

2018/19 Bermuda Budget Snapshot

February 22, 2018

“

This Government will continue to cultivate and grow the business side of Bermuda's economy. International business is the single largest contributor to economic activity in Bermuda. It is a partnership that has fuelled growth and expansion in this country.”

The Hon. E. David Burt, JP MP
Premier and Minister of Finance

“

Premier Burt's first budget provides some welcome tax relief to those with the lowest income levels, without increasing the overall payroll tax burden on employers. The Government remains committed to reducing Bermuda's national debt as a priority; in tandem with taking meaningful action to stimulate the economy such as through the inversion of the 60/40 rule. We look forward to further consultation with the Government, along with other key stakeholders, as Bermuda continues to explore alternative ways to broaden and diversify its tax base, and maintain our status as the leading jurisdiction for international business.”

Mike Morrison
CEO, KPMG in Bermuda

National Debt

 \$2.57bn
at March 31, 2018

rising to

\$2.66bn
by March 31, 2019

 \$89.7m
of new borrowing

 Annual debt service costs are estimated at
\$188.2m

Revenues

 4.6%
\$1.09bn

 Payroll taxes
\$454m
41.7% of revenue

 Customs duties
\$253m
21.6% of revenue

Expenditures

 1.4%
\$1.18bn

 Forecast capital expenditure of
\$62.2m

 Increased budgets for education, health, tourism and economic development


Growth and Technology

First technology incubator by July 2018

Initiatives to promote Bermuda as a jurisdiction for FinTech, Blockchain and Cyber security innovation


2017 GDP growth revised down to between


0.75% - 1.25%

 Revised height restrictions and relaxed condo ownership restrictions in the Hamilton EEZ

Payroll taxes

 Tax cuts for those earning less than
\$96k

 Deemed employees (business owners) taxed on a cash / income received basis

 No increase in other payroll tax rates

Contact us



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National debt



- Gross public debt will stand at \$2.57bn at March 31, 2018 is forecast to rise moderately to \$2.66bn by March 31, 2019;
- A new tranche of borrowing totaling \$89.7m will be required to finance the 2018/19 estimated budget deficit;
- Debt servicing costs are estimated at \$188.2m for 2018/19, a modest increase compared with \$186.1m in 2017/18; and
- 2018/19 is projected to be the final year of net debt increase. The overall budget deficit will not be eliminated until 2019/20 – this is one year later than the original target.

KPMG Opinion: *Bermuda continues to be faced with high debt. However, we are encouraged that the Government remains committed to reducing debt as a priority; this must be pursued in tandem with meaningful action to diversify the economy. Reducing the national debt is of paramount importance to maintain Bermuda's sovereign debt rating and to avoid further increases in debt servicing costs which would have a detrimental effect on the Government's capacity to fulfil its public spending commitments.*

Nonetheless, with a debt-to-GDP ratio hovering between 40%-45%, the Government is in a difficult situation and will be squeezed further if forecasted revenues / costs for 2018/19 prove to be overly optimistic.

The Government should continue its wide consultation with Bermuda's stakeholder groups with the Tax Reform Commission, to ensure that Bermuda's tax system meets the country's fiscal needs whilst ensuring that Bermuda remains an attractive and sustainable jurisdiction of choice for international business.

Revenues & expenditures



- ▲ Total revenue is forecast to rise by 4.6% (\$475m) to \$1.09bn in 2018/19;
- ▲ Revenue from payroll tax is estimated at \$454m or 41.7% of total revenues;
- ▲ Revenue from customs duties is estimated to be \$253m or 21.6% of total revenues;
- ▲ Total expenditure including debt service, capital expenditure and sinking fund contribution is estimated to be \$1.180bn for 2018/19, an increase of 1.4%;
- ▲ Operating expenses are projected at \$929.1m for 2018/19, an increase of 0.76% from 2017/18;
- ▲ Significant (16%) increase in the health budget, including restoration of \$25m subsidy for hospital care for children, seniors and the needy;
- ▲ Further growth in budgets for economic development and tourism (9%), public works (7%), and education (4%), offset by savings planned in transport and regulatory affairs and other Ministries;
- ▲ Interest on debt estimated to grow by 3.8% from 2017/18 to \$124m; and
- ▲ Capital expenditure in 2018/19 forecast at \$62.2m, an increase of \$1.8m on 2017/18 focused on schools, road works, IT projects and purchase of new buses.

KPMG Opinion: *The Government has focused on increasing revenues through a temporary increase in land tax for commercial properties and by closing the "notional salary" loophole by requiring "deemed employees" of owner-managed businesses to declare and pay tax on their cash drawings. There will be a margin increase in the cost of running the civil service with the Government opting to increase funding for education and workforce development, health, tourism and economic development in order to implement its growth strategy. There is more to be done in reforming public services to optimise efficiency and value for money.*

Payroll taxes



- The lowest employee band for payroll tax will be reduced from 4.75% to 4% resulting in a reduction in payroll tax payable for all workers earning less than \$96,000;
- For all deemed employees of owner-managed businesses, notional salaries will be replaced with a requirement to declare all income received, on a cash basis;
- Elimination of employer portion of payroll tax for all disabled employees;
- Certain new entrepreneurs to be exempt from all employer and employee payroll tax for the first year of business; and
- There will be new payroll tax provisions for taxi operators by implementing an annual charge of \$1,000 to be settled upon registration.

KPMG Opinion: *The Government has recognised the need to move away from payroll tax as its primary method of raising tax revenues. It is welcome that payroll tax for those in the lowest income bands has been further reduced and the additional increases proposed under "phase 2" of the previous Government's budget have not been implemented. The Government is looking at other ways of broadening Bermuda's tax base, and exploring ways to create incentives for companies to locate additional staff in Bermuda through payroll tax relief for new positions created.*

Foreign capital



- The long-standing 60/40 rule is proposed to be inverted to 40/60; only 40% Bermudian ownership will now be required for companies operating domestically;
- The Registrar of Companies has begun consultations on allowing global law firms to have a presence in Bermuda;
- The Ministry of Finance will consult on increasing the type of banks operating in Bermuda; and
- Revised height restrictions and relaxed condominium ownership restrictions for approved developments in the Hamilton Economic Empowerment Zone.

KPMG Opinion: *The inversion of the 60/40 rule is an encouraging development for foreign investors wishing to engage in business in the country. This shift should improve access to capital for Bermuda's small and medium-sized businesses; which should stimulate the kind of growth the Government is looking for.*

Other taxes and duties



- Proposed increase in customs duty on sugar content in foods, once the consultation period ends on March 1, 2018, offset by elimination of duty on certain healthy foods;
- Proposals to introduce a new Professional Service Tax (PST) have been abolished. The Corporate and Financial Services Taxes will remain in place;
- Lower duty rate on textiles; increased duty on tobacco and increased duty on wines by 30 cents per litre;
- A temporary 5% increase in land taxes on commercial properties to yield an additional \$15m in revenue;
- Increasing fees on cell phones as well as implementing a Government authorisation fee of 2.5% on the telecommunications industry; and
- Most other government fees will increase by 5%.

KPMG Opinion:

It was refreshing to see the Government take a collaborative approach in its pre-budget consultations and respond to feedback from key stakeholders. The Government should look at alternative ways to broaden and diversify Bermuda's tax base.

The Government should remain cautious of the impact that new taxes could have on the cost of doing business in Bermuda. Any move towards taxes based on consumption will need to be balanced with a reform of the current levels of customs duties.

Growth



- The 2017 GDP growth estimate has been revised down by 0.75% from 1.5%-2% to 0.75%-1.25% following seven years of economic contraction;
- The total number of filled positions was reported to have increased by a marginal 0.1%, or 40 jobs, primarily in the hospitality sector, to a total of 33,521. The official unemployment rate remains at 7%;
- Total visitor arrivals to Bermuda increased by 7.7% in 2017 - a 10.7% increase in air arrivals and a 5.1% increase in cruise passengers. Visitor spending rose by 20.3% to \$431m, and imports increased by 17.6% in the first three quarters of the year, primarily due to the America's Cup; and
- Total retail sales for 2017 increased by 2.9% (\$32.7m) while jobs in this sector rose by 0.7%.

KPMG Opinion:

The lowering of 2017's GDP estimate underscores the urgent need to stimulate and diversify the economy in order to drive growth. The Budget has largely avoided increasing the cost of employment whilst the proposed inversion of the 60/40 rule and incentives for job repatriation are likely to boost economic activity.

Major ongoing construction projects, the LF Wade Airport Terminal, Caroline Bay at Morgan's Point and at the St. Regis Hotel will add investment spending amounting to about 8.0% of GDP over the next three years.

While overseas demand for financial services will continue to drive export statistics, rising imports needed for major infrastructure projects will act as an offset and as a result, the current account surplus is likely to narrow. In addition, a tighter labour market and higher energy costs could exert upward pressure on inflation.

Technology



- The first technology incubator space will be operational by July. Discussions have begun on developing the world's first global risk management digital market on the island; and
- Bermuda is developing a legal framework and regulatory regime over blockchain-based technology.

KPMG Opinion: *Developing a third pillar to the Bermuda economy is a priority for the Government and the development of a technological hub for insurance, regtech and blockchain based technology is consistent with this strategic goal.*