TAX HAVEN IN A SLUMP

PAUL KNIGHT reports from Guernsey, the 24-square mile island (pop: 58,000) which until this year has been a haven for tax avoiders.

PROPERTY sales on Britain's off-shore tax haven have slumped since the Thatcher government reduced the top income tax rate to 40%.

Guernsey is an island close to the French coast, which like neighbouring Jersey has relied heavily on tax exiles for its prosperity as a financial centre.

In the past, the demand for homes pushed up house prices. So to protect locally-born people a two-tier system was created, in which foreigners were excluded from occupying part of the housing stock.

Since Chancellor Nigel Lawson's last tax-cutting budget the sale of the Open Market homes – those available to non-islanders – has slumped. Estate agents report that houses in the mid-range of £300,000-450,000 are "very difficult to push".

In June 1987, 22 Open Market homes were sold – almost half the total for the first six months of this year. Between January and July this year sales amounted to £15.5m, compared with £20.6m over the same period in 1987.

This supports the claim by Norman Lamont, Financial Secretary to the British Treasury, that a tax rate of over 50% has the disincentive effect of encouraging people to "shelter their income".

In the past, the tax shelter has enriched Guernsey landowners who sold properties to mainlanders seeking a haven for their money. But the favourable tax regime under Premier Margaret Thatcher has persuaded some rich people to remain in their mainland homes!

FACT: Guernsey's income tax rate is 20%. There is no Capital Gains Tax, Inheritance Tax, Corporation Tax or Value Added Tax.

FACT: Guernsey's property tax rates have not been increased since 1948. An average Open Market house worth £250,000 ($437,000) is liable for a property tax of £175 ($300) per annum.

Explained Mr H.L. Van Varick, Executive Vice President of American Savings Bank of New York:

"This often happened when a

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homeowner saw a neighbour's house selling for less than the outstanding principal balance on his own house, so the sacrifice of making monthly payments appeared to be too great."

A row is now on in Washington, DC, over who pays – and how. Danny Wall, chairman of the FHLB Board, asked the House of Representatives to pass a resolution which would give the FSLIC the power to raise money through the issue of loan notes.

The notes, which have been issued to raise money to bail out the foundering S&Ls, have not been well received by the financial institutions because of the lingering doubts about FSLIC's own long-term solvency. Some Federal Home Loan Banks – the lenders of last resort to the S&Ls – have refused to accept FSLIC notes as collateral for cash advances.

The politicians are split on what to do. The Reagan Administration regards the

RISK-FREE JACKPOTS

TROUBLED savings and loans associations have become the only gamble in town where the odds are stacked in favour of the punters.

Because of Federal insurance – depositors are covered for every cent up to $100,000 they invest in S&Ls and commercial banks – a crisis-torn institution is forced into a situation where shrewd insiders can spot a risk-free chance to make money. This is how it works.

A weakened S&L is forced to pay above market rates to attract the deposits it needs to keep going. Because it particularly needs long term money, it offers premium rates for deposits of a year or more.

Two Californian S&Ls recently offered 1.5% more than their rivals, which then drove up the rates throughout the local deposit market.

Money brokers spot these opportunities, and invest sums of around $90,000 a time for clients. But that is only the half of it.

The brokers buy long term deposits carrying the premium rate in the hope that the S&L will go bust before the deposit matures. Since the Federal taxpayer covers the principal and accrued interest – and the money is paid out – so the depositor enjoys the long-term rate of interest and receives his money back early.

It's a game in which money is paid to depositors to cover their risks – yet there are no risks!

• The two California S&L's depositors received $1.35 bn (£750m) after Federal regulations closed them down in June.