

PricewaterhouseCoopers Bermuda's Review 2008 Bermuda Budget Statement

Social indulgences pay for social infrastructure

Government debt ceiling to increase to \$550 million

If you buy a pleasure boat, buy real estate, drive a car, travel, work, own a business or if you smoke... it will cost you more... In the Budget Statement presented today, the Honourable Finance Minister Paula Cox reported that "we must bear one another's burdens...".

Sinners

Taxes increased:

- Duty on cigarettes increased
- Duty on cars increased
- Vehicle licence fees increased
- Duty on pleasure boats increased
- Airport departure tax increased

Winners

Benefits shared:

- Free tuition at Bermuda College
- Free day care
- Free public transportation
- No-interest loans to first time home owners
- Reduced stamp duties
- Increased pensions

"As Government plans our country's finances for the next five years, equity and fairness will continue as the key principles underlying our tax policy in building the tax base to meet our commitments." ... "Government has sought to distribute the additional tax burden in a fair and equitable manner...."

It is worthwhile to note that there is a cost to enhance the Social Infrastructure, and despite additional tax burdens, as shared, there is further Government borrowing increasing Bermuda's National Debt from \$349 million to \$465 million. Each person's burden of the National Debt has increased from \$5,500 to \$7,500. While the Honourable Minister stated the Government's objective of promoting personal savings, the Budget Statement reported that to support the level of Government spending, the National Debt Ceiling will be raised from \$375 million to \$550 million. The Government has chosen to share the burden as follows:

Payers

Business

- Increase in company fees by 6.5%
- Increase in social insurance by 6.75%
- Increase in payroll tax by 0.5%

Real Estate

- Licence fees for sale of land to non-Bermudians to increase to 25% for houses; to 18% for condominiums
- Tax on fractional units set at 10%; second time sale fees to be set at 18%
- Higher stamp duty on sales of land in excess of \$1m

Recipients

- Employee portion of payroll tax to remain unchanged
- Lower payroll tax for small and medium businesses to remain unchanged
- Retail establishments to enjoy concessions
- Economic Empowerment Zones continue
- Lower stamp duty on sales of land to \$1m
- Customs duty relief for construction of affordable housing
- No changes to land tax

Impact on business

GDP growth is now expected to exceed the original estimate for 2007 by 0.5% and Government is cautiously optimistic that GDP for 2008 will be in the range of 2.5% and 3%, notwithstanding the global economic outlook.

The payroll tax rate increases by 0.5% for a business with an annual payroll of \$1 million or more and is to be fully borne by employers, although the salary cap remains at \$350,000. This increase is expected to yield an additional \$5.5 million in revenue.

Fees under The Companies Act 1981 are to increase by 6.5%, with effect from April 1, 2008, yielding an estimated \$2 million in revenue.

Travel costs will be affected by a \$10 increase in departure tax.

Social insurance contributions will increase by 6.75%, from \$56.96/week to \$60.80/week effective August 1, 2008.

On the plus side, Government will introduce a bill to provide concessions to retail establishments similar to those granted to hotels and restaurants for imported material and equipment used in renovation and refurbishment projects.

As in the last year, the Bermuda Small Business Development Corporation will receive another \$3 million to continue their work and the special rate of payroll tax of 4.75% for new business start-ups in the Economic Empowerment Zone will continue for another year.

What is unknown is how "luxury" type taxes, such as the increase in import duties on vehicles and boats will affect the related businesses.

Everyone is affected:

- No employee payroll tax increases
- Social insurance increase by 6.75% (approximately \$2 per week for the individual)
- 5% increase in pensions from August 2008
- Increase in airport departure taxes by 40% to \$35
- Lower stamp duty on house sales below \$1m (\$500 savings)
- Higher stamp duty on house sales above \$1m (1% increase for first \$500k over \$1m and another 1% for houses in excess of \$1.5 m)
- Higher priced boats (duty increase from 33.5% to 55%)
- Higher priced cars (\$1,500 more for cars with import costs over \$10,000)
- Increased duty on cigarettes (estimated at 50 cents per packet)
- No changes to land tax rates
- 3% increase in vehicle licences
- Free day care for children under 4 years (eligible families only)
- Free bus and ferry on a phased basis (Bermudians only)

The main tax effects

Sin taxes	<ul style="list-style-type: none"> ▪ Duty on cigarettes to be increased from 15.5 cents to 18 cents ▪ Duty on cars will remain at 75% and 150% but the threshold value separating tiered rates will be reduced from \$12k to \$10k ▪ Duty on motor boats and sailboats to increase from 33.5% to 55% ▪ Vehicle licenses to be increased by 3%, effective April 1, 2008. Retail establishments to enjoy concessions on materials imported for renovations and improvements
Payroll	<ul style="list-style-type: none"> ▪ Standard rate of payroll tax assessed on businesses with annual payrolls of \$1m and more and exempted companies to be raised from 13.5% to 14% (salary cap to remain at \$350k) ▪ 4.75% employee portion of payroll tax to remain unchanged
Business	<ul style="list-style-type: none"> ▪ Government seeking new sources of income in telecommunications sphere ▪ Lower rates of payroll tax for small and medium businesses (taxi drivers, farmers, fisherman) to remain unchanged ▪ Fee increases of approximately 6.5% under the Companies Act 1981, effective April 1, 2008
Real estate/ Construction	<ul style="list-style-type: none"> ▪ Customs duty relief to private sector developers for constructing affordable housing units ▪ Stamp duty on sales of land up to \$1m will attract a slightly lower stamp duty as the lowest band in the rate structure will be reduced from 2.5% to 2% ▪ Stamp duty on sales of land in excess of \$1m will attract a higher stamp duty as the top two bands in the rate structure will be increased by 1% each, to 6% and 7%, respectively ▪ No changes to land tax ▪ License fees for sale of land to non-Bermudians to increase from 22% to 25% for houses and from 15% to 18% for condominiums. ▪ First time sale fees on fractional units set at 10%; second time sale fees to be set at 18%
Retail	<ul style="list-style-type: none"> ▪ Retail establishments to enjoy concessions on materials imported for renovations and improvements ▪ Extension of period during which special payroll tax is available to businesses within the Economic Empowerment Zones from one year to two years
Seniors	<ul style="list-style-type: none"> ▪ Pensions and allowance governed by Contributory Pensions Act 1970 will increase by 5% effective August 2008 ▪ To finance the increase in pensions, Social Insurance contributions to increase by 6.75% with effect from August 2008
General	<ul style="list-style-type: none"> ▪ Government to commence negotiations with OECD countries and continue existing discussions with the European Union regarding tax legislation ▪ Old State House in St George's exempt from land tax because of its historical and cultural significance as a national treasure ▪ Returning students granted relief on customs tariff upon accompanied belongings ▪ Airport departure tax to be increased by \$10 to \$35

Social agenda

Affordable housing

- 500 interest free down payments to first time Bermudian home owners
- Duty relief to private sector developers constructing affordable housing
- No changes in land tax rates
- Rent geared-to-income programme for BHC tenants (25% of income with additional 10% compulsory savings)
- Putting good quality homes within reach of more Bermudian families

Seniors

- 5% pension increase from August 2008

Healthcare

- Establishment of urgent care centres in the East & West (development at Southside commenced)
- FutureCare programme to assist seniors without means to have insurance coverage
- Implementation of the National Drug Control Master Plan enabling courts to enforce drug treatment as a component of sentence

Students and education

- \$1m set aside to provide free education for students at Bermuda College with standard requirements in place to retain the benefit

- Relief from duty on accompanied belongings for returning students
- Accountability framework established for principals, teachers and students
- Academic performance standards implemented
- Review of national curriculum

Transport

- Free bus and ferry fares on a phased basis for Bermudians (no further information available)
- Increase in departure tax by \$10 to \$35
- Implementation of new Border Management system, introducing electronic manifests and elimination of the immigration passenger form for travelling Bermudians
- Continuation of development of new IT infrastructure at airport

Policing

- Development of new court and police complex in Hamilton
- Increase in police manpower

Environment

- Recycling campaign including continuation of Marsh Folly landfill site into green space, a nature reserve and recreation space

- Sea water reverse osmosis plant to become operational mid 2008
- Expansion of waste management facilities

Recreation

- Upgrade of Port Royal Golf Course continues
- Improvement projects for Bermuda's national parks (Fort St. Catherine, Paget Island and Ports Island)

Other social programs

- Encouragement of personal savings
- Free daycare initiative for qualifying families with children under 4 years old
- Expansion of the existing Economic Empowerment Zone to include eastern and western ends of the island
- Introduction of new variety of citrus into Bermuda with programmes to provide information about citrus culture
- Dog owners and breeders given greater freedom to choice in selecting dogs.

Economic overview

The Ministry of Finance anticipates GDP growth in the range of 2.5% to 3% at \$6 billion for fiscal 2008/09.

The revised estimate of total revenue for 2007/08 is \$929 million, which compared to the original estimate of \$917 million, represents an increase of approximately 1.3%. The projected total revenue for 2008/09 is \$985 million, which compared to the revised estimate for 2007/08 of \$929 million, represents an increase of approximately 6%.

The Government's current spending for fiscal 2008/09 of \$961.8 million is projected to increase by 6.5% over the revised 2007/08 estimate of \$903.5 million. The overall employment level barely grew in 2007, showing an increase of just 221 to 39,832, with financial services being the leading contributor.

Capital expenditures for fiscal 2008/09 amount to \$154.8 million bringing total current and capital expenditures for fiscal 2008/09 at \$1.1 billion. The current statutory debt ceiling is \$375 million and was last adjusted in 2005 based on a policy of having the statutory debt ceiling not exceed 10% of GDP. At the end of 2007/08, Bermuda's debt was \$349 million (before sinking fund).

With the 2008/09 budget, the Government intends to increase the country's borrowings to \$465.4 million (before sinking fund) and plans to adjust the statutory debt ceiling in 2008/09 to \$550 million. This would put the borrowing per capita at approximately \$7,500/person compared to approximately \$5,600/person in the prior year.

Tourism

Tourist arrivals in 2007/08 were up by 4%, leading to an increase in net foreign exchange earnings and increased visitor spending. However, passenger tax revenue is estimated to be \$4.5m lower than that budgeted for 2007/08. In 2008/09, passengers arriving at the airport will benefit from more efficient immigration processes as a result of investment in the technology infrastructure, funded by an increase in departure tax from \$25 to \$35.

Completion of the new cruise ship terminal for a further \$10m will enable the development of the Dockyard area into a first-class tourist destination and will also enable the redevelopment of the Hamilton and St. George's waterfronts. The budget statement is careful to note that the development of the second pier will not necessarily result in an increase in the number of cruise ship visitors.

Investment in facilities for tourist use such as Fort St. Catherine, various parks and Port Royal Golf Course will improve the tourism product, as will capital investment in remediation work at the former Club Med site and Morgan's Point.

Retail establishments will benefit from concessions on imported materials and equipment for renovation or refurbishment similar to those previously granted to hotels and restaurants. Social insurance and the standard rate of employer payroll taxes will both increase – the latter by 0.5%. Both of these measures will have an impact on companies in the tourism industry.

The Department of Tourism's budget for 2008/09 has been decreased by \$5m to \$35m.

Economic figures

The economic figures in this table have been adjusted to reflect actual figures for the prior years. Percent changes relate to original estimate. Please note that the Government now uses current market prices for GDP calculations.

Highlights of the 2008/2009 Budget:	07/08 Revised \$m	08/09 Estimate \$m	% Change
Revenues	929.1	985.3	6.0
Current Account Expenditures (Excluding Interest and Sinking Fund)	881.1	931.7	5.7
Capital Expenditures	143.1	154.9	8.2
Budget surplus / (Deficit)	(117.6)	(131.4)	11.8
Debts and Guarantees (Before Sinking Fund)	349.0	465.4	33.4
The economic figures in the table below have been adjusted to reflect actual figures for prior years			
	2006	2007	2008
Population (Estimate)	62,000	62,000	62,000
GDP (at constant market prices (1996), \$b) – ESTIMATED	4.4	4.6	4.7
GDP per Capital (\$)	70,968	74,196	75,806
% Change	5.4	3.0	2.5 - 3.0
	06/07	07/08	08/09
Current Account (\$m)			
Revenue	883.7	929.1	985.3
Expenditure (Excluding Interest and Sinking Fund)	836.1	881.1	931.7
Balance	47.6	48.0	53.6
Current Account Expenditure per Capita (\$)	13,485	14,211	15,027
% Change	18.0	5.4	5.7
Capital Expenditure (\$m)	108.4	143.1	154.9
Capital Expenditure per Capita (\$)	1,749	2,308	2,497
% Change	(6.0)	32.0	8.2

This briefing is intended as a general guide to the Budget 2008. It is not intended to be comprehensive and should not be used as a basis for decisions. For that purpose advice should be obtained which takes into account all the client's circumstances.

Every effort has been made to ensure the accuracy of the information contained herein. In view of its purpose the reader will appreciate that we, the Bermuda firm, are unable to accept liability for any errors or omissions which may arise.

% changes rates to revised estimate/actual as appropriate

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