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2015 Budget Commentary – Under the Lens

June 15, 2015

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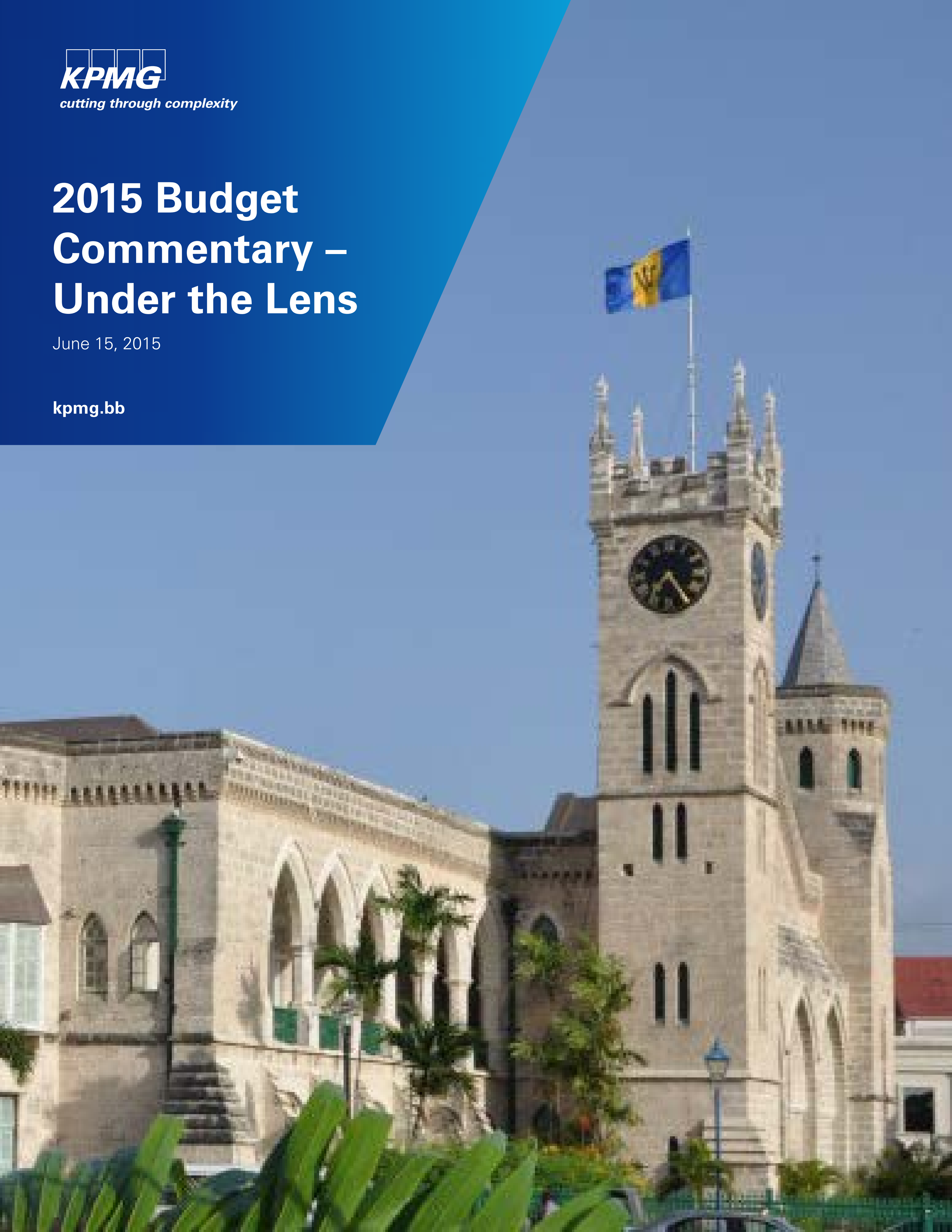

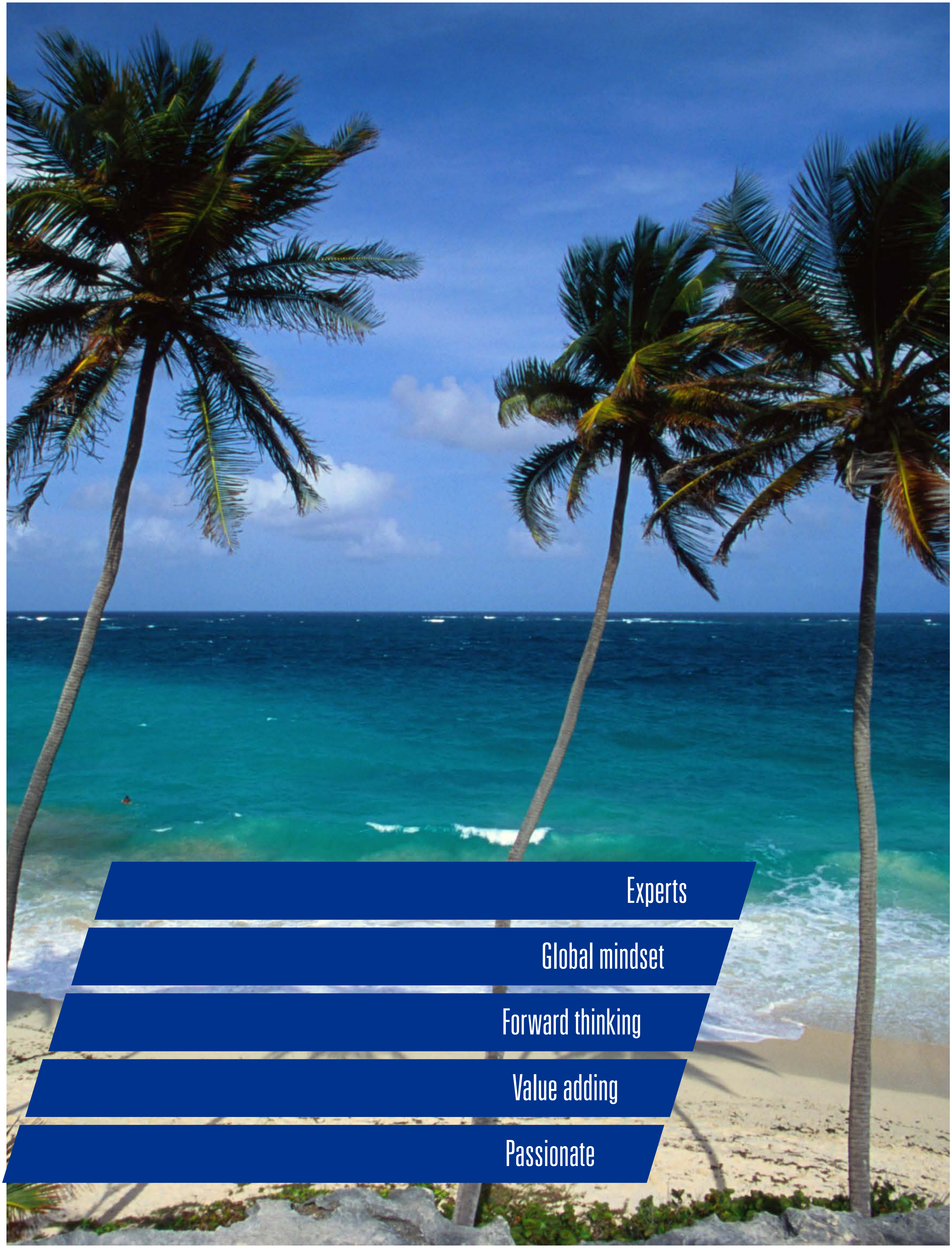
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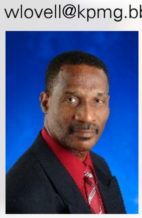

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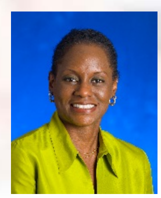


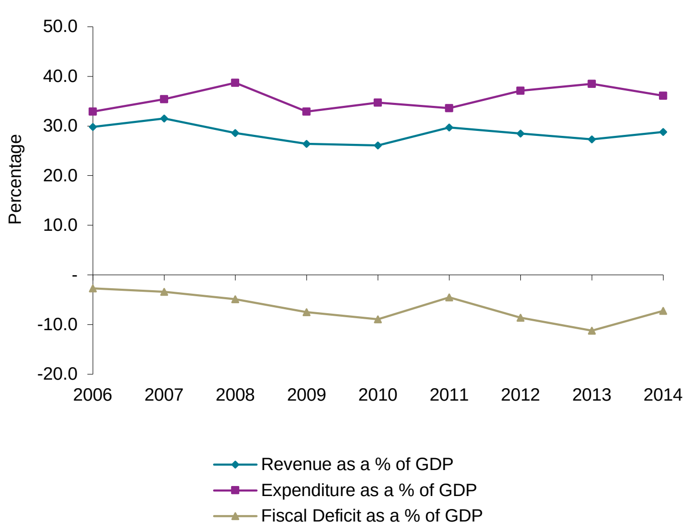
Executive Summary

- The Minister of Finance and Economic Affairs, the Honourable Christopher Sinckler delivered the much anticipated Government's Financial Statement and Budgetary Proposals on Monday June 15, 2015. The Minister declared to the country that the home grown economic stabilization and recovery plan which was devised right here in Barbados (the Barbados Programme) is working. The primary objectives of the 19 month adjustment programme were to:
  - Restore and stabilize the foreign exchange reserves so as to be able to protect our fixed exchange rate;
  - Reduce the fiscal deficit to sustainable levels; and
  - Lay the foundation for returning the Barbados economy to a sustainable growth path.
- These objectives are consistent with the Medium-Term Fiscal Strategy ("MTFS") 2010-2014 dated January 2010 the aim of which over the medium term was to:
  - Reduce the overall fiscal deficit and generate a balanced budget by 2014/15 and a surplus by 2015/16;
  - Keep economic growth to acceptable levels by focusing on the foreign exchange earning sectors; and
  - Ensure a reduction in the debt ratios to sustainable levels.
- The Minister noted that based on a comprehensive review by the Division of Economic Affairs as at March 31, 2015 as a result of the programme, the Barbados dollar is safe, the fiscal deficit has been cut by nearly half and is well on the way to more sustainable levels, and a tourism-led recovery in the Barbados economy is underway. The Minister also said that the empirical results, which will shortly be reported, will show that not only was the Government able to meet the overall fiscal target but they were also able to turn around a primary deficit of $385 million to a primary surplus of $85 million dollars in one fiscal year.
- Regarding Government Revenues the MTFS policy was to:
  - Improve efficiency of existing revenue collecting agencies;
  - Carry out a comprehensive review of the existing tax framework;
  - Return the tax base to its relative size.
- As these policies to drive economic growth take effect, it is expected that revenues would benefit from the increased economic activity. From the proposals it appears the Government is projecting revenues of $BD204.7 million from the improved efficiency per the MTFS and for tourism to be the leader of increased economic activity. In addition projected revenues are expected from the Energy sector via the aggressive facilitation of the build-out of an alternative energy sector. However, there appears to be no further commitment at this stage towards International Financial Services, Manufacturing or Agriculture.

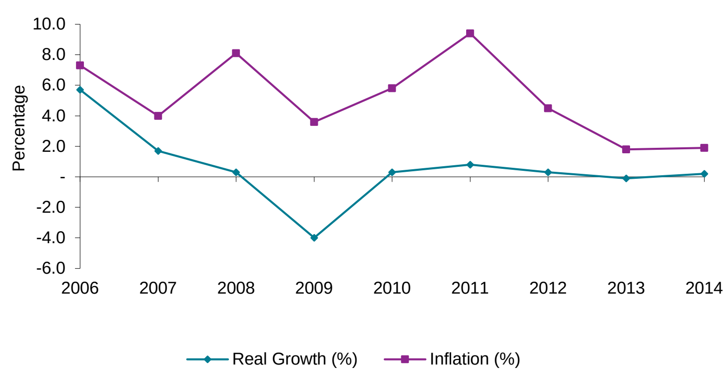
Economic Overview

- Preliminary information received from the Accountant General indicated that current revenue for the fiscal period ended March 31, 2015 increased by 6.9% from the amount recorded for the corresponding period during 2014. Current expenditure decreased by 6.9% from the 2013/2014 figure, and the deficit was reduced to 6.8% of GDP at market prices. Now that the foundation for returning the Barbados economy to a sustainable growth path has been established, and consistent with the MTFS, the Government plans to push forward its medium term economic agenda to:
  - Achieve continued stabilization and growth of the International Reserves;
  - Reinvigorate and deepen economic growth to a minimum annual average of between 2.5 to 3.5% of GDP;
  - Reduce the fiscal deficit to be at least no greater than the rate of GDP growth by the end of fiscal 2017, and nearly balanced budget by 2020;
  - Achieve a primary surplus of at least 4% by the end of fiscal 2018 and thereafter annually of about 5%;
  - Establish and achieve a medium term debt anchor that uses the above outcomes to stabilize debt growth by 2018 and start the process of reducing the debt to GDP ratio to a target below 100% in the next five years.
- Some of the measures to be adopted include but are not limited to:
  - Facilitating Economic Investment - Public/Private Sector;
  - Facilitating the cost and ease of doing business in Barbados: "One Stop Shop";
  - Introducing a Credit Bureau;
  - Launching a Competitiveness Commission; and
  - Continuing Legislative Reform.

Revenue, Expenditure and Fiscal Deficit as a % of GDP



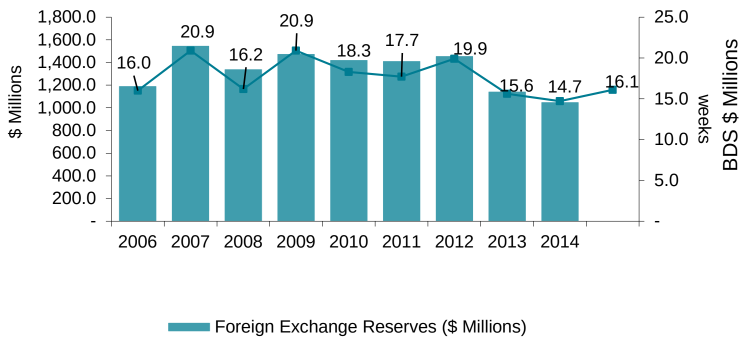
Real Growth and Inflation



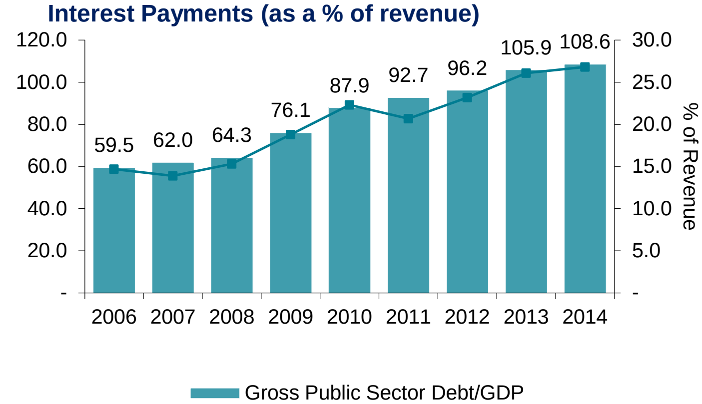
Source: Central Bank of Barbados Analysis of Barbados' Current Economic Performance March 2015
Source: Central Bank of Barbados Review of Economic Performance for the First Quarter of 2012, and KPMG Analysis

Economic Overview

Foreign Exchange Reserves and Cover



Gross Government Debt/ GDP and Government Interest Payments (as a % of revenue)



Economic Dashboard

	2006	2007	2008	2009	2010	2011	2012	2013	2014	Jan - Jun 2015 (p)
Economic Indicators										
Real Growth (%)	5.7	1.7	0.3	(4.0)	0.3	0.8	0.3	(0.1)	0.2	0.6
Inflation (%)	7.3	4.0	8.1	3.6	5.8	9.4	4.5	1.8	1.9	1.9
Foreign Exchange Reserves ($ Millions)	1,194.1	1,549.9	1,343.3	1,477.4	1,423.7	1,414.8	1,457.7	1,144.2	1,052.2	1,135.3
Foreign Exchange Reserves, cover weeks	16.0	20.9	16.2	20.9	18.3	17.7	19.9	15.6	14.7	16.1
Summary of Government Operations										
Revenue as a % of GDP	29.8	31.5	28.6	26.4	26.1	29.7	28.5	27.3	28.8	na
Expenditure as a % of GDP	32.9	35.4	38.7	32.9	34.7	33.6	37.1	38.5	36.1	na
Fiscal Deficit as a % of GDP	(2.7)	(3.4)	(4.9)	(7.5)	(8.9)	(4.5)	(8.6)	(11.2)	(7.2)	na
Public Debt										na
Gross Public Sector Debt/GDP	59.5	62.0	64.3	76.1	87.9	92.7	96.2	105.9	108.6	na
Government Interest Payments (as a % of revenue)	14.7	13.9	15.3	18.8	22.3	20.7	23.2	26.1	26.8	na

Source: Central Bank of Barbados Analysis of Barbados' Current Economic Performance March 2015
Source: Review of the economic performance for the First Quarter of 2012
Source: KPMG Analysis
Note: p - provisional
Note: na - not available

Budget Commentary

Key:
- Positive
- Negative
- Both Positive and Negative
- Neutral

Item	Commentary	Impact on Tax Payer
Corporate Taxation	**Key changes announced in the Budget** ■ Group Losses will no longer be allowed. Surrendering companies of a Group will no longer be allowed to offset the tax payable of its affiliated member. ■ The carry-forward period for tax losses will be reduced from nine years to seven years. **Our view** ■ This measure will have a negative impact on conglomerates and groups of companies and may also affect the financial viability of companies that are struggling financially. The emphasis appears to be on a perceived loss of tax revenues rather than maintaining economic activity through financial and employment initiatives which should lead to more tax revenues. This may be a retrograde measure which could result in inefficient taxation on a consolidated basis from group members. ■ Consideration could have been given to introducing from income year 2016. ■ If there was a perceived loss of revenue for companies with losses, a measure such as a payroll tax would have ensured that all companies pay some tax. **Summary of proposal** ■ May result in increased revenue for Government and a greater ability to forecast revenues, however for a developing country this may be deemed unattractive for investors. **Who is affected** ■ Conglomerates and affiliated companies. Companies whose nature of business may create losses. **Timing** ■ Effective income year 2015.	
Corporate Taxation	**Key changes announced in the Budget** ■ Deductions for contributions to special funds, etc. the applicable claim will be reduced from 150% or 120% where applicable to 100% respectively. **Our view** ■ While these expenditures were not incurred to produce assessable income of the company, the intention was to encourage private support of Funds for the benefit of enterprises. The claim of $48 million on expenditures of $32 million is on the assumption that all claims were at 150%. However, some of the contributions provided for a claim at 120%. This measure should result in additional tax revenue for government. The reduction of this deduction may result in a decrease in the amount entities contribute towards these funds. **Summary of proposal** ■ The special funds include The Arts & Sport Promotion Fund, The Regional Negotiating Fund, The Tourism Development Fund The Hotel Equity Fund The Enterprise Growth Fund and contributions in respect of Market Development. **Who is affected** ■ Entities who would have contributed to the various funds and the beneficiaries of such funds. **Timing** ■ From income year 2015.	

Budget Commentary

Item	Commentary	Impact on Tax Payer

Individual Taxation

Key changes announced in the Budget

- The following deductions will be allowed along with the existing personal allowances; contributions to trade unions and statutory associations, donations to charities including the church, and energy audit retrofits.
- Other special credits such as foreign currency earnings allowance and double taxation relief will also remain in keeping with Treaty arrangements.

Our view

- This measure will generate additional revenue for the government by reducing the number of allowances available to taxpayers. However it will also cause a decrease in the disposable income of individuals. The *"Ounce of Prevention"* tax credit on comprehensive annual medical examination introduced in the 2012 budget to encourage early detection and treatment of non-communicable diseases for persons over 40 years has been eliminated. The home (1996) and rental (2007) allowances, once thought to assist with the country's housing needs have been removed. It appears that the Government is seeking to eliminate refunds altogether.

Summary of proposal

- This measure sees the elimination of deductions for investments in venture capital funds, medical expenses and home improvements including mortgage interest and insurance. While maintaining the capacity to generate considerable revenue, this measure is restrictive in nature and contrary to measures and motives expressed in prior budgets. The summary speaks of a "one off" donation to charities including the church, while the speech and main text did not mention the "one off" item. Some clarification is required.

Who is affected

- Individuals who would have utilised these allowances including home owners and persons over 40 year old.

Timing

- Effective income year 2015.

Individual Taxation

Key changes announced in the Budget

- Current Income tax rate of 17.5% will be reduced to 16% and the higher marginal rate of 35% to 33.5%.

Our view

- The rate has been decreased to counter the elimination of allowances and deductions. It is intended to result in a reduction of the amount of tax refunds being processed. An analysis of the sample remuneration indicate that this measure along with the removal of the allowances is regressive.

Summary of Proposal

- The rate reduction should result in a reduction of approximately 60% of the current volume of tax refunds being processed.

Who is affected

- All individuals currently deriving taxable income.

Timing

- To be implemented for income year 2015.

Sample Tax Computations - Individual

Current				
Gross earnings		**$ 50,000**	**100,000**	**200,000**
Less:				
Statutory deduction		(25,000)	(25,000)	(25,000)
Two children		(2,000)	(2,000)	(2,000)
Home allowance		(10,000)	(10,000)	(10,000)
Total deductions		(37,000)	(37,000)	(37,000)
Taxable income		$ 13,000	63,000	163,000
Tax payable:				
First $35,000 @	17.5%	2,275	6,125	6,125
Over $35,000 @	35.0%	-	9,800	44,800
Annually		2,275	15,925	50,925
Monthly		190	1,327	4,244
Effective Tax		**4.6%**	**15.9%**	**25.5%**

Proposed				
Gross earnings		**$ 50,000**	**100,000**	**200,000**
Less:				
Statutory deduction		(25,000)	(25,000)	(25,000)
Two children		(2,000)	(2,000)	(2,000)
Home allowance		-	-	-
Total deductions		(27,000)	(27,000)	(27,000)
Taxable income		$ 23,000	73,000	173,000
Tax payable:				
First $35,000 @	16.0%	3,680	5,600	5,600
Over $35,000 @	33.5%	-	13,300	48,300
Annually		3,680	18,900	53,900
Monthly		307	1,575	4,492
Effective Tax		***7.4%***	***18.9%***	***27.0%***
Change in Effective Tax		***61.8%***	***18.7%***	***5.8%***

Budget Commentary

Item	Commentary	Impact on Tax Payer
VAT	**Key changes announced in the Budget** ■ All betting and gaming services and supplies which are currently exempted from VAT will be subject to VAT at the standard rate of 17.5%. **Our view** ■ This will generate additional revenue for the government in an area that was previously exempt from VAT however this may have a negative effect on the contributions available to the sporting and cultural bodies which these lotteries support. **Summary of proposal** ■ The proposal is an attempt to widen the VAT net, while reducing the number of exempt items **Who is affected** ■ Lottery, betting and gambling entities currently exempted from VAT. Possibly Associations benefitting from financial support. **Timing** ■ September 1, 2015.	
VAT	**Key changes announced in the Budget** ■ The VAT registration threshold requirement will be increased from the current level of $80,000 to $200,000. **Our view** ■ While reducing the tax compliance burden on both the taxpayer and the VAT Department, the measure is likely to increase VAT revenues while increasing the cost of inputs for small suppliers. ■ What about the VAT registrants who are currently below the $200,000 threshold? **Summary of proposal** ■ A previously suggested recommendation provides for a more efficient tax coverage which is in line with the establishment of the Barbados Revenue Authority. **Who is affected** ■ Small suppliers with significant input VAT who are unable to pass on the additional costs to consumers. **Timing** ■ Effective January 1, 2016.	
VAT	**Key changes announced in the Budget** ■ A new VAT basket of basic food items. ■ All other food items from the original VAT basket subject to the standard rate of the VAT of 17.5%. **Our view** ■ A reduction in the basket of basic food items creates a larger pool of taxable items on which VAT can be levied and reduces administrative efforts in determining taxable and zero rated items. ■ Measures to address the most vulnerable were not tabled. **Summary of proposal** ■ Increased revenue measure for government aimed at reducing the amount of foods classified as basic whilst eliminating from the basket of good, foods of little nutritional value and/or other foods out of the price reach of the most vulnerable. **Who is affected** ■ Everyone. **Timing** ■ Effective September 1, 2015.	

Budget Commentary

<table>
<tr><th>Item</th><th>Commentary</th><th>Impact on Tax Payer</th></tr>
<tr><td>Property Tax/ Land Tax</td><td>
Key changes announced in the Budget
The proposed new Land Tax structure effective 2015/2016:
<table>
<tr><th>Tax Year</th><th>Vacant Land</th><th>Non-Residential</th><th>Residential</th></tr>
<tr><td>2015-16</td><td>0.80%</td><td>0.70%</td><td>0.0% on First $150,000
0.1% on the next $300,000
0.45% on the next $550,000
0.75% on excess over $1,000,000</td></tr>
</table>
Our view
■ Rates have returned close to what they were before the 2012 land tax changes. With these new rates properties valued at $250,000 and $450,000 carry identical increases of $40. Also properties valued at $600,000 and $1,000,000 carry the same increases of $215
Summary of proposal
■ The measure while expected to yield $44 million is viewed as regressive.
Who is affected
■ Persons owning land.
Timing
■ Effective 2015 /2016
</td><td></td></tr>
<tr><td>Other</td><td>
Key changes announced in the Budget
■ Mobile airtime excise duty on cellular phones will be imposed at a nominal rate $0.03 per minute for both service providers LIME and Digicel.
Our view
■ The Government anticipates earning $32.7 million from this measure.
Summary of proposal
■ This mobile airtime excise duty on cellular phones will be used to fund the Scholarship and Grants Program to aid with the University of the West Indies tuition fees.
Who is affected
■ Cellular phone users.
Timing
■ Effective August 1, 2015.
</td><td></td></tr>
<tr><td>Other</td><td>
Key changes announced in the Budget
■ Individual professional operators provided for under the registration regime of the Profession, Trade, and Business Registration Act, will be eligible for reduced licence fee on production of a valid tax clearance certificate from the Barbados Revenue Authority in order to renew their respective licences to practice in this jurisdiction.
Our view
■ The increased regulation should provide for greater registration and quality control measures as well as ensuring that all funds owing to the government are paid.
Summary of proposal
■ Reduction in tax revenue from registrations estimated at $2 million.
Who is affected
■ Professional operators under the registration regime of the Profession, Trade, and Business Registration Act
Timing
■ Effective immediately.
</td><td></td></tr>
</table>

Budget Commentary

Item	Commentary	Impact on Tax Payer
Other	**Key changes announced in the Budget** ▪ New excise on Sweetened Beverages at rate of 10% levied on the value of the product before VAT is applied. Applies to imported and locally produced beverages. **Our view** ▪ A revenue generating tariff with a health component aimed at deterring the consumption of sweetened beverages such as soft drinks, juice drinks and other similar beverages. It excludes plain milk and evaporated milk which would be taxed separately below. An increase in tariffs on these while reducing consumption will likely be met with opposition from manufacturers and retailers of local soft drinks. **Summary of proposal** ▪ Aimed at shifting the behaviours of consumers, producers and importers of sweetened drinks to healthier alternatives. **Who is affected** ▪ Consumers, producers and suppliers of sweetened drinks **Timing** ▪ August 1, 2015.	
Other	**Key changes announced in the Budget** ▪ CESS on all milk and milk substitutes at 5% for milk products containing 60% or more of liquid fresh cow's milk and 10% for all other milks and milk substitutes to fund the subsidy/incentive provided to farmers. **Our view** ▪ This is an attempt to bolster the milk industry while reducing imports to the sector and saving foreign currency. **Summary of proposal** ▪ It is hoped that the measure will not affect local consumption. **Who is affected** ▪ Foreign milk importers and local milk producers and procurers. **Timing** ▪ Effective August 1, 2015.	
Other	**Key changes announced in the Budget** ▪ Establishment of a Scholarships and Grants Program to aid with University of the West Indies Tuition fees with $2,500,000 in the first year (2015/2016 academic year), $5,000,000 in the second year (2016/2017 academic year) and $7,500,000 in the third year (2017/2018 academic year) to reach $15,000,000 over the three-year period. To be eligible for partial tuition grants, persons must be students of the university and their household income must be $25,000 or less, or $45,000 or less if more than one person in the household is at university. Preference will be granted to applicants who withdrew from their studies for financial reasons. The initial proceeds are to be procured from the tax on mobile usage. **Our view** ▪ It is unclear how the Scholarships and Grants will be managed and students selected. **Summary of proposal** ▪ A measure to alleviate the burden felt by the students and their families due to the increase in tuition costs at the University of the West Indies. **Who is affected** ▪ University of the West Indies students and their families. **Timing** ▪ From academic year 2015/2016.	

Budget Commentary

Item	Commentary	Impact on Tax Payer
Other	**Key changes announced in the Budget** Proposed new Tipping fees: ■ Set at $40 per load for all categories of waste tipped at the Waste Treatment Facility inclusive of Municipal Solid Waste, Rock and Soil/Construction and Demolition Waste, Green Waste, Coconuts and; ■ Liquid waste delivered to be handled by the Sanitation Services Authority will also be charged at $40 a truck load. **Our view** ■ The removal of the Environmental Levy would have negatively impacted government's cash flows and therefore alternative means of revenue generation for solid waste management had to be introduced. It therefore seems that this fee in combination with the Municipal Solid Waste tax were created to fill that void in unison. **Summary of proposal** ■ This proposal would increase government revenue while also increasing the expense of haulers in depositing waste in the landfill. **Who is affected** ■ Waste haulers. **Timing** ■ Currently in force.	

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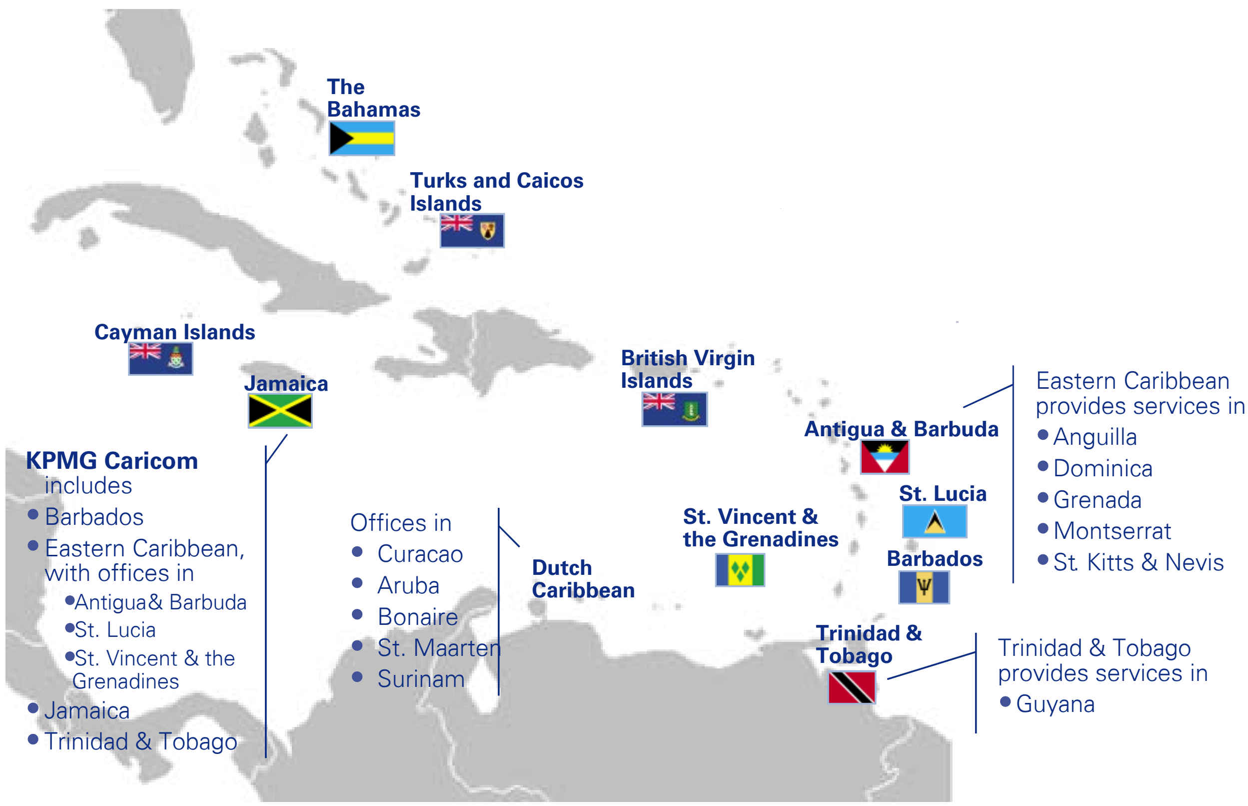

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