

# *Tax News*

Barbados Budget  
August 17, 2011

**pwc**

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# The storm rages on

## Introduction

The Minister of Finance has now delivered his second budget presentation in what continues to be a very difficult economic environment. Faced with the most recent downgrade of the country's debt in May of this year, the Minister acknowledges that the situation is precarious, with Government continuing to borrow to finance the total amount of the annual debt service. The twin concerns of deficit and debt that plague so many countries around the world continue to be our greatest challenges.

Having just implemented tax increases effective at the beginning of the year, the Minister has imposed no further taxes at this time and few will disagree with this approach, despite the concern over the deficit. The reality is that the society cannot bear more taxation at this time and any further increases would most likely be counter-productive. Several of the measures are aimed at increasing tax compliance, spreading the tax burden amongst a larger group of tax payers and providing an ease in land tax. At the same time, while the Minister has introduced some targeted incentives in critical areas such as alternative energy, there has been no real attempt to reduce taxes, either at the personal or corporate level. Although some will argue that the economy would benefit from the stimulus which might be created through a reduction in taxes, the Minister has clearly decided that now is not the time and he must maintain current revenue levels if he is to avoid drastic expenditure cuts and the consequential impact on employment levels. His choices are very limited.

The Minister has indicated the need to reduce the deficit for 2011/2012 including amortization to within \$500 million as a matter of urgency. Based on the Minister's strategy as outlined, the projection is for a deficit of \$461.9 million or 5.2% of GDP based on performance for the first quarter of the year. This is slightly better than that of the Medium Term Fiscal Strategy of 5.6% and is to be achieved through a revenue increase of \$150.9 million and an expenditure decrease of \$514.8 million over the prior year. The details on expenditure reduction are broad and not specific, the strategies including cuts in transfers to

statutory entities. However, to some extent these transfers are being replaced with a funding package of \$110 million from the National Insurance Board. It is unclear how this arrangement, which results in a loan to these entities, serviced through the Consolidated Fund if necessary, will achieve a real reduction in expenditures. There has in recent years been some public discussion about the extent of Government debt held by the National Insurance Board and, while there are clearly advantages to Government being able to access such funding, there are also associated risks which are no doubt subject to careful monitoring by the NIB. Beyond this item, achieving the necessary efficiencies will require a significant commitment across the entire public sector.

We were expecting to see more from the Minister in some critical areas. Specifically, we were surprised that no mention has been made of the opportunities to improve the country's financial position through an aggressive programme of privatisation and, in an environment where there is limited capacity to either raise taxes or reduce expenditures, significant efforts must be made to drive economic activity. We would therefore have expected a stronger emphasis on specific initiatives to facilitate business, both domestic and international. On the international front, the country's ability to maintain and grow the sector will demand a higher level of agility and responsiveness from Government than has been achieved to date. On the domestic front, business profits are significantly down after three years of recession and business owners are digging into their reserves to maintain operations and employment. An improved business environment is critical and urgent consideration must be given to the recommendations from industry representative groups.

While we are all keenly looking for signs of recovery, Barbados does not exhibit many positive signs at this time. While it is encouraging that tourism numbers are up, overall spending is not. Some comfort may be taken from the fact that our foreign currency reserves remain at a reasonable level.

One of the areas given significant attention by the Minister is alternative energy. With the cost of oil imports in 2009 representing 6% of GDP, a level comparable to Government expenditure on education, it is heartening to see Government's commitment in this area.

The risks to the country of our current reliance on imported oil, the price of which is entirely beyond our control, are enormous as are the benefits from the development of alternative energy sources. This is an important element of a broader greening of Barbados which will benefit every aspect of life within the country.

## Separation of business and employment income

The Minister has proposed, with effect from income year 2011, to separate the computation of tax payable on business income from employment income and prevent the offsetting of losses from businesses against employment income.

### Comments

This proposal removes one of the longstanding benefits that have been enjoyed by individuals who had both employment income and business income. This amendment will increase taxes from employment income and will compensate to some extent for the decline in corporate tax revenue. It can be argued that this change might act as a disincentive to part-time entrepreneurs who are seeking to earn additional income in tight economic times but will have no opportunity to offset losses in the early years of a new business. This measure underscores the financial challenges which are currently being experienced in the economy and an attempt to stop further haemorrhaging of Government's revenue.

## Renewable energy

The Minister has proposed a number of initiatives with respect to the conservation of energy and is looking for a paradigm shift in the move to renewable energy and energy efficiency. These measures include:

- an increase in the energy conservation and renewable energy deduction from \$5,000 to \$10,000 for individuals and \$25,000 for registered small business;
- an extension of the energy conservation and renewable energy deduction to lessees once it is proven that approval was granted by the owner of the property;
- the write-off of 150% of costs associated with the conversion to alternative energy over a five year period for businesses whose filings with the Inland Revenue Department and VAT Division and whose compliance with NIS and Land Tax are up to date or who have in place arrangements to settle their arrears;

- a rebate of up to \$5,000 to farmers who retrofit structures to house livestock with solar energy;
- the discontinuation of the duty free concessions offered to the hotel and manufacturing sector on the importation of electric water heaters;
- the provision of an energy grant of \$5 million through the Welfare Department, with effect from October 1, 2011, to provide relief to the most vulnerable groups such as the elderly, disabled and the unemployed indigent to mitigate the high cost of electricity;
- the negotiation of a second energy based loan of US\$75 million to execute the preparation of renewable and energy efficiency policies through the necessary legislation to supplement the initial loan of US\$75 million;
- submission of draft renewable energy and energy efficiency policies to Cabinet along with proposals for the amendment of the relevant legislation; and
- drafting of legislation on the renewable energy policy to facilitate the generation of electricity by renewable energy systems and the sale of electricity to the grid.

The Minister further advised that Government through its comprehensive programme will create an institutional, policy and operational framework that will set the appropriate incentives to generate substantial energy savings, reduce the cost of electricity to households and businesses and contribute to a reduction of oil imports and hence liberate foreign exchange for other purposes.

### Comments

The rising cost of oil and in turn electricity is of grave concern to many Barbadians and the world at large. Many persons the world over are seeking various alternatives to the costly commodity, especially as the average cost of crude oil is not expected to decline. The incentives proposed for individuals and companies should encourage persons to seek alternative energy sources.

The energy grant should be welcome news to those persons who are among the more vulnerable in our society. However, it is not clear whether the grant will be offered to those persons who are currently in the welfare system or on what basis, if any, other persons may be able to obtain such a grant. It is hoped that further details on this will follow and also that legislation on the renewable energy policy will be "swift in coming".

In the first financial statement and budgetary proposals by the late Prime Minister Right Honourable David Thompson, the Government indicated its desire to take a lead in moving Barbados away from dependence on imported fossil fuels and towards energy independence. These proposals included reviewing its own buildings and fleets of vehicles with the goal of energy conservation in mind and examining alternative energy projects for Government installations. The Minister alluded to some progress in this area in his presentation.

## Land tax

### Land tax bands

Effective tax year 2011/2012 the adjusted bands for residential properties have been proposed as follows:

### Improved land

On which there is a dwelling house that is used exclusively for residential purposes:

On first \$190, 000	Nil
On amounts between \$190,000 to \$500,000	0.10% of the improved value
On amounts between \$500,000 to \$1,250,000	0.45% of the improved value
On amounts exceeding \$1,250,000	0.75% of the improved value

### Land tax rebates

Land tax rebates and/or exemptions for income year 2012/2013 have now been extended to approved manufacturers who can certify exports to a value of \$100,000 or more in any one calendar year.

In addition, any company, certified by the Division of Energy to be engaged in the production of solar energy and/or the manufacturing sector of solar energy equipment will be entitled to the rebate of no more than 50% on the land tax demanded for that year.

The above-mentioned will, effective from 2012/2013, join the list of four other categories of properties/persons currently entitled to the rebate, namely hotels, agriculture, villas and pensioners.

Effective 2011/2012 registrants within the hotel sector and standalone restaurants off property will be allowed to pay their land tax bill during the last quarter of the Government's fiscal year (January to

March) without losing access to the discount granted.

A tax clearance from IRD and/or VAT will be required to access the rebate.

## Comments

The adjustment to the bands will offset recent valuation increases, which created a certain amount of consternation in the current economic environment. Whether an individual sees an increase or decrease over the prior year will depend on the valuation of their specific property and the extent of the increase in that valuation in the recent triennial re-assessment.

The concession to pay the tax bill in the last quarter of the Government's year and still obtain the discount should ease the burden of the cash flow for those in the tourism industry.

The manufacturing sector for a long time has been seeking concessions for the industry and will welcome these proposals.

## Tourism

### Land tax rebates

The Minister has stated that for hotels and villas enjoying land tax rebates, the 25% or 50% rebate should be calculated based on the tax demanded and not on the site or improved values of the properties.

As noted above, with effect from tax year 2011/2012 it is proposed that registrants of the hotel sector and stand alone restaurants "off property" be allowed to defer the payment of their land tax bills.

### Global insurance for the cruise industry

In order for local businesses that offer attractions and tours to travelers in the cruise industry to contract with the cruise ships, it is often necessary for such businesses to obtain the required insurance coverage from a foreign insurers.

On the remittance of payments of insurance premiums to foreign persons there is a requirement to pay 20% tax. Effective income year 2012, this tax will be reduced or will no longer apply.

### Timeshare input tax

The Minister seeks to correct an anomaly whereby the supply of timeshare property within the VAT Act is an exempt supply and therefore no refunds of input VAT are permissible, and the Tourism Development Act which allows for the recovery of VAT on inputs related to the construction of the timeshare property. Through zero rating the supply of an “approved” timeshare property, the recovery of all VAT suffered on inputs by persons holding a permit issued under the Tourism Development Act will be permitted.

### Motor sports tourism

With the increased popularity of motor racing the Government has attempted to facilitate the development of this area. In so doing, the following are proposed:

- an agreement to lease the Bushy Park facility to the Barbados Rally Club to enable a full upgrade of the race track and adjoining facilities to international racing standards;
- a commitment by Government to give favourable consideration to an appropriate package of tax and other concessions to facilitate the successful building of the facility; and
- effective September 1, 2011, all sporting vehicles, equipment and gear temporarily imported for the sole purpose of competitive activities will either be exempted or zero rated for the purposes of VAT.

It is stated that these concessions will go a long way towards elevating Barbados to the newest category 3 Circuit and Kart Facility in the Western hemisphere.

### Electric water heaters

Effective January 1, 2012, there will be no duty free concessions with respect to the importation of electric water heaters by hotels.

## Comments

These provisions should be well received.

The removal of the tax on remittances should be a considerable help to the operators of tourism attractions and tours through reducing their costs.

The zero rating of the supply of timeshare units proposed should also bring some considerable relief to the providers of timeshare properties and may even permit them to reduce their prices.

Tourism investors will welcome the deferral of land tax payments, which should increase their ability to manage cash flows.

The removal of concessions for electric water heaters is consistent with Government’s alternative energy programme.

Motor sports enthusiasts will welcome the concessions proposed in support of what is a vibrant and fast growing sport in Barbados, which has the potential to contribute significantly to foreign exchange earnings.

## Amendments to the Occupational Pensions Benefit Regulations and Income Tax Act

The Minister proposed to reintroduce into the Income Tax Act the provision that on the date of retirement, a member of a pension plan can receive up to 25 per cent of the commuted value of his pension in the form of a tax free lump sum. This re-instatement will come into effect on February 15, 2011 which coincides with the date the Occupational Pensions Benefit Regulations was enacted.

He revealed that after some concerns had been raised about the onerous fee structure set out in the regulations to the new pension legislation that the Financial Services Commission had reviewed these and recommended that they be revised taking into consideration the size of the pension plan based on its membership. The proposed new structure shall take effect from September 1, 2011.

It is also proposed that the regulations be amended to provide for a drawdown account for members under a defined contribution pension plan as an alternative to the purchase of an annuity on retirement as is currently the requirement under the Act.

## Comments

The proposed amendment to the Income Tax Act will resolve the last concerns which arose on the proclamation of the Occupational Pensions Benefits Regulations.



The fee structure as originally enacted has attracted much criticism, as it would have severely impacted on the cost of the administration of pension plans and also would have acted as a disincentive to the creation of pension plans in the future and indeed the maintenance of existing smaller plans. This proposal will be well received by all involved.

Since the purchase of an annuity is a costly undertaking, the proposal to allow for a drawdown account as an alternative is helpful, as it will allow the members on retirement to receive maximum benefits at reduced cost.

## International Business

The Minister has again noted the critical importance of the international business sector to the economic recovery and growth of Barbados.

He has identified key areas of focus for legislative changes deemed necessary to help grow the sector. These are to be addressed in conjunction with the Barbados International Business Association in the coming months and include the following:

- amendments to the Societies with Restricted Liability Act to allow for the amalgamation of such entities;
- the enactment of Foundation legislation;
- amendments to the Companies Act to allow for the incorporation of companies with Chinese names and English equivalents to attract more business from the Asian market;
- the enactment of Private Trust Company legislation to allow for the establishment of private trusts;
- amendments to the International Corporate and Trust Providers Act and the finalisation and laying of the relevant regulations.

The Minister has invited the relevant bodies to consider the establishment of a discounted multi-year licensing process for IBCs and ISRLs and has indicated a willingness to review the current level of Government licence fees.

## Comments

The Minister has again noted the importance of the sector. There is an outstanding issue of quantification of the direct and indirect impact of the sector to the economy. In his last budget presentation assurances were given that a mechanism would be developed to consistently measure its contribution and this remains an important goal.

The proposed Private Trust Company legislation will allow for the establishment of private trusts which do not handle third party funds, carry lower risk and as such may reasonably be subject to less strenuous reporting requirements. The enactment of Foundation legislation has the potential to allow Barbados to compete more readily with other territories that have already enacted such legislation and thus to attract further business from existing markets, such as Mexico. The proposed legislative changes are therefore aimed at allowing the sector to provide new or expanded services to existing and potential markets.

There remains room for clarification as to the resources to be made available for further development efforts, in particular as these relate to the negotiation of new treaties.

With respect to the overall operation and competitiveness of the sector, the Minister has provided a platform for discussion regarding attendant fees and greater flexibility in the licensing process. There remains a need to address other business facilitation issues important to the competitiveness and growth of the sector, such as streamlining of immigration and customs procedures.

## Agriculture

The following have been proposed for the agricultural sector:

- a rebate of up to \$5,000 to farmers who retrofit livestock housing using solar energy structures;
- the establishment of an Organic Matter programme with the provision of equipment as part of the Tractor Cultivation Scheme; and
- discussions on the recapitalisation of the Agricultural Development Fund. Once capitalised, interest rates on loans applicable under the fund will be reduced from 6.5% to 5% over the next three years.

## Comments

Any effective incentives granted to the agriculture sector will be well received as all acknowledge the important role of the sector and the need for Barbados to strive to reduce its food import bill, from both the perspectives of national food security and economic standpoint.

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## Culture

The Government is seeking to see Barbados “move from being a net importer to becoming a net exporter of cultural services to the World”. The Minister has voiced the Government’s intention to work with the industry to establish a public/private sector mechanism which will focus on promoting, marketing and distributing the products and services of cultural workers. Other measures proposed include:

- provision, by way of a Government backed guarantee, of a borrowing facility of \$50 million dollars in amounts of \$10 million every year for the next five years to support the promotional, marketing and distribution efforts outside Barbados of musicians, artists, designers and chefs;
- the support by the Ministry of Finance on a case by case basis for partial waivers of duties and VAT on some equipment required to upgrade music studios across the island, to be facilitated in collaboration with the Ministry of Culture and the Small Business Association; and
- the construction of a multipurpose, state of the art, Cultural and Performing Arts Centre, expected to be financed and constructed through a grant from the Government of the People’s Republic of China.

In addition, the Minister has called on all radio stations and networks in Barbados to commit to a policy of playing no less than 60% locally produced music on all stations in their networks.

## Comments

For a long time artistes in Barbados have been calling for more assistance from Government and other agencies to promote the various art forms. The proposals mentioned by the Minister will be appreciated by many Barbadian artistes. The Minister has not provided details on the borrowing facility and it is hoped that these will be available soon. No time line has been given for the construction of the performance centre. However, these measures should assist in the expansion of Barbadian cultural initiatives and generate much needed revenue. Looking back though, a new regime of incentives, concessions, credits and exemptions for cultural industries had been proposed in 2009 and to date we have seen no legislation enacted.

## Other

### High net worth individuals

The Barbados Income Tax Act permits an individual who is resident but not domiciled to claim a tax credit on income from foreign sources transferred to Barbados through the banking system of up to 93% (dependent upon the percentage of foreign currency to total earnings) of the tax otherwise payable on such foreign currency earnings in an income year. This translates to an effective tax rate of 2.45% for an individual whose income is solely from foreign sources.

It is proposed that a similar credit be made available effective income year 2012 to individuals who are both resident and domiciled in Barbados, in respect of income earned outside of Barbados.

### Penalties

With effect from income year 2011 the penalty for the late filing of tax returns will be increased from \$100 to \$500. The Minister has further indicated the need to impose more significant penalties on severe offences of failure to pay VAT and to file tax returns. His proposals to address these offences will be laid before Cabinet in the near future. This increased fee is aimed at encouraging the consistent filing of tax returns and payment of taxes due.

### Waivers

The Waiver of Interest and Penalty (“WIP”) Programme was extended last year with a view to allowing persons to minimize the cost of settling sums due and payable to Government agencies. The current programme offers a 50% waiver of outstanding penalties and interest where taxpayers settle these sums within a stipulated time frame, while remaining current on their obligations. The Minister has proposed that the programme, which is slated to end on December 31, 2011, be expanded to allow for a 100% waiver of interest and penalties on outstanding NIS, VAT or income tax payments due, provided that 80% of such sum is settled via a one-off cash payment.

This amnesty will also be available to individuals who have not filed personal income tax returns for any period prior to 2007, such that the 5% late fee on taxes payable will be waived, but the flat fee of \$500 will still be charged for each year of filing.

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### Professional fees

Paramedics, emergency medical technicians and emergency medical dispatchers who are subject to increased fees payable under the Professions, Trade and Business Registration Act, will now be treated in a manner similar to nurses and therefore pay the lower fee applicable to that category of medical personnel.

### Computers – import duties and VAT on parts

The importation of computer systems is exempt from taxation. In an effort to support and encourage the initiatives of local entrepreneurs in the area of computer system building and customisation, with effect as of September 1, 2011 all parts imported for the purpose of assembly of personal computers will also be free of all import duties.

### International securities market

The Minister has advised that definitive steps have been taken toward establishing an international trading floor for the listing and trading of offshore products. A Business Plan and a draft Memorandum of Understanding on the establishment of an International Securities Market have been submitted to the Ministry of Finance for consideration. It is felt that such a Market has the potential to further establish Barbados as an international business destination.

### Dematerialisation of Government paper

With effect as of January 1, 2012 the sale and trading in all Government paper will be conducted electronically. The present process of trading is deemed cumbersome and fails to facilitate a vibrant secondary market, as such the process of dematerialisation is aimed at making the trading process more efficient and providing new opportunities for investors.

### Housing

The Minister has proposed that Special Purpose Legislation and an appropriate Validation Order be used to address the issue of illegal extensions made by tenants of the NHC Estates. This legislation and Order will allow for the issuance of certificates of compliance by the Chief Town Planner and as such the finalisation of the relevant conveyances in favour of the relevant tenants. No extensions started after September 1, 2011 will be eligible for this programme and will therefore have to seek the full permission of the Chief Town Planner.

### Comments

The proposal to create an attractive tax environment for High Net Worth Individuals has the potential, along with related measures, to positively impact the level of foreign direct investment in this country.

All measures to increase tax compliance are welcomed, as unpaid taxes create a heavy burden on the country and on those taxpayers who routinely meet their commitments.

We eagerly await the proposed international securities exchange, as this has the potential to significantly broaden our market reach, by allowing Barbados to attract international business entities who wish to have the added benefit of having their securities listed. The listing of securities will allow issuers wider access to capital, whilst maintaining their status as international entities.

The other provisions will also be well received by those impacted. A more active secondary market for the trading of Government paper will be an important benefit from the move to electronic securities.



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