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Tax Newsflash

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KPMG in Jamaica

Foreword

It is with pleasure that we bring you this year's review of our country's budget.

As in previous years, we welcome your feedback on our bulletin. By its nature, this publication is meant to stimulate discussion and an exchange of ideas.

We thank our production team who made the timely issue of this bulletin possible, and we hope that you, our readers, find it useful.

Sincerely,

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Going for growth, no new taxes

Today, Dr. the Honourable Peter Phillips, Minister of Finance and Planning, presented what will become the first budget of Jamaica's next 50 years, and it seems to be a step in the right direction. He presented a budget that seeks to balance austerity measures with a growth agenda that, if executed well, offers hope.

The Minister emphatically announced that **there are no new taxes** in the budget. This was primarily because many of them were introduced in February in connection with the IMF conditionalities. A summary of the revenue measures announced in February can be viewed in our Tax Bulletin issued on February 12, 2013, www.kpmg.com.jm.

The Minister reiterated several initiatives that could change the tax landscape in Jamaica as we know it today. He previously mentioned them in the Fiscal Policy Paper, dated February 12, 2013. Based on these repeated references, it is expected that:
(a) discretionary waivers, other than for charitable organisations and for charitable purposes, will no longer be granted beyond a certain minimal threshold, except where it is required to satisfy the Government's contractual or legal obligations;
(b) rules affecting charities and charitable donations will be revamped (the Government will seek to harmonize the tax laws to address the treatment of charities as well as enact a Charities Act); and,
(c) an Omnibus Tax Incentive legislation will be tabled in Parliament, by September 2013, that will eliminate ministerial discretionary powers in the granting or validating of tax relief, and will put in place a transparent regime for tax incentives.

Growth Agenda

The Minister also presented several measures that comprise the "**Growth Agenda**." He talked about strategic investments that can change the country's economic landscape such as the logistics hub; a US$20 million investment by the Development Bank of Jamaica in new ICT centres (not including investments in the ICT sector by private businesses); nine Agro Parks; investments in general infrastructure such as roads and housing; energy cost reduction; public sector transformation; and tax reform.

He also went into some detail about integrated resort developments and implementing rules that were gazetted on Wednesday, April 17. He said that the law allows for three integrated resort developments, each with at least 2,000 new hotel rooms and casinos. He expects that the new resorts will create at least 30,000 new jobs as well as many construction jobs. The Government will start receiving proposals between June 1, 2013, and September 30, 2013, and a decision is expected to be made by early 2014.

Finally, he described micro and small enterprises as the backbone of the Jamaican economy and announced that the Development Bank of Jamaica will commit J$2 billion to the sector.

Constraints

On the austerity side, total expenditures have been reduced to approximately J$520.89 billion compared to J$602.53 billion in 2012/13. The bulk of the reduction comes from savings in debt repayment as a result of the National Debt Exchange (approximately J$91 billion). Allocations to most Government agencies also have been cut.

The largest component of the budget spend continues to be interest and amortization. Although reduced significantly from last year (from J$335.3 billion to J$225.24 billion), debt servicing still comprise 43.2% of the total expenditures.

The reduction in debt servicing is offset in part by the forecast increase in wages and salaries of public sector workers (from J$142.9 billion to J$160 billion which includes approximately J$17 billion for back wage agreements), which now comprise 30.7% of the budget. This means, in total, debt servicing and public sector wages continue to make up an inordinate percentage of total expenditures (73.9% this year versus 77.9% last year), leaving J$135.6 billion or 26.1% (versus J$136 billion/22.1% last year) to cover all other expenditures.

The silver lining in the significant reduction in debt amortization is that expenditures on capital projects will see a slight increase from approximately J$38 billion last year to J$44 billion in 2013/14.

The growth agenda coupled with the reduction in spending is good policy in these hard times, but there is little comfort that the way forward will be smooth.

Even as we stand on the cusp of a new IMF agreement with renewed hope, the numbers are not encouraging. At a macro level[1]:

- for the first nine months of the 2012 calendar year, real GDP declined by 0.3% when compared with the corresponding period of 2011.
- the October 2012 Labour Force Survey revealed an unemployment rate of 13.7%, 0.9 percentage points higher than the 12.8% reported for October 2011 (but 0.4 percentage points lower than the 14.1% reported for January 2012).
- the unemployment rate among youths was 35.3% in October 2012, 4.2 percentage points higher than the 31.1% reported for October 2011.
- inflation rates reported for the first three quarters of the 2012/13 fiscal year trended higher in comparison to the same periods in the previous fiscal year.
- the Jamaica dollar has been depreciating continually against the US$.

Looking Forward

The macro economic outlook for the next four fiscal years is brighter with forecast growth of 0.8%, 1.4%, 1.8% and 2.2%. These are not "hockey stick" forecasts by any means but, based on prior performance, they might as well be. For there to be any reasonable possibility of meeting the forecasts, Jamaicans will need to keep both eyes on the road and put "pedal to the metal" and not let up for a long time to come.

[1] *Source: Government of Jamaica's Fiscal Policy Paper FY 2012/13 dated February 12, 2013*

Revenue measures

There were **only two tax measures** announced by the Minister today. The Minister made it clear that these tax measures were part of the drive of the GOJ to:

(a) collect outstanding taxes; and

(b) remove inefficiencies and distortions in the tax system.

Tax Collection

During the fiscal year the Government will concentrate on collecting taxes already imposed.

Tax Collection efforts may bear significant fruit in this financial year as increased efforts by Tax Administration Jamaica (TAJ), coupled with the recent prohibition against the granting of discretionary waivers, (with certain exceptions), could see taxpayers being forced to pay up tax arrears.

The Tax Collection (Amendment) Act, 2013, passed in March 2013, allows the Minister to write off uncollectible tax arrears. However, the regulations to this legislation, which would, among other things, set out the criteria for determining a debt to be "uncollectible", is not yet drafted, therefore, the regime is not yet in operation. Even upon implementation, taxpayers' arrears would need to fit within the prescribed conditions to satisfy the test of being "uncollectible" before they are written off.

Taxpayers should expect to see increased issuance of notices of assessment, increased tax audits and increased publications by TAJ of the list of tax offenders.

TAJ may continue to use cross-checking facilities to locate and identify delinquent taxpayers. In this regard, TAJ, in the past, has announced that it would use public records such as the list of companies and businesses registered at the Companies Office of Jamaica, as well as the list of members of professional associations and the telephone directory to identify possible delinquent taxpayers.

Taxpayers have commonly failed to comply with tax requirements in relation to certain transactions. These failures, in our experience, include:

- *Not withholding tax on certain payments to non-residents;*

- *Employees not reporting other income (side jobs or businesses);*
- *Landlords failing to report rental income; and*
- *Business owners erroneously claiming personal expenses as business expenses.*

Non-compliance, perhaps, may be due to lack of knowledge of the tax laws or indifference on the part of the taxpayer. These failures may be "low-hanging fruits" for the TAJ and make easy tax collection targets.

The Tax Administration has traditionally struggled with the issue of taxpayer compliance. The widespread non-compliance of taxpayers is exacerbated by the Administration's apparent tentativeness in utilizing the full arsenal of tax enforcement measures available to it. However, the Minister has projected an increase in the collection of tax revenue for this fiscal year and has also emphasized the legislative reform that will unfold over the next four years. It is hoped that this legislative reform will place the appropriate emphasis on enhanced statutory powers that will ensure that the projected tax revenue is collected.

Removal of Inefficiencies and Distortions

GCT on Residential Electricity

With effect from July 1, 2013, the supply of electricity to all residential customers will be a zero-rated supply.

The Minister explained that the decision to move this service from an exempt supply to a zero-rated supply was made to honour the Government's commitment to the Jamaica Public Service Company Limited (JPSCo) that it would not increase the cost of supplying electricity and by extension would not increase the cost of electricity to JPSCo's customers. Currently, the GCT Regulations expressly exclude JPSCo from claiming GCT input tax credits in respect of its supply of electricity to any of its customers, even though the supply of electricity to commercial and industrial customers is taxable at standard rate. With this change, GCT input tax costs borne by JPSCo would now be recoverable from the Government instead of being passed on to residential consumers.

Based on the Minister's announcement JPSCo would not be able to claim all of its GCT input tax costs and would only recover those related to the supply of electricity to residential customers. This *may result in a reduction in the cost of electricity to those customers. Since the announced change relates only to residential customers, the lingering question is whether the GCT input tax costs incurred in respect of JPSCo's supply of electricity to its commercial and industrial customers are now recoverable.*

Customs Administration Fee (CAF)

On June 1, 2013, changes to the fee structure of the recently introduced CAF will be implemented.

These changes are aimed at addressing an identified inequity between the fees payable on imported finished goods and the fees payable on imported raw materials. It is believed that the import cost of raw materials should not be equivalent to the import cost of finished goods, since manufacturers will incur further costs in producing their finished goods. This distortion will be remedied by the implementation of a new fee structure, which would adequately take account of the difference in input costs for finished goods and raw materials.

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