of customer deposits. That is an implausibly high number given the size of the economy. Interviews with respondents revealed that much of this was likely to be business from clients across the world, conducted via Jersey based intermediaries.

To give a more plausible estimate of the size domestic banking assets and liabilities, Jersey's ratios of deposits and customer loan values to gross value added were restricted to the European Union average. (See Figure 50.)

A significant amount of activity was also reported as originating in other Crown Dependencies, most of which again is activity directed through intermediaries. However, interviews also revealed that, in some cases, Guernsey residents are better off banking in Jersey. Therefore we treat some of the deposits and loans reported as originating in Guernsey as genuinely domestic to the Channel Islands. The same methodology is applied as for Jersey, except that Guernsey deposits and loans in Jersey are capped at 25 per cent of total calculated domestic banking assets.

Figure 50: Calculation of domestic banking demand in Jersey and Guernsey

Jersey banks' balance sheets, £ million	Liabilities		Assets
	Private individuals	Corporates	Customer loans
EU average liability to GDP	*0.7*	*0.4*	*3*
Estimated Jersey domestic demand	**2,685**	**1,407**	**10,985**
Estimated Guernsey domestic demand	*1,417*	-	*5,798*
Estimated Guernsey domestic deposits in Jersey	**354**	**-**	**796**

Source and notes: (a) Liability to GDP ratio calculated from data downloaded from Statistical Data Warehouse of the European Central Bank. (b) Jersey domestic demand calculated using Jersey GVA (2011) taken from States of Jersey website. (c) Guernsey domestic demand calculated using Guernsey GDP (2011) taken from States of Guernsey website. (d) 25 per cent of domestic Guernsey private domestic deposits assumed to be in Jersey for tax reasons.

The remainder of the deposits and loans that were reported in the survey as originating in Jersey and the Crown Dependencies were apportioned according to the geographical distribution of settlors in the trust industry. (See Figure 51.)

Figure 51: Allocation to location of ultimate client of deposits and loans reported as from Jersey or another Crown Dependency but in excess of estimated domestic business

	Liabilities		Assets
	Private individuals	Corporates	Customer loans
United Kingdom	45%	38%	52%
of which Res Non-Dom	*41%*	*0%*	*13%*
Guernsey & IoM	0%	4%	0%
Other offshore	13%	8%	8%
Europe	11%	33%	22%
Rest of World	31%	17%	18%
Total	100%	100%	100%

Sources: Capital Economics' survey 2012/3

7.6 Private individuals' deposits of United Kingdom origin but not non-dom

This note investigates the nature of United Kingdom private individuals' deposits that were not reported as originating from United Kingdom non-doms. As part of this, it also compares the deposits implied by the returns from the European Union savings directive with the results from our survey.

Private individuals' deposits from United Kingdom sources which are not non-doms, fall broadly into one of three categories.

First, some of the apparent United Kingdom residents' deposits are not that at all – but are from British expatriates who are living, working, resident and domiciled abroad but using an address back home for their bank account for convenience or security. One of Jersey's largest banks conducted an analysis of their accounts for us and found that 6.9 per cent of the balances held on personal accounts with United Kingdom addresses were from individuals who were actually resident abroad at that point in time.[63]

Second, there are some individuals who are resident and domiciled in the United Kingdom who are actively banking in Jersey with good reason. These res-doms may be preparing for a foreign posting during which they will become expatriate or are serial expatriates currently between foreign postings and not wanting or needing to remit their foreign earnings to Britain. Others may simply find offshore banking more appropriate to their needs. For example, Britons requiring accounts in foreign currencies may be directed by their domestic high street bank to its offshore subsidiary – while former expatriates may have simply wished to maintain the good relationship they had developed with their Jersey-based private bank manager after returning home.

Third, some res-dom depositors using Jersey are doing so passively or unknowingly. Inertia and lethargy are well documented traits of the personal banking market. We have not been able to measure it fully, but it is suspected that there are a large number of inactive and/or small balance accounts among the £9 billion of not non-dom deposits. Indeed, it is possible that some account holders do not realise that they hold Jersey accounts – as many banks automatically move facilities offshore if they believe a customer is no longer liable to United Kingdom tax in order to avoid their liability should they fail to apply properly a withholding charge. There is also likely to be some legacy from deposits attracted on the island some years ago when certain sorts of onshore business were actively sought by some banks.

Nonetheless, there is nothing inherently wrong or illegitimate about someone who is resident and domiciled in Britain banking offshore – provided that any tax that is properly due on the interest earned is declared and paid.

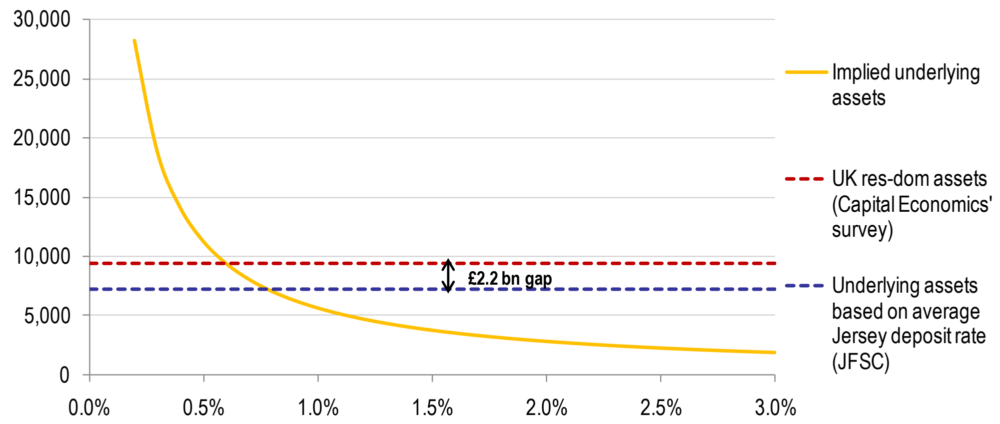
There is evidence to suggest that that is what is happening by and large. Under the European Union savings directive, in which the island participates, banks are required to ensure that any interest paid on accounts held by individuals resident and domiciled in the member states is either disclosed to the relevant national tax authorities or

63 Source: Confidential information kindly provided to Capital Economics via the Jersey Financial Services Commission in March 2013.

has an amount retained for repayment to the appropriate home exchequer. In 2011, the amount retained was initially set at twenty per cent; but rose to 35 per cent from 1 July.

In 2011, the States of Jersey's Comptroller of Taxes, who is responsible for implementing the savings directive, exchanged information with HM Revenue and Customs relating to £45 million of interest paid on accounts registered to British res-doms. In addition, he collected £3.6 million of retention charges on accounts held by Britons, of which £2.7 million was paid to Whitehall with the remainder held by the Jersey authorities following an agreed formula to cover their costs in implementing the scheme. These retention payments relate to in the region of £13 million of interest paid, which when added to the figures for information exchange mean that savings directive measures covered roughly £57 million of interest paid to British res-doms in 2011. Depending upon the interest rate assumed, it is possible to calculate the value of the deposits underlying these interest payments. We estimate that the interest paid in 2011 averaged around 0.6 per cent per annum in Jersey's private banks and 1.0 per cent per annum among the retail banks there – but the range will have been wide between individual banks and individual types of account.[64] But, assuming an average rate of 1.0 per cent would suggest British res-dom deposits of £5.7 billion were subject to the European Union's mechanism – whereas 0.6 per cent would yield £9.4 billion. (See Figure 52.)

Figure 52: Estimates of underlying United Kingdom res-dom deposits from EUSD returns with varied interest rates, 2011 (£ millions)



Sources: Capital Economics' analysis, States of Jersey, Jersey Financial Services Commission

Given the uncertainties around what interest rates would have applied, it is not possible to say categorically that all of the estimated £9 billion of United Kingdom not non-dom deposits in Jersey were subject to information exchange or a withholding tax. However, the likelihood is that the overwhelming majority were – and most, possibly as much as £4-7 billion, had full details exchanged with the British taxman.

7.7 Scale of activity in Jersey reliant on its Crown Dependency status

This note examines what might happen to Jersey and the United Kingdom if the tax code and legislation of the Crown Dependencies were harmonized with that of the United Kingdom, and describes the scenarios used to calculate the net additional benefits and costs of Jersey to the United Kingdom .

How much of the financial flows recorded in the survey are the bailiwick and its self-governing tax neutral status truly responsible for?

Survey respondents considered a fictional and hypothetical world where the three Crown Dependencies, including Jersey, adopted the United Kingdom's tax code and legislation. They estimated how much of their business would stay, and what proportions would go elsewhere.

64 Source: Calculated using aggregated regulatory returns' data kindly provided by Jersey Financial Services Commission relating to the scale of interest paid and liabilities for a sample of private and retail banks.

The banks estimated that nearly two fifths of their business would remain in the British Isles and a similar amount was suggested by the funds administrators and managers – whereas the trust and corporate and institutional vehicle respondents reported that little more than one tenth of their business would stay in the sterling zone. (See Figure 53.)

Figure 53: Impact of hypothetical scenario of Crown Dependencies integration into United Kingdom on location of business that would be conducted currently in Jersey

£ million, 2011	Banking	Trusts	Funds
Stay within Crown Dependencies	**32%**	**6%**	**5%**
UK	**6%**	**5%**	**35%**
Other offshore financial centres	**56%**	**80%**	**59%**
Of which			
Overseas Territories	27%	58%	8%
European centres	26%	6%	6%
Return to home jurisdiction (excl. above)	**2%**	**5%**	**1%**
Other	**5%**	**3%**	**0%**
Total	100%	100%	100%

Sources: Capital Economics' survey 2012/3

This would suggest that around £1 trillion of up-streaming and investment in British assets that is attributable to Jersey would be at risk if the Crown Dependencies lost their status. (See Figure 54.)

Figure 54: Indicative estimates of the value of assets at risk of leaving sterling zone under the hypothetical scenario of Crown Dependencies integration into United Kingdom, 2011 (£ million)

£ million	Banks	Trusts and other corporate vehicles	Funds	Total	
	Bank assets	Trust assets	Fund assets		Potential % loss in assets
Assets at risk	128,016	744,571	116,624	**989,210**	**84%**

Sources: Capital Economics' survey 2012/3

Although business is lost by sterling area intermediaries, it may be argued that capital flows may still come to the United Kingdom because of the City of London's pre-eminence in such markets.

But even this isn't guaranteed.

There are other major financial centres in the Americas and Asia, and emerging ones in the Middle East, that compete with London. These have their own feeder offshore centres – such as the Caribbean jurisdictions working with institutions in New York. Meanwhile, in Europe, Switzerland offers significant depth of capital markets within an offshore and still legally secretive banking environment.

It is reasonable to assume that the business most at risk is that which originates from outside the 'London time-zone'. Including Switzerland and the Middle East, as well as American and Asian time-zones, this amounts to around £170 million of asset value, which is around 30 per cent of the total investment. (See Figure 55.)

Figure 55: Indicative estimates of the value of assets mediated via Jersey by broad location of ultimate client, 2011 (£ million)

Net Asset Value, £ million, 2011	All Jersey business	Jersey flows to the UK		At risk Jersey flows to the UK
	Total investment less trust assets held on deposit	All investment in UK assets	Investment from non-dom and foreign clients	Investment originating outside London time zones
London time zones	898,591	426,975	333,584	39,509
of which				
Switzerland	*41,261*	*16,686*	*16,686*	*16,686*
Dubai time zones	*48,538*	*22,823*	*22,823*	*22,823*
New York/Caribbean time zones	179,888	83,248	83,248	83,248
Tokyo/HK/Shanghai time zones	100,474	49,671	49,671	49,671
Total	**1,178,953**	**559,895**	**466,504**	**172,428**

Sources: Capital Economics' survey 2012/3

7.8 Benefit to United Kingdom banks of up-streamed Jersey deposits

This note outlines the calculations made to estimate the benefit of up-streamed deposits from Jersey to the United Kingdom banking sector.

Given that deposits appear to be inelastic to the interest rate offered, up-streamed deposits from Jersey help British banks meet their liquidity requirements at a lower cost. But what is the value of this?

Quantifying the impact of up-streamed assets is problematic because it is difficult to construct a watertight counterfactual scenario against which the current position can be compared. The current disagreements between high profile international organisations over the analysis of the likely impact of the Basel III reforms only serve to illustrate this point.

Our choice of counterfactual assumes that the alternative for United Kingdom banks would be to use long term wholesale funding (loans of one year or more), which is typically more expensive than customer deposits. This cost has to be absorbed somewhere.

If the banks themselves absorb all of the extra costs then this will mean a fall in employment and spending on other goods and services. It is assumed that all funding from Jersey is lent out again. Our calculations illustrate the potential magnitude of this effect, under our two counterfactual scenarios in which a proportion of assets and financial activity leaves Jersey. (See Figure 56.)

The gross effect column only considers the total effect of up-streamed deposits whilst the second column shows the effect if banks funded themselves using wholesale markets. The result is that around 2,500 – 6,900 jobs are net additional.

The assumption that all of the cost increases are absorbed by the banks is extreme, but it serves to illustrate a point. In reality customers and shareholders would likely absorb any costs as well (through higher loan costs or lower equity returns), although those would also lead to job losses.

Figure 56: Indicative calculations for the impact of up-streaming on employment and gross value added via revenue from intermediation only, 2011 (£ millions)

2011	Gross effect	Net additional impact (jobs)
	(d)	
Assets upstreamed to the UK (£ m)	**117,545**	**117,545**
Funding - lending spread[(a)]	1.0%	1.0%
Funding-lending spread with non-Jersey equivalent funding[(b)]	-	0.4%
% of upstreamed assets that would move outside UK and the Channel	-	30% - 84%
Revenue from loans (£ m)	1,175	1,008 - 583
Direct GVA[(c)]	756	100 - 400
Indirect and Induced effects[(c)]	526	100 - 300
Total GVA supported (£ m)	**1,282**	**200 - 600**
Direct employment supported[(c)]	2,872	500 - 1,400
Indirect and induced employment effects[(c)]	10,794	2,000 - 5,400
Total jobs supported	**13,666**	**2,500 - 6,900**

Sources: Capital Economics' survey 2012/3, Office for National Statistics and Bank of England

Notes: (a) Imputed from Bank of England Data. Based on assumption the Jersey deposits are priced at UK sight deposit rates. (b) Based on Interbank 1 year lending, Quarter average December 2011. (c) Analysis done using Office for National Statistics input-output tables. (d) Calculates the gross impact of upstreaming from Jersey. Assumes all extra money is lent out.

In all, once we include the impacts of spending in the supply chain and the spending of employees, we find that up-streamed deposits support around 13,700 jobs in the United Kingdom and around 2,500 – 6,900 of those jobs would not exist if deposits were not up-streamed from Jersey.

7.9 Trust sample

This note outlines the coverage of responses provided to the trusts section of the Capital Economics' survey.

In all, nineteen private trust administration submissions and sixteen corporate vehicle administration submissions were received.

The nineteen completed survey submissions on private trust business covered 23 different entities employing 1,800 people.

Considering only those with private individuals and families as settlors, our survey sample reported total assets settled in Jersey worth £237 billion. The sample was scaled up in line with official estimates of overall turnover and employment in the sub-sector to obtain results for the island as a whole. Overall, an estimated £0.4 trillion of assets are held in such vehicles.

There is significant overlap between the firms in Jersey that carry on trust business for private individuals and those that service corporate and institutional clients. In our survey, fifteen respondents reporting on trusts for private individuals also disclosed commercial client activity. There was just one submission with only the latter. Assets of £272 billion assets were reported by firms administering corporate and institutional vehicles.

The raw results are shown in Figure 57.

Figure 57: Raw survey responses – private trust and corporate vehicle administration

Net Asset Value £ million, 2011	Settlors				Beneficiaries			Assets	As shares		
	Private trusts	As share	Corporates and other non-private	Total	Private individuals	Corporates and other non-private	Total	All	Settlors	Beneficiaries	Assets
Jersey	4,939	2%	35,073	40,012	2,454	38,175	40,629	16,788	8%	8%	3%
United Kingdom	105,279	44%	90,288	195,567	107,458	90,017	197,476	250,606	38%	39%	49%
of which Res Non-Dom	*94,608*	*40%*	-	*94,608*	*81,549*	-	*81,549*	-	*19%*	*16%*	*0%*
Guernsey & IoM	1,067	0%	10,278	11,345	1,115	11,137	12,252	5,973	2%	2%	1%
Other offshore	29,240	12%	18,213	47,453	29,808	19,837	49,646	33,570	9%	10%	7%
Europe	24,746	10%	77,160	101,906	23,819	73,478	97,296	99,644	20%	19%	20%
Rest of World	71,400	30%	40,643	112,043	72,017	39,010	111,027	101,745	22%	22%	20%
Total	**236,671**	**100%**	**271,655**	**508,326**	**236,671**	**271,655**	**508,326**	**508,326**	**100%**	**100%**	**100%**

Sources: Capital Economics' survey 2012/13

7.10 Employment-related trusts and special purpose vehicles

This note discusses employee benefit related trusts and provides an estimate of the assets held by these entities.

In this report, we have not examined the trusts and similar businesses by type or purpose of vehicle; instead, we have analysed the sector by client: private individuals versus institutions. However, there is one 'type' that has received the attention of British authorities recently, so we have examined them in greater detail. They are trusts and similar vehicles established as part of the process of rewarding, incentivising and sharing risk with employees.

From limited information that we obtained from our survey, we estimate that there is somewhere broadly in the region of £100 billion of assets held in these type of schemes. Of this, around 50 per cent are used by employers located in the United Kingdom. (See Figure 58.)

Figure 58: Indicative estimate of the value of assets held in employee benefit trusts

NAV, £ million, 2011	Settlors		Beneficiaries	
	Corporate settlors	as a share	Private individual	as a share
Jersey	1,145	1%	429	0%
United Kingdom	52,862	53%	53,291	53%
of which Res Non-Dom	-	-	*39,969*	*40%*
Guernsey & IoM	572	1%	0	0%
Other offshore	1,002	1%	1,145	1%
Europe	21,852	22%	22,281	22%
Rest of World	22,567	23%	22,853	23%
Total	**100,000**	**100%**	**100,000**	**100%**

Source: Capital Economics' survey 2012/13

Some forms of these vehicles have come under scrutiny by the media and by HM Revenue and Customs as potential mechanism for the avoidance of tax. Indeed, according to a recent report by the National Audit Office, tax authorities fear that £1.7 billion of British taxes may have been avoided through 'employee benefit trust' schemes and a further £0.6 billion through 'employment intermediary schemes' – some of which can be mediated through offshore structures. [65] However, HM Revenue and Customs now considers that these schemes do not work. And whilst the schemes that existed prior to the 2011 legislation still present some unpaid tax liabilities and some ongoing disputes, losses through these schemes will not continue to accumulate. Hence we do not consider employee benefits trusts as contributing to the 2011 tax leakage in our bottom-up estimate. (See Note 7.16.)

7.11 Funds sample

This note outlines the coverage of the fund management and administration responses to the Capital Economics' survey.

In all, sixteen submissions covering sixteen entities and £141 billion of net assets under management or administration were received. Jersey's regulatory authorities report that there are £194 million of regulated funds administered on island.[66] Although the regulatory figures do not cover the entire industry, it does suggest that our sample is covering the majority of business. The survey sample represents just over half of the sub-sector's turnover. (See Figure 46.)

Most of the sample reported on funds that they administered only (£111 billion of net asset value); indeed, nine out of the sixteen respondents said that they only carried on administration services. A further £27 billion of the sampled funds were managed and administered – while £4 billion managed only. Almost half of the value of the funds in the sample was private equity, while £54 billion was in specialist property vehicles and £5 billion in hedge funds. (See Figure 59.)

Figure 59: Funds' respondents and their assets under administration and/or management

Net Asset Value £ millions, 2011					Number of firms		
	Administered only	Managed only	Managed and administered	Total	Administration only	Management and administration	Total
Assets	**111,053**	**3,700**	**26,696**	**141,450**	**9**	**7**	**16**
Of which:							
Private Equity	44,754	3,700	21,820	70,273	7	5	12
Property	50,949	0	2,558	53,507	7	4	11
Hedge	3,637	0	884	4,521	4	3	7

Sources: Capital Economics' survey 2012/3

The raw results are shown in Figure 60.

65 National Audit Office, *Tax avoidance: tackling marketed avoidance schemes* (The Stationery Office, London), 19 November 2012. p13. Note: figures in respect of employee benefit trust schemes are identified as being then currently under review by HM Revenue and Customs.

66 Source: Jersey Financial Services Commission.

Figure 60: Raw survey response – fund administration and management

Net Asset Value £ million, 2011	Investors			Assets	
	Total 'immediate investors'	Total 'ultimate investors'	As % share	Total	As % share
Jersey	4,630	171	0%	2	0%
United Kingdom	52,087	56,627	40%	28,374	20%
of which Res Non-Dom	5	5	0%	-	-
Guernsey & IoM	1,808	100	0%	963	1%
Other offshore	5,579	411	0%	169	0%
Europe	36,453	38,473	27%	80,738	57%
Rest of World	40,893	45,669	32%	31,203	22%
Total	**141,450**	**141,450**	**100%**	**141,450**	**100%**

Sources: Capital Economics' survey 2012/13

7.12 Professional services sample

This note outlines the coverage of the professional services section of the Capital Economics' survey.

In all, eleven submissions for professional services were received. Responses covered just over half of the industry by employment and turnover, when compared to the official statistics.

The raw results are shown in Figure 61.

Figure 61: Raw survey response – professional services

Net Asset Value £ million, 2011	Clients			
	Immediate Client	Ultimate Client	Initial Client	Ultimate Client
Jersey	126,981	20,297	60%	10%
United Kingdom	65,910	101,076	31%	47%
Guernsey & IoM	5,266	215	2%	0%
Other offshore	2,833	61	1%	0%
Europe	4,854	42,269	2%	20%
Rest of World	7,465	49,390	3%	23%
Total	**213,309**	**213,309**	**100%**	**100%**

Sources: Capital Economics' survey 2012/13

7.13 Calculation of impact of foreign investment into the United Kingdom

This note provides further explanation of our calculation of the benefits of foreign investment in the United Kingdom mediated by Jersey.

We start with the number of direct jobs supported by foreign direct investment in the United Kingdom as reported by UK Trade and Investment. We then reduce this number in line with Jersey's proportion of overall United Kingdom foreign investment, although we make an adjustment to eliminate non-sterling banking assets. This is to reflect the fact that as an international financial centre much of the money will be lent out abroad (and likely more than will come in from foreign financial centres) and so will not be translated into an impact on the United Kingdom economy. Of course the fact that there is extra liquidity for the foreign exchange market will have a positive effect, for example by allowing United Kingdom citizens to change money for investments abroad.

Investment from foreigners in the United Kingdom would have actually supported far more jobs in 2011/12 than the UKTI figures reflect as foreign direct investment is a relatively small proportion of total inward investment. We adjust the number to allow for this. The multiplier of 9.3 shown in Figure 62 is calculated from the international investment position as published by the Office for National Statistics. We then have to include the induced and indirect effects, and we further uplift to include all investment into the United Kingdom by United Kingdom residents through Jersey as these had been previously excluded. This gives us around 112,000 jobs in total and again by using the input-output table we arrive at a contribution to gross value added of £5.7 billion.

Figure 62: Indicative calculation of benefits of investment intermediated by Jersey

Jobs created by FDI[(a)]	112,659
Jersey's foreign assets as % of total investment in the UK (excluding non-sterling loans)[(b)]	3.9%
Ratio of FDI to total investment (excluding derivatives)[(c)]	9.3
Including indirect and induced effects[(d)]	2.1
Ratio of total to foreign investment in UK via Jersey[(e)]	1.3
Total jobs	**111,751**

Sources: Capital Economics , UKTI and Office for National Statistics

Notes: (a) As reported by UKTI for 2011/12: http://news.bis.gov.uk/Press-Releases/Jobs-boost-as-UK-attracts-increased-overseas-investment-67d9d.aspx. (b) Excludes non-sterling bank loans as it is assume that these do not lead to direct investment in the United Kingdom, even though they might help by adding additional liquidity to the foreign exchange market. (c) Based on Office for National Statistics figures for total external investment position, with total excluding financial derivatives. (d) Based on Office for National Statistics input-output tables. (e) Based on Capital Economics' survey results.

7.14 Estimating the number of non-dom clients

This note provides estimates of the number (as opposed to asset value) of non-dom clients using financial services in Jersey.

Six respondents to the survey were able to provide data on the number of non-doms in the United Kingdom that they have as clients.

Scaling up from these suggests there are in the region of 15,000 banking clients and 8,000 trust clients who are currently non-dom. Given the sample size, these results should be used with appropriate caution. (See Figure 63.)

Figure 63: Estimates of the number of United Kingdom non-dom clients of Jersey financial services

	Sample	Estimated number of non-dom clients
		Weighted average of estimates from sample
Banking	2 (16% of employment)	15,400
Trusts	4 (17% of employment)	7,900

Sources: Capital Economics' survey 2012/3

7.15 HM Revenue and Customs' tax gap analysis

This section discusses HM Revenue and Customs' calculation of the tax gap and the proportion that is relevant to activity in Jersey.

The tax gap analysis is the United Kingdom tax authority's own estimate of the scale of tax that is liable but not collected each year. They estimate that £32 billion of tax revenues in 2011 were lost, which is equivalent to six per cent of the total actually collected.[67] Of this, around £4 billion was thought to be lost through evasion and £5 billion avoidance. (See Figure 64.)

Figure 64: Components of the United Kingdom tax gap as estimated by the HMRC, 2011 (£ billion)

£ billions, 2011	
VAT	**9.6**
Avoidance	1.5
Excise duties	**2.3**
Other indirect taxes	**1**
Income tax, national insurance and capital gains	**14.4**
Inaccurate returns by individuals in self assessment	*4.4*
Underpayment of employment taxes by business	*3.7*
Non-declaration by those who do not do returns	*1*
Avoidance	*2.1*
Ghost and moonlighters	*3.2*
Corporation tax	**4.1**
Avoidance	*1.4*
Inheritance tax	**0.2**
Stamp duty	**0.6**
Total UK tax gap	**32.2**

Sources: HM Revenue and Customs

Using these official estimates as a starting point, an envelope within which Jersey's contribution to the overall gap must lie can be calculated. The logic goes:

67 Sources: Capital Economics' survey 2012/13 and Institute for Fiscal Studies.

Only a fraction of the supposed losses in the tax gap analysis can in anyway even partly be facilitated by offshore centres like Jersey. These in-scope elements are the £4 billion of estimated tax evasion and the £4.3 billion of avoidance of direct taxes, stamp duty and inheritance tax;[68]

Jersey is only one of many offshore centres. In the absence of a better source of data, it is reasonable to allocate to Jersey any 'offshore tax leakage' in proportion to its share of recorded portfolio investment flows from the United Kingdom into all offshore financial centres;[69] and

To illustrate the maximum extent of the envelope, we implausibly assume that the entire in-scope tax gap is routed through offshore centres.

On this basis, we estimate that Jersey could have been responsible for a maximum of £0.7 billion of the £32 billion tax gap in 2011 and is equivalent to 0.12 per cent of all tax revenues. (See Figure 65.)

HM Revenue and Customs probably underestimate the tax gap given the methods they use to assess elements of it, which would push up Jersey's maximum contribution. On the other hand, the actual amount for which the bailiwick is responsible will come well below the theoretical maximum because it is likely that a significant proportion of both evasion and avoidance has no offshore component whatsoever.

Figure 65: Calculating the maximum contribution of Jersey to the United Kingdom tax gap, 2011 (£ billion)

Total avoidance tax gap (£bn)[(a)]	4.3
Total evasion tax gap (£bn)	4
Jersey's share of UK investment in tax neutral jurisdictions[(b)]	8.3%
Avoidance loss attributable to Jersey (£bn)	0.3
Evasion loss attributable to Jersey (£bn)	0.3
Total (£bn)	**0.7**

Sources: HM Revenue and Customs and International Monetary Fund

Notes: (a) Includes tax losses from stamp duty and inheritance tax, but excludes VAT avoidance. (b) Based on IMF CPIS survey data for portfolio investment.

7.16 A bottom-up estimate of tax leakage

This note provides our bottom-up estimate of the maximum tax leakage from the United Kingdom through financial services activity in Jersey.

Jersey's share of tax leakage can be estimated bottom-up by considering each of the vehicles that United Kingdom taxpayers can use to hold assets offshore in order to evade or avoid tax. (See Figure 66.) The estimates produce an upper bound figure of around £150 million per annum for evasion and £630 million per annum for avoidance in 2011. Our estimates are based on a combination of our survey results, our own modelling of how specific schemes reduce tax and interviews with financial services industry professionals to establish the extent and nature of different types of activity.

There is a vast array of wealth management vehicles and their structure can be highly complex. We cannot provide detailed accurate calculations of them all. Instead, we have focussed on modelling representative examples of the activity that is carried out in Jersey. Whilst there may be vehicles that provide a means of tax reduction not represented here we believe our estimates to be of the appropriate order of magnitude. (See Figure 66.)

68 We do not include figures for VAT avoidance as the use of Channel Islands to benefit from 'low value consignment relief' was withdrawn in the 2011 autumn statement.

69 Source: International Monetary Fund, *Coordinated Portfolio Investment Survey*.

Figure 66: 'Bottom-up' calculation of maximum potential annual tax leakage from United Kingdom mediated through Jersey, £ million 2011

£ millions, 2011	Maximum tax leakage
Evasion	**151**
Banks	19
Private trusts	132
Avoidance	**479**
Funds	0
Private trusts non-doms	0
Private trusts not non-dom	132
Property trusts	253
Offshored corporate services	94
Administrative losses	
Banks (Withholding tax losses)	4
Total evasion and avoidance	**630**

Sources: Capital Economics' survey 2012/3

We examine potential tax evasion first. Evading tax in another country is illegal in Jersey. Moreover, there is an information exchange agreement with the United Kingdom in place. This means that Jersey gives information to United Kingdom authorities on accounts held by specific individuals under investigation. As a result Jersey is not an attractive location for evading tax, but that does not mean it does not take place at all.

To come to an estimate for evasion, we start by postulating that there are United Kingdom resident domiciled individuals who may be holding cash and other assets in Jersey and not declaring the income earned on those assets to HM Revenue and Customs. We do not include corporate and institutional clients, as they are unlikely to find a meaningful hiding place from tax on income or interest in an offshore account given the level of financial reporting demanded of even small companies nowadays, nor do we include the assets held in Jersey by United Kingdom resident non-dom clients. The latter are not liable to British tax on their foreign and offshore earnings, while Jersey offers them scant protection from United Kingdom authorities should they attempt to evade taxes on their domestic income and wealth using vehicles on the island.

In the banking sector, if we compare the amount of assets implied by the European Union savings directive reporting (see Note 7.6) to our figure for deposits held by United Kingdom residents who are not non-doms (circa £9 billion), we find that a maximum of 40 per cent of banking assets held by Britons in Jersey might not have been declared and therefore might have been evading income tax at a rate of up to 50 per cent. This suggests a maximum tax leakage of £19 million per annum using 2011 data. (In addition, the exchequer in London may have received less via the retention regime than it would have done if the interest income were declared to it. The shortfall could have been as much as £4 million in 2011 – if one assumes that all the interest should have been taxed at 50 per cent and taking account of the deductions make by the States of Jersey for administering the system.[70] This appears in Figure 66 under the administrative losses heading.)

We apply a similar logic to the trust industry. We do not have figures equivalent to the European Union savings directive data for banking to compare to. Instead, to create the upper-bound estimate for the United Kingdom tax gap facilitated by Jersey, we assume that all of the Jersey-held assets of United Kingdom res-doms are engaged in either evasion (as they are not declared) or avoidance (as they are part of a legal vehicle in which the tax is not paid). This is a tough assumption, and likely overstates grossly the level of tax leakage. We estimate that the maximum leakage of British taxes through evasion or avoidance using Jersey private trusts is a maximum of £264 million per annum using 2011 data, assuming an average three per cent rate of return earned on the assets. For the sake of simplicity, we allocate half of this, £132 million per annum, as tax leaked through the non declaration of income arising from trust assets, i.e. evasion.

There may also be historic unpaid taxes relating to the initial capital deposited or settled in Jersey. We believe any such values are likely to be small, and probably immaterial. First, if a British taxpayer were to hide assets offshore, it

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70 This shortfall will have reduced in subsequent years – as the retention rate rose from twenty to 35 per cent on 1 July 2011. Our calculations for the 2011 calendar year are based on an average withholding tax rate of 27½ per cent.

would make more sense for him to do so not in Jersey but in a secretive jurisdiction that does not cooperate with the HM Revenue and Customs. Second, although British tax may now be liable on the income from them, many of the assets themselves will have been settled or deposited at a time when it was legal and possibly even encouraged by the then Westminster government. But even if such unpaid taxes existed and were repatriated, they would offer only a one-off windfall – with no lasting benefit to the exchequer.

Overall we estimate a maximum tax leakage of £151 million per annum through evasion.

Our tax avoidance estimates look at the main types of vehicles in Jersey that might be used to avoid United Kingdom tax. In some cases, a type of vehicle could be in one incidence facilitating avoidance of tax and in another facilitating an intended and legitimate tax reduction. We try to make the distinction as far as possible, but not knowing the true proportions we err towards overstating the levels of avoidance.

We exclude private non-dom assets for the same reasons given above. We also exclude offshore funds as they offer no meaningful tax advantage to Britons – other than, the deferral of tax on any gains rolled up in the funds until they are distributed and repatriated, which will be minimal. Moreover, United Kingdom legislation allows similar tax reliefs for many types of investment funds domiciled in the United Kingdom.

By and large, much of the private res-dom business appears to be a legacy from times when the United Kingdom tax system intentionally conferred advantage to Jersey-based trusts, and that largely those trust assets receive no tax advantage by being in Jersey today. However, there are a few, increasingly obscure, situations in which a trust might enable a United Kingdom res-dom to avoid tax. Our analysis takes an estimate of how much business might be non-residual (based on the estimated half-life of trusts and the estimate of trust assets in Jersey by the Edwards Report[71]) and models a case where an individual sets up a trust as a United Kingdom resident and so pays income tax on all her earnings, but then becomes a non-resident before taking the benefits from the trust. She therefore avoids income tax on the income rolled up in the trust, which we assume accumulates at three per cent a year.

There are other ways in which British tax could be avoided through Jersey private trusts, which we have not modelled. However, we believe our exemplar is representative. Moreover, in our calculations, we make the tough assumption that all trusts settled by British res-doms are either evading or avoiding tax – so our results are likely to overstate any tax leakage.

We estimate that a maximum of £264 million of British tax is evaded or avoided through Jersey private trusts. For the sake simplicity, we allocate half of this, £132 million per annum, to avoidance.

In addition to private trusts there are the trusts and other vehicles established by companies and institutions. We estimate that net assets from settlors in the United Kingdom covered by these amounted to £149 billion in 2011. They cover a multitude of structures and purposes – but the two most relevant to potential tax leakage are employment-related and property-holding vehicles. We consider each in turn.

We estimate that, for 2011, in the region of £50 billion of assets were settled in Jersey by British employers as a part of the process of rewarding, incentivising and sharing risk with employees.

These structures, which include so-called ‘employee benefits trusts’, have sound reasons for locating offshore other than the minimisation of tax payments to the HM Revenue and Customs, including: tax neutrality and the lack of regulation of trust companies in the United Kingdom. In many cases, they have been created in line with the policy objectives of successive Westminster governments, such as greater employee share ownership or deferment of bonuses for senior executives in banking.

However, there have also been examples where they were developed with the intention of avoiding income tax and national insurance contributions. Often these schemes have operated by manipulating the differential treatment under the British tax code of remuneration, which is taxable, and loan advances, which are taxed only on the benefit received comparable to a commercial loan until written off or paid down. This loophole was addressed by the tax authorities in 2010. The changes made by HM Revenue and Customs mean that employment taxes now become payable once a benefit is ear-marked for an individual. So both employee benefit trusts that disguised remuneration as loans and milder ones which only deferred tax no longer work. We therefore count no tax avoidance losses from employee benefit trusts in 2011. There could have been some losses in 2011 from employee benefit trusts as uncertainty about what the changes applied to, may have led to non-payment of tax liabilities, but these should all eventually be recouped.

We estimate that there were around £100 billion of net assets held in Jersey structures by British companies and institutions that were not employee benefit-related. The various types are listed in Section 4.

71 Home Department, *Cm 4109: Review of Financial Regulation in the Crown Dependencies* (The Stationery Office, London), November 1998.

Some structures will be property holding vehicles. And some of these property holding vehicles will be reducing tax in a way that was entirely intended by the British parliament to encourage foreign direct investment into commercial property. These structures benefit the liquidity of the commercial property market – by allowing investors globally to add British real estate to their portfolios on a similar cost basis to other asset classes like general equities and bonds. Without such vehicles, stamp duty land tax would typically add a four per cent charge on every transaction, and would likely render commercial property uncompetitive against other classes where no such costs apply.

However, others may be exploiting the loophole in the law to avoid stamp duty payments on transfers of residential property. But, we don't know the proportions of each, so using wide assumptions for the scale of this activity and plausible figures for the frequency with which property changes hands, we estimate that a maximum of £253 million per annum of stamp duty land tax revenues would have been lost in 2011 through this route.

The second type of structure that appears under corporate avoidance is offshore corporate services. These vehicles provide financial or human resourcing or other services to a parent company in the United Kingdom. Most of these will be entirely legitimate (and not avoiding tax) as they are, for example, international shipping companies whose staff do not work in the United Kingdom anyway. However, it is possible that some are set up only to exploit the difference between corporation tax in Jersey and the United Kingdom. Renting workers employed by the Jersey firm at a mark-up to the United Kingdom firm, allows the United Kingdom firm to reduce its taxable profits.

The numbers in Figure 66 assumes that firms make revenues worth ten per cent of assets, and charge a mark-up of ten to fifteen per cent to the parent firm. This gives an upper bound of £94 million in avoided tax. However, there is good reason to believe that this incidence of this and other types of profit reallocation activity is low. This is because, first, we found little evidence in our survey and interviews.

Second, there is little rationale in the Channel Islands for the type of profit reallocation that for which Switzerland and the Netherlands are used. Jersey has few double taxation agreements with other countries, which would leave any corporate using it as its tax hub at the risk of paying twice. Moreover, in most cases the island is too small for it to have meaningful operations there; as such companies may find it difficult to defend a significant apportionment of revenues and profits to it. As a result few British companies (other than financial services firms) have a presence in Jersey, and those that do are simply serving the local market or appear to be focused on managing their global property portfolios.

Overall this gives an estimate of up to £479 million per annum for tax avoidance.

Pulling together the calculations for avoidance and evasion, the bottom up approach has identified a maximum potential tax leakage of £630 million per annum using data for 2011.

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