

2001 Financial Statement

‘Preparing for Competition in the Global Economy’

August 9, 2001

The Prime Minister and Minister of Finance and Economic Affairs, the Right Honourable Owen Arthur presented his Government’s Financial Statement – Economic and Financial Policies on August 8, 2001.

His proposals were based on two objectives:

- 1) To stimulate economic activity in the short term so that real growth could be restored to 3% per annum up from the current rate of 1%; and
- 2) To continue to develop new fiscal, sectoral, human resource development, capacity building, institutional reform, productivity enhancing measures necessary for Barbados’ economy to be competitive in the regional, hemispheric and global economies.

Economic performance

Barbados’ economic performance over the past year has remained robust with continued real growth in GDP. However, expectations for the first half of 2001 are for real growth of less than 1% compared to 3.1% for the corresponding period in 2000. This is the result of a sluggish

performance by the tourism industry and the continuing decline of manufacturing and agriculture. The average annual rate of inflation has been kept in check at 2.7% at April 2001 and the unemployment rate remained at its December 2000 level of 9.3%.

For the 2000/01 fiscal year, Government has maintained a modest fiscal deficit at 2.1% of GDP at factor cost, which was below the budgeted deficit of 2.6%. The budget for the 2001/02 fiscal year anticipates a fiscal deficit of 3.9% of GDP but revised projections now expect this to be maintained at 3.2%.

(\$ millions)	Budget 2000/1	Actual 2000/1	Budget 2001/2	Projected 2001/2	Quarter 1 2001/2
Revenue	1,725	1,717	1,796	1,818	404
Expenditure	1,838	1,808	1,975	1,969	444
Deficit	-113	-91	-179	-151	-40
Deficit (% of GDP)	-2.6	-2.1	-3.9	-3.2	n/a

These fiscal deficits have been financed by Government borrowing, however, the debt service ratio, which compares the total external debt service with exports of goods and service (out of which such debt is serviced) is expected to be 6.1% for 2001/02 which is well within the international standard of 20-25%.

The Proposals

The 2001 proposals include:

- Increased incentives for agriculture and agro-processing particularly in the areas of sugar, cotton, vegetable cultivation,

fisheries and dairy and other livestock farming;

- Introduction of the Sustainable Tourism Bill to provide for broad-based incentives applicable to all areas of the tourism product and the development of a national tourism policy;
- Gradual reduction in the corporate tax rate from 40% down to 37.5% for 2002 and further reductions to 33% by 2006;
- Introduction of allowances for expenditure on intellectual property;
- Promised reform of income tax rates and bands and the existing allowances for income and corporation tax;
- Amendments to certain legislation affecting the international financial services sector;
- Relief on Property Transfer Tax exigible on sale and leaseback transactions;
- Reduction in retail prices of gasoline and diesel;
- Reduction in Severance Fund contributions;
- Extension of the tax holiday period under Fiscal Incentives Act from 10 to 15 years and incentives for retooling;
- Increased pensions;
- Efficiency in VAT department's administration.
- Revised phased liberalization of the telecommunications sector was announced;
- Regulation of the credit unions; and
- Increased taxes on gambling.

Agriculture

The Prime Minister announced a "land use policy", which reserves 31,000 hectares out of our total land area of 43,176 hectares, for agriculture, to be allocated as follows:

Sectors	Hectares
Sugar and cotton	11,000
Vegetables	1,500
Root crops	1,200
Fruit	1,000
Managed grasslands	10,000
Tree/conservation	6,300

Sugar

Government will persevere with cane production but has embarked on bold schemes to make sugar production viable. These include:

- Additional financial support of \$10.55 per tonne for 2000 crop;
- sale in Barbados for local consumption of the first 10,000 tonnes produced;
- a new market programme aimed at selling our sugar, not as a bulk commodity but as a branded special product, for direct consumption to niche markets;
- the production of a number of high grade, high-quality sugars and sugar based products, also for niche markets including our local tourist market;
- the movement to a single sugar factory by the year 2005.

Comments

This is a comprehensive approach to addressing the challenges that are confronting the agricultural sector as a result of globalization and is a bold and well-conceived course of action. Its success will depend on the support and commitment of the partners involved, including investors.

However, farmers need to know what financial assistance will be provided for 2001 and beyond.

Cotton

2,000 hectares be allocated to the production cotton. Government will support the industry and provide:

- an increase in the price support for cotton production – up from \$3.20 per lb to \$4.80 per lb;
- a grant to farmers of \$500 and \$250 per hectare for idle land of plot sizes from 0.2 to 8 hectares and over 8 hectares respectively, brought back into cotton production;
- a rebate of 25% of the cost of certification of organic cotton farms up to a maximum of \$2,000 per farm;
- a ten-year tax holiday for investment in cotton production. Processing and marketing to encourage production from the lint stage to the yarn, fabric and final product stages;
- a technical assistance fund of \$500,000 to assist producers, processors and investors in areas such as feasibility studies, market research, product development and engineering;
- establishment of a revolving working capital fund of \$1,000,000 for those involved in all aspects of the cotton industry to militate against cash flow difficulties;
- duty free concessions on plant, machinery and equipment for all aspects of the cotton industry;
- legislation that would circumscribe the development of cotton as an integrated industry similar to that which obtains for sugar;
- establishment of a cotton research and development fund based on 1% from industry proceeds.

Comments

Government is clearly committed to the idea of cotton for product diversification and a revenue and foreign exchange earner. The above measures are designed to provide the catalyst for investment and growth in this sector. We have seen many attempts in the

past to rejuvenate this sector but none as concerted as this.

The Prime Minister also outlined broad based strategies for assisting local producers including:

- allocation of funds from the Agricultural Development Fund to enterprises embarking on retooling and strengthening areas of activity that hold strong potential in the local and export markets;
- a grant of 30% of the cost of establishing a post harvest facility on the farm for sorting, grading and packaging agricultural products up to maximum of \$5,000 per farmer;
- a grant of 40% of the cost for procuring post harvest equipment such as dipping tanks, grading tables, packaging materials, etc.;
- a grant of 30 percent up to a maximum of \$5,000 of the cost of establishing appropriate chilled facilities;
- a technical assistance fund of \$100,000 to facilitate farmers accessing training in post harvest technology and quality assurance systems. Farmers seeking to benefit from these funds will be required to meet 25% of the cost of the training program.

Comments

These incentives together with those that currently exist such as the agricultural cash rebate should give the industry a much needed kick start.

Export agriculture

The Prime Minister announced measures to stimulate the export of locally produced agricultural products. These include:

- a rebate of 30% up to a maximum of \$10,000 per exporter per year, on the cost

of international transport and freight for fresh produce exports;

- establishment of a technical assistance fund of \$250,000 to assist producers and marketers in the conduct of feasibility studies, access new technology and implement quality assurance schemes related to the export of fresh agricultural produce. Producers and marketers seeking to benefit from these funds will be required to meet 25% of the cost of the respective activities.

Comments

These are only a small part of wider measures required to achieve success in the area of export of local produce. Farmers will have to pool their resources in order to create a climate for tapping into the international markets that are opening up as a result of globalization. These initiatives could include joint marketing and shipping among others.

Tourism

So far performance of this vital sector of the economy has been disappointing, with overall tourist arrivals decreasing by 2.7% in the period to June 2001.

This industry, which is Barbados' prime foreign exchange earner, has been targeted by the Government in its measures to stimulate the economy, by pledging its support to the existing strategic marketing thrusts (developed by the Barbados Tourism Authority in conjunction with the private sector) and by committing \$20 million over three years, with \$6.5 million to be provided immediately.

The proposals under the Sustainable Tourism Bill will extend to operators of restaurants, villas, time-share properties, sports/recreational facilities, and to the establishment and restoration of monuments and other outstanding historical

structures as designated by the National Trust. The most significant of these incentives include:

- Qualifying hotels and restaurants can purchase locally or import a wide range of building materials and equipment for the initial construction or refurbishment of their facilities free of all duties and taxes;
- A deduction for income tax purposes of 150% of the interest on certain loan financing;
- Various expenditures on marketing, training, product development, tourism research, development and operating of trails in rural areas to be used as tourist attractions, for developing computer software which can be used to more effectively measure the performance of the tourism industry amongst others will be granted deductions for tax purposes of 150% of the actual expenditure;
- Additional 50% of expenditure on training may be claimed as a deduction where the tourism project has an employee share ownership scheme;
- Where two or more small hotels are consolidated, no property transfer tax will be payable on hotels purchased for that purpose;
- An investment tax credit of 20% of the expenditure improvements to waste water disposal systems
- An investment tax credit of 30% of the initial capital and equipment cost where such expenditure exceeds \$100,000 related to the refurbishment, upgrading or construction of a facility or attraction which is based on the natural, historical or cultural heritage of Barbados;
- No withholding tax on dividends paid by an approved tourism product to a resident or non-resident.
- Offset of approved capital expenditures over 15 and 20 years.

Owners of villas will be given concession on land tax provided that the villas are registered with the Barbados Tourism Authority and committed to the tourism rental pool for at least nine months of the year. This relief will constitute a rebate equal to 25% of the land tax chargeable.

Comment

This package of incentives displays a strong commitment by the Government of Barbados to this sector. They go well beyond any measures previously available to the sector by encompassing a number of ancillary activities that have an important role to play in the delivery of a quality tourism product.

These measures will be welcomed by all operators in the industry and are long overdue considering that the current tourism incentive legislation, the Hotel Aids Act, was introduced in 1967.

Corporation tax

With effect from income year 2002, the corporation tax rate will be decreased by 2.5% to 37.5%. Further decreases are slated over the next four years to yield, by 2006, a corporation tax rate of 33%.

Tax allowances presently granted to corporations will be reviewed.

A tax deduction will be permitted for 50% of expenditure on intellectual property ("IP"). This amount will be deductible over a 10-year period.

Comment

It is not clear how the rate reduction for income year 2002 will be effected. Will it be introduced in a staggered fashion? This was the case in 1992 when the rate was increased from 35% to 40%; the old rate applied for the period up to June 30, 1992 and the new rate

applied thereafter. Companies with year-ends that are not coterminous with the calendar year will need to monitor this development.

The Prime Minister did not indicate which allowances would be changed but intimated that all would be reviewed.

The introduction of tax allowances for IP is welcome. However, the definition of IP will determine how many companies will be able to take advantage of this new deduction.

Income tax

The Prime Minister promised to change the rates, bands and thresholds and allowances pertaining to income tax for the income year 2003.

Comment

Reductions in the rates and bands of income tax would be most welcome since these have been in place for almost 10 years.

Property Transfer Tax

The recent amendments to the Property Transfer Tax Act ("PTT") regarding sale and leaseback transactions made the cost of entering into such arrangements very prohibitive. It has also prevented companies from effectively managing their cash flow. It is proposed that PTT exigible on such transactions will only be deductible for tax purposes if the lease has been registered with the Registrar of Titles and the relevant PTT and stamp duty paid. It is also proposed that PTT payable on the leaseback of property will be computed on one-half of the capitalized value of the lease.

Comment

While this reduction is welcome, we await guidance on computation of the capitalized value of the lease. Also, the Inland Revenue

Department will now require evidence of registration of the lease to support the PTT deduction so claimed.

International Business Sector

The Prime Minister noted that new legislation would be introduced to permit the formation of Protected Cell Companies and Segregated Accounts and branch registration would be permitted under the Exempt Insurance Act. Similarly, certain reforms aimed at permitting activity within Caricom for International Business Companies, Exempt Societies with Restricted Liabilities and the Exempt Insurance Act would be enacted.

Comment

It is a pity that it has taken almost a year to see these changes legislated and approximately two years for the introduction of Protected Cell Companies and Segregated Accounts. Efforts need to be made to have such legislative changes and the introduction of new “products” introduced in a speedy manner, to meet the needs of this fast changing market.

Energy

With effect from August 13, 2001 gasoline and diesel prices will be reduced by 12.6% and 8.5% respectively as illustrated below:

\$ Per Litre	Current Price	Proposed Price	Price Reduction
Gasoline	1.66	1.45	0.21
Diesel	1.29	1.18	0.11

Comment

This reduction is in keeping with Government’s stated policy of passing on any reduction in oil prices to the consumer.

Social Security

The Prime Minister proposed the reallocation of excess reserves from the Unemployment Fund and the Severance Fund to the National Insurance Fund, as well as the reduction of the contribution rate of the severance fund by 0.5% effective from October 1, 2001.

Comment

These measures have prevented the need to raise the contribution rate or ceiling at this present time.

There was no mention of the funded status of the National Insurance Fund.

The reduction of the severance fund contribution rate from 1% to 0.5% reduces the employers’ contribution rate to 9.25%.

Pensioners

There will be a 7% increase in both minimum contributory and non-contributory pensions effective October 8, 2001. The last increase was in September 1998.

Comment

Pensioners will receive some long overdue relief.

Manufacturing

In addition to the incentives given to the manufacturing sector in the prior years, further financial assistance by way of a new \$25 million Industrial, Investment and Employment fund, was established. This fund will be geared to financing the retooling of industries and providing technical assistance. It is anticipated that through the use of this fund thirty new competitive industrial firms will be created over the next five years.

An additional protection to the manufacturing sector of an applied duty of 60% on extra-regional imports of selected products replaced the surtax regime.

Comment

This is some welcomed news for the business community.

Barbados has made provision for safe-guarding certain agro-processed products, namely, selected oils and fats, processed meats, jams and jellies and selected beverages.

Comment

Manufacturers have succeeded in availing themselves of additional protectionist measures. They must prepare themselves for full trade liberalization in 2005.

Exchange Controls

The Prime Minister proposed to provide the Securities Exchange of Barbados (SEC) with the authority to approve the purchase and sale of shares listed with stock exchanges in member states of the Caricom up to a value of \$3 million. Previously the SEC only had the authority to approve purchase or sales transactions up to a value of \$2 million.

Comment

This gradual liberalisation of exchange controls is in keeping with Government's stated policy.

Value Added Tax

The Prime Minister mentioned that institutional arrangements have been put in place to enable the VAT office to complete refunds within 3 months and, once the system has proven its worth, he will consider making interest payable after 90 days rather than the present 180 days.



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