States of Jersey

SUMMARY OF FINANCIAL REPORT AND ACCOUNTS 2013

TREASURY
& RESOURCES

Overall Position for 2013 – Income and Expenditure

The States ended the year in a good position. Whilst income was lower than budgeted, expenditure was also less than approved.

General Revenue Income

General Revenue Income policy is set via the States Annual Budget, and covers the main sources of States Income such as Taxes and Duty.

Budget 2013	**Actual 2013**	**1.4%**
£646.0 million	**£636.7 million**	less than the 2013 Budget

Departments' Near Cash Revenue Expenditure

The majority of day-to-day expenditure is made through Departments, as approved in the Medium Term Financial Plan.

MTFP 2013 Approval £626.2 million	**Actual 2013** **£636.2** **million**	**3.5%** Less than the Final Approved Budget
Additional Allocations £32.8 million		

Capital Expenditure

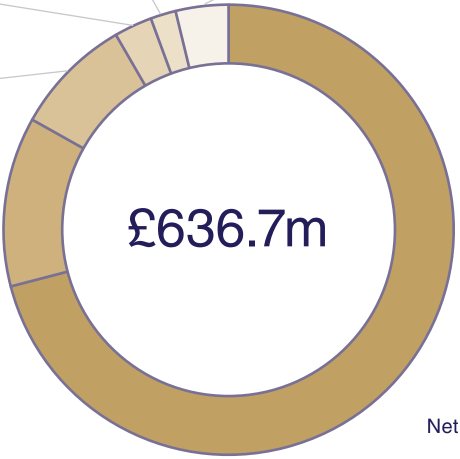
Capital Expenditure is that which enhances assets held by the States for delivery of services, e.g. property and equipment.

Consolidated Fund	**Actual 2013** **£43.2** **million**	**£101.1** million for future years
Trading Operations	**Actual 2013** **£8.3** **million**	**£43.6** million for future years

Whilst Capital Projects may span a number of years, the whole budget is allocated at the beginning of the Project. This means an element of Capital Approvals will be outstanding at the end of every year.

2013 General Revenue Income

General Revenue Income in 2013 was £8 million (1.4%) less than budgeted – mostly due to lower than budgeted Stamp Duty (£7.2 million) and lower than expected Tax revenues (£3.3 million), offset by better than budgeted Fines and Other Income (£3.5 million).



Personal Income Tax

A maximum of 20% standard rate with marginal relief to protect lower income earners.

Company Tax

Companies pay tax under the 0/10 Regime: 10% for Financial Services Companies and 0% for all other non-financial service entities and 20% for property companies and utilities.

Goods and Services Tax

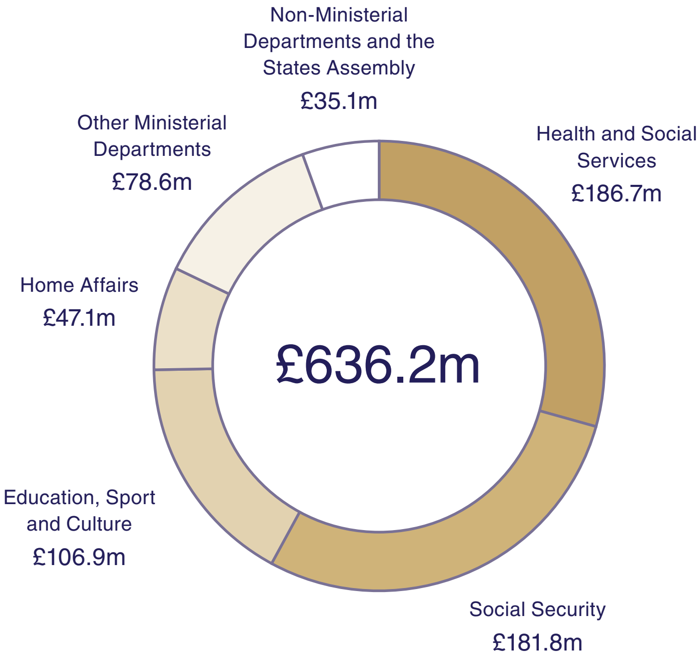
A consumption tax of 5% on imports and supplies made in Jersey. The underlying principles are that the tax is low, broad and simple.

Impôts

Impôts duties are duties charged on goods as they are imported to the Island. The duties apply to a range of commodities including alcohol, tobacco and fuel.

2013 Departmental Revenue Expenditure

Departments spent £636.2 million to provide services to the public – that equates to £15,300 per household.



Health and Social Services
£186.7 million

Promotes health and social wellbeing for the whole community, providing prompt services to all and protecting the interests of the frail and the vulnerable.

Social Security
£181.8 million

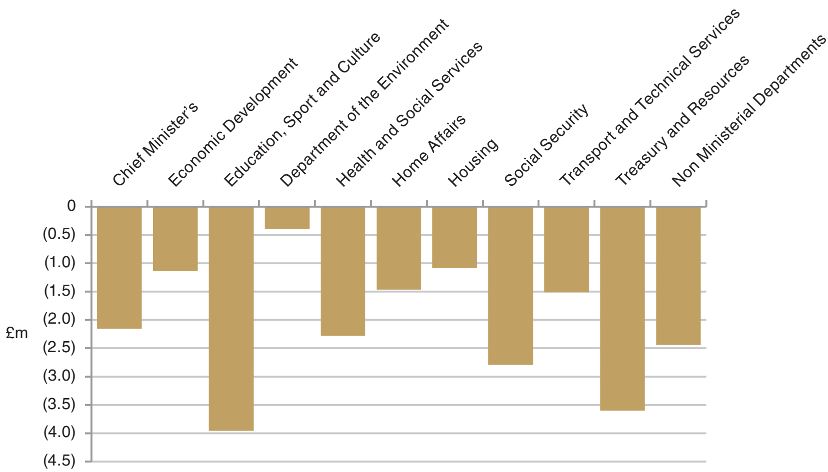
Responsible for the administration of contributions and benefits, the Health and Safety Inspectorate, and a number of employment services.

Education, Sport and Culture
£106.9 million

Provides educational, sporting and cultural opportunities for the people of Jersey, supporting Jersey's commitment to encourage lifelong learning and enabling everyone to realise their potential.

2013 Underspends

As a result of States-wide, careful management of spending, Departments spent £22.8 million less than the total approved amount for 2013. This means that some of this funding can be carried forward by Departments into 2014.



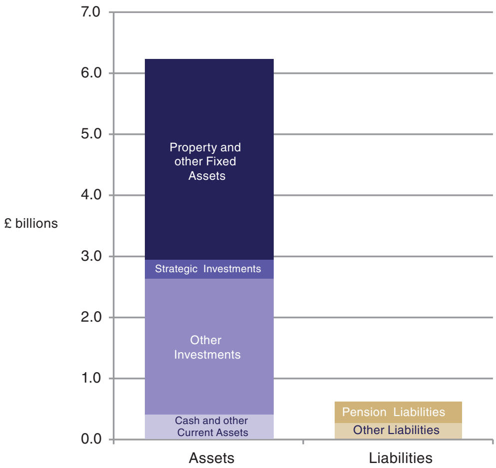
Contingencies of £20.7 million were also maintained during the year.

Carry forwards to 2014

£19.9 million (3.2% of 2013 original departmental budget) of the departmental underspending has been carried forward to fund service priorities. £18.3 million will also be retained as a contingency.

The States Balance Sheet

The States has a healthy balance sheet, with valuable assets and relatively small liabilities. It is vital that the States manages the balance sheet as well as the budget.



Consolidated Fund Balance

This is the States' "Current Account", and as at 31 December 2013 the Consolidated Fund had a balance of £7.5 million.

Strategic Reserve

Jersey has a prudent approach to managing its money and has a "rainy day fund" in the form of the Strategic Reserve. During 2013 strong investment returns from a diversified portfolio delivered an extra £91.9 million - the Strategic Reserve now stands at over £743.1 million. The States have agreed that investment returns will be used to fund the Future Hospital Project.

Social Security (Reserve) Fund

This fund sets aside funds for the future provision of pension benefits to reduce the impact of pensions in future generations. The fund saw returns of £195.6 million and stands at £1.2 billion.

Managing the Balance Sheet

Balance Sheet: Key Initiatives

Some of the key initiatives that the States is taking to manage the balance sheet better include:

- The Effective Management of the Property Portfolio through Jersey Property Holdings.
- Strategic land development through SOJDC.
- Incorporation proposals for Housing and Harbours and Airport.
- Optimising the shareholder value from the States' ownership of utilities.
- Maximising our return on investments in particular the Strategic Reserve and Social Security Reserve.
- Maximising Pension Fund investments and managing future liabilities through planned revisions to the Schemes.

Housing Incorporation

Following a States decision in May 2012, and approvals of relevant legislation in 2013, the Housing Transformation project will go ahead and this means the Housing Department will move to a Company limited by guarantee in 2014. The new housing association will be responsible for the management of all directly provided social housing for the States of Jersey.

The housing association will make a contribution to the States similar to that from the current Housing Department, and so there won't be a significant impact on net expenditure of the States.

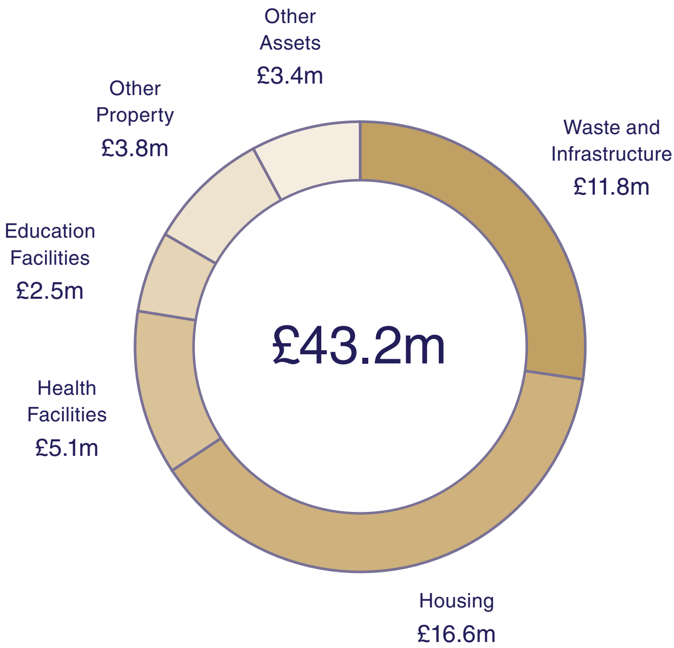
Ports of Jersey Incorporation

Harbours and Airports have now moved from two separate teams to one integrated group. A proposal will be made to incorporate these two separate entities into a new Ports Authority that will move outside the States and become a Strategic Investment wholly owned by the States.

As Harbours and Airports are already obliged to be self-funding the outcome of the incorporation process will not have a significant impact on net expenditure of the States.

2013 Capital Expenditure

A key part of managing the balance sheet is investing in the Assets that the States uses to provide operational services to Islanders. The capital programme recognises the need to invest in the States Assets, and the valuable stimulation that this provides to the Islands' economy. During 2013 amounts were spent on a diverse range of projects:



As well as works on the Island's Infrastructure and Social Housing, major schemes in the year included works on Phillips Street Shaft, the new school in St Martin, refurbishment of Clinique Pinel and improvements to the Prison.

Trading Operations also spent £8.3 million on various projects.

PLANNED PRISON IMPROVEMENTS – STORE ROOM

THE NEW ROLL-ON/ROLL-OFF RAMP IN TRANSIT FROM THE NETHERLANDS

Capital Expenditure – Long term planning

The 2014 Budget Statement included three major projects with individually identified funding sources:

- The Future Hospital – to be funded through returns on the Strategic Reserve.
- Social and affordable Housing –using Jersey's strong balance sheet to borrow funds for the longer term at record low rates of interest.
- Liquid Waste Strategy – using a combination of existing capital budgets, the main capital programme and investment from the Currency Fund.

In addition, the draft 2012-2032 Long Term Capital Plan was published as part of the Medium Term Financial Plan, as has subsequently been updated and extended to 2037. This plan looks ahead to the long term pressures within capital, and includes projects such as:

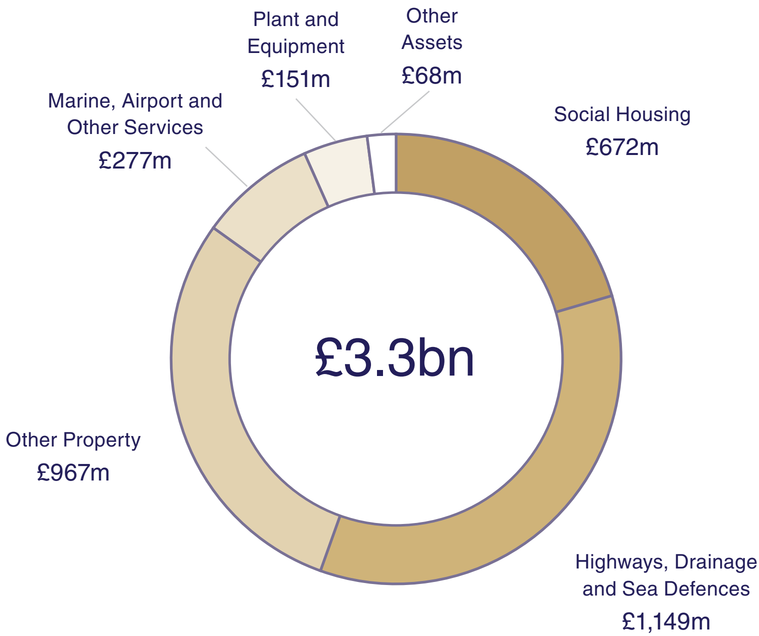
- TTS Infrastructure and Solid Waste Maintenance
- Development and refurbishment of a number of schools
- Redevelopment of Sports Facilities
- Improvements to the Prison, and relocation of Police, Fire and Ambulance Headquarters
- Office Rationalisation

These projects will be funded from a mixture of tax receipts and other funding sources.

States Assets

Property, Plant and Equipment

The States holds Assets to be used in providing services. During the year the States' Property and other Assets were revalued in line with accounting requirements to £3.3 billion.



Depreciation

Depreciation is an amount that represents the cost of "using up" fixed assets – spreading their cost over their useful life. In 2013 depreciation of £52.8 million was charged (including amounts in Trading Operations).

Pension Schemes

The States operates two main pension schemes:

- Public Employees' Contributory Retirement Scheme (PECRS)
- Teachers' Superannuation Fund (JTSF).

These funds are valued in two ways:

- The Actuarial Valuation allows assessment of the sustainability of the scheme, and is carried out every 3 years.
- The IAS 19 (Accounting) Valuation is a snapshot of the current position and assumes a highly conservative investment return which is not reflective of the returns expected from the Fund.

Under an Actuarial Valuation, the ability of the employer and employee contributions to continue to support the benefits is taken into consideration, including the employer's commitment to repay the pre-1987 debt.

Future payments are disregarded under the prescribed method for calculating an IAS 19 Valuation, and so is a less appropriate measure of the long term the long-term sustainability of the Pension Fund.

The current position of each scheme under both methods is given below:

Method	PECRS	JTSF
Actuarial (2010)	£40.6 million surplus	No surplus or deficit
IAS 19 (2013)	£766.9 million deficit	£299.0 million deficit

Whilst the IAS 19 valuation shows deficits in each scheme, the Actuarial Valuations, which provides a more realistic assessment of the long-term sustainability of the Fund, shows a surplus for PECRS, and that the JTSF has neither a surplus or deficit. The surplus in PECRS will be used in accordance with the Scheme Regulations.

Pension Review

Why is review necessary?

- People are living for longer, and drawing on the fund for longer. In 1980 a man retiring at age 60 could expect to live until he was 76, now he can expect to live until 87.
- Investments haven't grown fast enough to generate the required returns, together with the contributions, to fund the pensions.
- The way that we work and live has changed: flexible hours, part-time jobs and different life styles.

The current scheme is no longer sustainable and affordable.

What Principles have been applied

The scheme must be:
- Sustainable (for at least the next 25 years)
- Affordable (for members, employers and the taxpayer)
- Fair (for all members)

What is being proposed?

- Career Average Revalued Earning (CARE) Scheme – for every £66 earned £1 will be added to a members pension pot.
- Additional employee contributions – up to 8% for Non-Uniform employees and 10.1% for Uniform employees – phased in.
- Normal retirement age linked to Jersey state pension age for non-uniform employees, and increased from age 55 to age 60 for Uniform employees.
- Changes to rules to recognise changes to the way we live, for example, recognising co-habiting or civil partners as well as spouses.
- Risk sharing between employer and employees – including a contribution cap for employees, employers and tax payers.

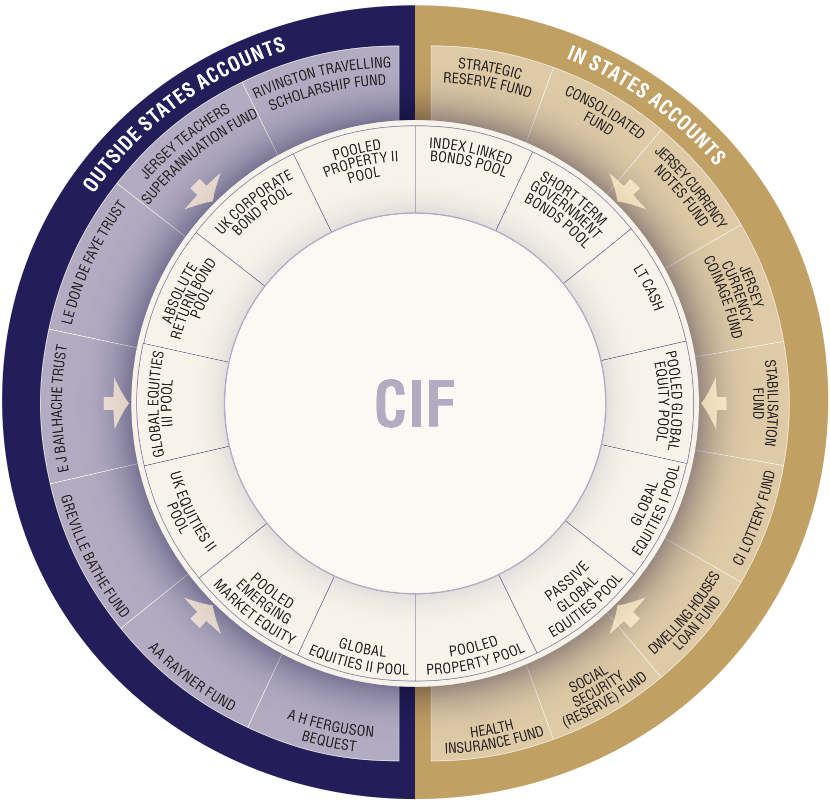
More details can be found on www.gov.je/pensionreview

States' Investment Strategy

The States of Jersey invests any amounts that either aren't immediately needed, or can't be used due to the purpose of the Fund that they have been allocated to. These investments are managed in line with Investment Strategies designed to support the Fund's aims, for example by focusing on income generation or capital maintenance.

The States operates a Common Investment Fund (CIF) to enable States Funds (both in the Accounts and outside of them) to pool resources and benefit from greater investment opportunities, economies of scale and improve risk management.

The Common Investment Fund currently operates fourteen Investment Pools, and has 16 Participant Funds.



Changes to the Investment Strategy

During the year the States has changed both individual funds Investment Strategies and the underlying Pools operated in the CIF to improve the investment options available to Participant Funds. Some of the more substantial changes were:

Consolidated Fund

During the year, improved cash management has allowed a higher proportion of the Consolidated Fund to be invested on a longer term basis, in a balanced portfolio of non-cash assets which are likely to generate higher returns.

Corporate Bond Pools

During the year the corporate bond pools were restructured, replacing long and short term corporate bond pools with a UK corporate bond pool and a global “Absolute Return” bond pool. These new pools allow the investment managers to better pursue the participants Investment Strategy.

Alternative Investment Classes

Investment Strategies also allow Funds to investment in “Alternative Investment Classes”, and during 2013 a Property Investment Pool was set up within the CIF, the first Pool to offer this type of investment.

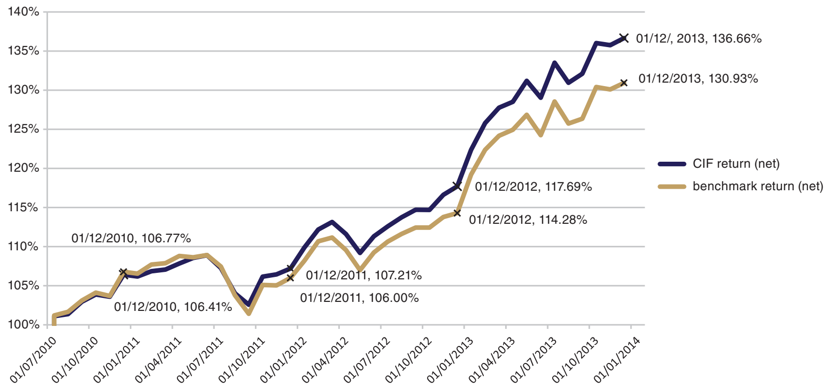
In addition, the Currency Fund has issued Infrastructure Investments totalling £14.9 million outside of its CIF investments. These Investments generate a return to the States whilst supporting the development of the Island’s Infrastructure.

The Common Investment Fund – 2013 Performance

The Common Investment Fund allows States Funds to benefit from economies of scale and a range of diversified investment opportunities that increase returns and manage exposure to risk.

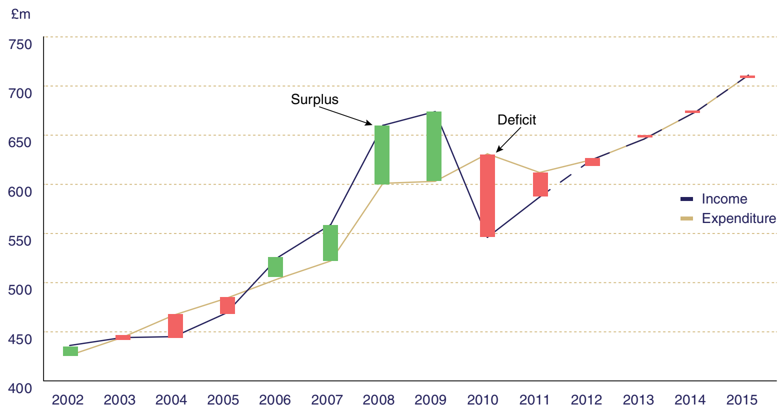
During the year the CIF generated significant income for the States of Jersey; earning net income of £251.0 million in total, representing a return on capital of around 15.9% – exceeding industry wide benchmarks by 1.3%.

The diagram below shows the performance of the CIF, compared to the benchmarks since it was established in 2010.



Not only does the CIF allow Special Funds maximise returns, it provides the opportunity for Trust and Bequest funds under the administration of the Treasury to benefit as well, giving them more money to spend on their charitable causes.

Looking Forward: Forecast Financial Position to 2015



The graph shows a return to broadly balances income and expenditure in 2013 to 2015 and this is based on the following principles.

Balancing Tax and Spending

Resource Principles

- Be prudent, taking account of the uncertain economic and financial outlook.
- Identify and implement all possible savings and efficiencies. (For 2013 and beyond we will optimise methods of service delivery and provide value for money).
- No additional spend unless matched by savings or income.
- Maintain balanced budgets over the medium term for current expenditure and achieve an appropriate balance between taxation and spending over the course of the economic cycle.
- Actively manage the Balance Sheet as well as the Budget by maximising investment returns within agreed levels of risk.
- Plan our expenditure on capital and infrastructure over the long term and consider carefully the appropriate sources of funding for major projects, including borrowing.

The States also have a number of principles that underpin the system of taxation:

- Taxation must be necessary, justifiable and sustainable.
- Taxes should be low, broad and simple.
- Everyone should make an appropriate contribution to the cost of providing services, while those on the lowest incomes are protected.
- Taxes must be internationally competitive.
- Taxation should support economic development and social policy, where possible.

States of Jersey

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