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Jamaica: *Budget 2016/17*

Balancing public expectations
with IMF commitments

12 May 2016

Kingston
Jamaica

Budget 2016/17

Introduction

The Hon. Audley Shaw, Minister of Finance & the Public Service laid the Government of Jamaica's (GoJ) 2016/17 Budget before Parliament today during what could be described as one of the most keenly awaited Budget Presentations for some years. This was the first Budget presented under the new JLP administration led by the Most. Hon. Andrew Holness, Prime Minister.



Brian J. Denning,
Tax Services Leader

The principal challenge for Minister Shaw this year is to achieve a most difficult balancing act. On the one hand, he has to manage strong public expectation based on a key pre-election promise to remove persons earning under J\$1.5m per annum from the income tax net. On the other hand, many (including a wide cross-section of the business community) have been fearful that this proposal is too costly to fully implement at this juncture and that it risks derailing the country's Programme with the International Monetary Fund (IMF).

To date Jamaica has passed all quarterly IMF tests under the current four-year Programme (which is set to end on 31 March 2017). It is widely felt that this prudent fiscal course has brought a level of stability and confidence to the economy and that any departure from same would generate significant uncertainty which could prove detrimental to Jamaica. The new administration has committed to maintaining the course along this disciplined fiscal path.

In keeping with recommendations from various quarters, the GoJ announced today that it would increase the tax-free threshold to J\$1.5m on a phased basis by 1 April 2017. Given the clear pre-election promise to do so, Minister Shaw had to deliver on this but the wider ramifications of this policy proposal have yet to emerge. As Jamaica increasingly shifts from direct taxes to indirect taxes, this latest proposal could precipitate a total abolition of personal income tax (PIT) in the event that the number of individuals remaining liable to income tax renders such a regime unsustainable.

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New Measures At a Glance

The table below highlights the new tax measures announced today in Parliament. A total **J\$13.78bn** in new taxes were announced (for FY 2016/17) to fund the initial phased increase in the tax-free threshold (of \$1,000,272) which is estimated to cost **J\$12.5bn** for FY 2016/17 (**J\$16.7bn** on an annualised basis). An increase of the tax-free threshold to J\$1.5m will cost in excess of **J\$31bn** on an annualised basis (excluding the increase in rate on incomes over J\$6m).

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New Tax Measures Announced	J\$bn	Click for Info
Increase in the Income Tax-Free Threshold to J\$1.5m on a phased basis	(12.50)	
30% income tax rate imposed on income in excess of J\$6 million per annum		
Increase in SCT on automotive fuels by J\$7 per litre	6.489	
Introduction of SCT on Liquefied Natural Gas (LNG) and revision of HFO rates	1.415	
Increase in SCT on certain tobacco products / substitutes – to \$14 per stick	0.574	
Increase in Departure Tax to US\$35 per person (from US\$14.53 approx.)	<u>5.300</u>	
Grand Total	<u>1.278</u>	

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Capital A & B – \$120.5bn

Other – \$54.9bn

Education – \$90.5bn

Nat. Security – \$55.7bn

Health – \$52.9bn

Finance (Other) – \$66.9bn

Debt Service – \$138.5bn

Petro Caribe – \$14.5bn

Loan Inflows – \$89.4bn

Capital Rev. – \$0.3bn

Grants – \$5.2bn

Bauxite Levy – \$2.8bn

Non-Tax – \$30.5bn

Tax – \$447.4bn

\$579.9 billion

\$590.1 billion*

* Additional J\$10bn to be used to settle upcoming debt repayment obligations



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Diving into the Detail (1)

We now examine each new revenue measure announced today in further detail:

Increase in Tax Threshold to J\$1.5m on a phased basis

The following table highlights the proposed phased increases in the income tax-free threshold over the next year:

Effective	Annual J\$	Monthly J\$	Monthly Benefit @ 25% J\$	Monthly Benefit Increase J\$
Current Threshold	592,800	49,400	12,350	-
From 1 July 2016	1,000,272	83,356	20,839	8,489
From 1 April 2017	1,500,096	125,008	31,252	10,413

As the increased tax-free thresholds will become effective during the calendar year, the annual tax-free thresholds for the Years of Assessment 2016 and 2017 shall therefore be \$796,536 and \$1,375,140 respectively.

The Minister estimates that the initial increase in the tax-free threshold to J\$1,000,272 per annum will take a further 74,035 persons out of the income tax net. We anticipate that the further increase in the threshold to J\$1,500,096 could take an additional 60,000+ out of the net.

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In his presentation, Minister Shaw explained that the increase in threshold was deemed necessary so as to partially combat the impact of inflation on the earnings of individuals. He cited that if one applied the effects of inflation since 1980 to the income tax threshold, which was \$7,500 at that time, the current level should equate to approximately \$1,362,000. The proposed \$1.5 million threshold therefore reflects an increase of just over 10% of that value.

PwC Commentary: *The increase in the tax-free threshold to J\$1.5 million per annum will have particularly positive implications for PAYE workers on lower incomes as their tax burden will be lifted and spread across the wider economy in the form of indirect taxes. The proposed policy has broader implications however, as the threshold increases will also significantly reduce the number of individuals who will contribute to income tax (perhaps to less than 110,000 persons in total).*

Data published by the Statistical Institute of Jamaica indicates that as at January 2016, Jamaica's Total Employed Labour Force stood at 1.163 million persons. This would suggest that 90% of Jamaica's Employed Labour Force will not contribute even J\$1 in income tax to the Consolidated Fund. In contrast, the remaining 10% will be required to carry the entire income tax burden with yet a further burden being placed on perhaps as few as 12,000 persons (due to increasing the rate to 30% on incomes above J\$6 million per annum).

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Unless compliance levels are increased dramatically and significantly greater numbers contribute to the income tax pot, the continued viability and practicality of maintaining a personal income tax (PIT) regime must be considered.

The increasing shift away from direct taxes toward indirect taxes may be viewed as a tacit recognition that PIT is not an effective form of taxation in the Jamaican environment. If so, then the big question to be addressed is whether PIT should be abolished entirely rather than maintaining a complex tax framework and administration to extract income tax (which by its nature should be broadly applied) from such a small subset of the overall population. Given that most public services are consumed by the majority of our population, the significant inequity of requiring the few to pay for the majority ought not to be ignored. Any abolition of PIT would need to be carefully evaluated in order to properly consider the full ramifications.

It is also noted that the Budget Presentation did not specifically address other payroll taxes (e.g. Education Tax, NHT/NIS/HEART contributions). Any comprehensive reform of the PIT regime ought in our view to encompass broader payroll tax reform which is long overdue. The need for such an evaluation is even greater in light of the current PIT proposal including consideration of the administrative utility of collecting only statutory contributions from so many or the inequity of making contributions if one cannot qualify for meaningful benefits under these programmes.

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Diving into the Detail (4)

New 30% Income Tax Rate on Incomes over \$6m

In an effort to mitigate some of the revenue loss expected from the phased increase in the income tax threshold, the GoJ intends to simultaneously introduce a 30% income tax rate to be applied to incomes in excess of J\$6m per annum. The current income tax rate is 25%.

The following table illustrates the monthly position for the next three Years of Assessment:

Monthly Income Taxed At:	2016 Jan.- Jun.	2016 Jul.-Dec.	2017 Jan. – Mar.	2017 Apr.- Dec.	2018 Jan.-Dec.
Threshold (@ 0%)	\$49,400	\$83,356	\$83,356	\$125,008	\$125,008
Next @ 25%	Balance	\$416,644	\$416,644	\$374,992	\$374,992
Balance @ 30%	n/a	Balance	Balance	Balance	Balance

For incomes marginally above J\$6m per annum, the benefit of the increased tax-free threshold will exceed the additional income tax chargeable at the 30% tax rate. When the threshold initially increases to J\$1,000,272 per annum, the additional monthly tax shelter from same will be fully clawed back at an annual income levels of approximately J\$8m while higher levels of income will bear a greater net income tax burden under this proposal.

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PwC Commentary: *The inevitable losers from this measure are those persons who earn significantly over \$6 million, notwithstanding that they will obtain some benefit from the proposed increase in the income tax threshold.*

When the J\$1.5m threshold takes full effect, an individual earning approximately \$10.5m per annum will have the additional tax shelter given by the increased threshold fully clawed back as a result of the higher marginal income tax rate of 30%. In an individual earning J\$15m per annum for example currently pays income tax of \$3,592,425 per annum (after NIS deductions) whereas his/her income tax payable will move to \$3,813,726 – an increase of \$221,301 per annum.

We are of the view that the proposed 30% income tax rate is a retrograde step. It is not in keeping with the general thrust of tax reform already implemented which seeks to broaden the tax base and reduce rates. In light of current compliance levels and the lack of contribution to income tax by 90% of the Total Employed Labour Force, it seems most inequitable to target a subset of perhaps less than 12,000 persons to pay a further 5% income tax on top of the multiple statutory contributions imposed on top of the current 25% income tax rate.

Given this inequity, it is also likely that some of these persons could take protective measures to reduce their exposure to this excessive taxation as was done in 2011 when the Government introduced a 35% income tax rate to be imposed on incomes over J\$10m. This policy did not achieve the tax revenues anticipated and it was subsequently withdrawn.

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Increase in SCT rate of J\$7 per litre on automotive fuels

Special Consumption Tax (SCT) on the importation or manufacture in Jamaica (i.e. refining) of automotive fuels will be increased by \$7.00 per litre with effect from **13 May 2016**.

The following table summarises the position:

	Gasoline – Unleaded 87	Gasoline – Unleaded 90	Automotive Diesel Oil (ADO)	Ultra Low Sulphur Diesel
Current – J\$ per litre *	25.1061	25.4792	24.4145	24.4145
Proposed – J\$ per litre	32.1061	32.4792	31.4145	31.4145

* Includes J\$2 SCT per litre which replaced cess previously charged by PCJ

PwC Commentary: We note that the Ministry Paper did not specifically address whether this increase will apply to Leaded Gasoline or Marine Diesel Oil. The GoJ is capitalising on current depressed oil prices to impose further SCT on gasoline. This will also trigger additional ad valorem SCT payable (levied at 10%) as this is imposed on the price inclusive of specific-rate SCT. The effect of this tax increase will be felt across the economy as it will increase the cost of public and private transportation as well as the haulage of goods.

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Introduction of SCT on Liquefied Natural Gas (LNG)

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At present LNG is liable to General Consumption Tax (GCT) at 16.5%. With effect from **13 May 2016**, the GoJ proposes to impose both a specific rate and *ad valorem* rate of Special Consumption Tax (SCT) on LNG of **\$4.56 per mmbtu²** [mmbtu = one million British Thermal Units (BTU)] and **3.5%** respectively. LNG shall become a prescribed petroleum product and therefore will become exempt from GCT.

In his presentation, Minister Shaw indicated that the introduction of this new tax regime (along with the changes to the tax imposed on HFO – see below) is designed to standardise the taxation of petroleum products competing with LNG. The proposed applicable rates for each fuel type are listed in the table below:

Fuel	GCT	Specific Rate SCT	Ad Valorem SCT
LNG	Exempt	\$4.56 per mmbtu ²	3.5%
HFO	Exempt	\$2.0006 per litre	0.395%
LPG (Propane)	Exempt	\$2.006 per litre	0.395%
Diesel	Exempt	J\$31.4145 per litre	10%

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PwC Commentary: Jamaica has actively sought to reduce its reliance on Diesel Oil to generate electricity. In this regard the Jamaica Public Service Company Limited (JPSCO) recently retrofitted its major power plant at Bogue in Saint James in order to enable it to use LNG as its primary fuel source. LNG is a cleaner and more cost effective fuel source than Diesel Oil. The proposed imposition of SCT on LNG in lieu of GCT may have a material adverse impact on the cost of LNG. At present GCT charged on LNG should be fully recoverable by an electricity generating company such as JPSCO as the supply of electricity is a taxable activity.

Where this GCT is replaced with SCT (both specific and ad valorem) this SCT would not be recoverable and therefore would increase the cost of LNG to JPSCO and other users of LNG. This additional cost would therefore have to be either absorbed by JPSCO or passed onto its customers in the form of higher electricity prices. Any increase in electricity prices could have a significant multiplier effect across the economy given the extensive consumption of electricity for industrial, commercial and residential use.

Revision of HFO SCT rates

At present Heavy Fuel Oil (HFO) attracts a specific SCT rate of **J\$0.1512** per litre. With effect from **13 May 2016** it is proposed to increase the specific rate of SCT to **J\$2.0006** per litre and also impose an *ad valorem* rate of SCT of **0.395%**.

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Increase of SCT on cigarettes etc. to J\$14 per stick

In keeping with the Government's commitment to reduce local tobacco consumption (in conformity with the *Framework Convention on Tobacco Control*), special consumption tax (SCT) is being increased on certain tobacco products.

Effective **13 May 2016**, the SCT on cigarettes, cigars, cigarillos, cheroots (including substitutes for these products) will be increased from J\$12 to J\$14 per stick. This increase will not apply to the supply of unbundled tobacco.

Retention of Junior Stock Exchange Incentive

In his Budget Presentation, Minister Shaw referred to his earlier announcement in April 2016 of his intention to restore the income tax incentive to companies that list on the Junior Stock Exchange. It is intended to restore this incentive in the format it was originally granted with effect from 1 April 2016 and to pass the necessary legislative amendments to this effect.

The incentive as originally enacted granted the following income tax relief (subject to certain conditions) to companies which listed on the Junior Stock Exchange:

- (a) Full income tax relief on profits earned in the first five years of listing (years 1-5);
- (b) Relief of 50% of the income tax payable in the following five years (years 6-10).

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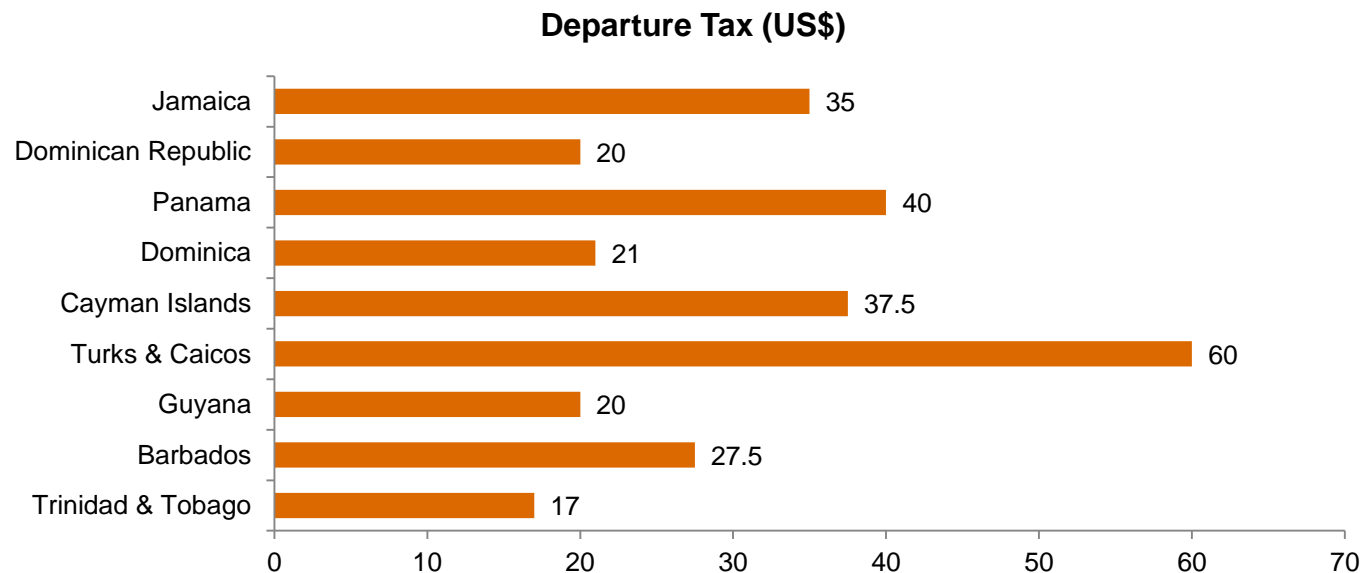
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Increase in Departure Tax to US\$35 per person

The GoJ proposes to increase departure tax to US\$35 with effect **1 June 2016**. The tax is presently levied in Jamaican dollars (equivalent to US\$14.53 at current rates). Going forward it is proposed to levy the departure tax in US\$. It is estimated that this increase will generate **J\$5.3bn** in FY 2016/17.

The following chart compares the proposed departure tax rate with rates imposed in selected Caribbean and Latin American jurisdictions:

Source: IATA





Let's Talk!

To discuss specifics on how the 2016/17 Budget measures will impact your business or for assistance on any other tax matter, please contact your local PwC contact or any of the Tax Services team listed here.

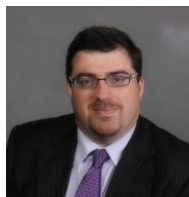
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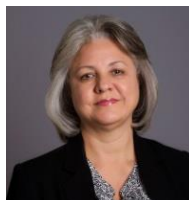
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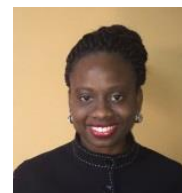
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