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Tax Newsflash

May 25, 2012

KPMG in Jamaica

Foreword

It is with pleasure that we bring you this year's review of our country's revenue 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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Key messages

In order to increase the projected primary balance of $60.2 billion to $83.6 billion, the Minister of Finance and Planning outlined tax measures of $23.4 billion.

Tax measures of J$23.4B

A new per minute telecom termination tax has been imposed on both domestic and international calls terminating on Jamaican mobile and fixed line network.

New Telecom tax of $5.25 billion (net)

A transitional arrangement will be put in place for corporate income tax. The rate structure of this tax will see unregulated entities now paying 25% with all regulated entities paying current rates.

Income tax on unregulated companies 25% from 33⅓%

Financial institutions (FIs) will be required to pay an Assets Tax at the rate of 0.2% of gross assets less loan loss provisions.

A 0.2% Assets Tax on FIs

The GCT rate will be decreased from 17.5% to 16.5%, however, several previously exempt items will become taxable.

GCT decreased by 1%

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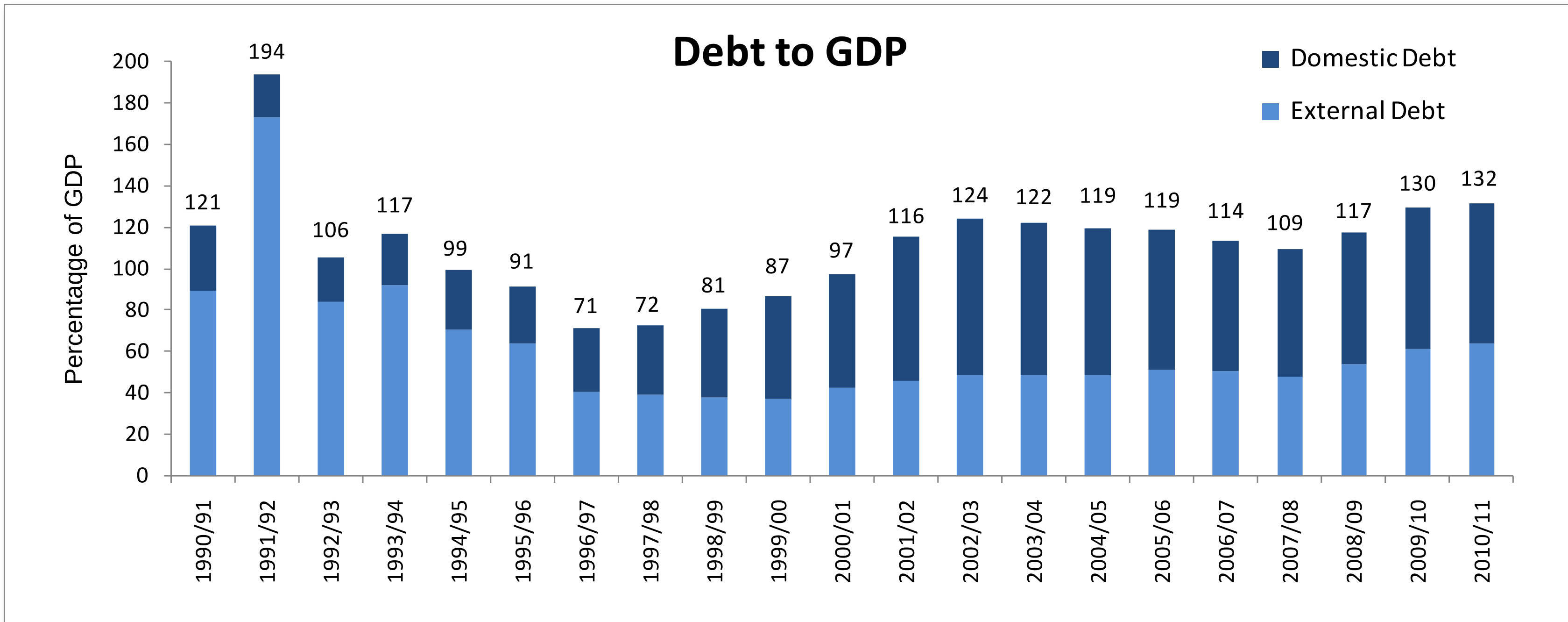
Economic Overview

Dr. the Honourable Peter Phillips, Minister of Finance and Planning, gave this year's budget presentation in the context of the global economy, where growth is projected to be approximately 3.2% for 2012.[1] Following three consecutive years of negative growth, real GDP grew in Jamaica by 1.3% in 2011/2012.

The economic concerns of high unemployment (12.8%), public sector deficit (7.3% of GDP), and the ratio of the debt to GDP (128% of GDP), remain (see table).



Source: Ministry of Finance and Planning, Debt Management Unit

[1] Jan Hatzius, Goldman Sachs' Chief Economist, Global Investment Research

For 2012/2013, the fragile economic growth is facing headwinds of concerns over increases in the banking system's non-performing loans, sluggish foreign direct investment, the risk of a collapse in the weakening Euro, and tensions in the Middle East which could lead to higher oil prices.

It is within this context that the IMF and the government agreed to a three pronged approach. "First, a growth-oriented environment aimed at improving productivity and competitiveness, while raising efficiency. Second, strong macroeconomic policies through significantly higher primary fiscal surpluses, fiscal and financial reforms, and further strengthening financial sector regulation and supervision. Third, a framework to ensure social cohesion."[2] The Minister of Finance and Planning's ("the Minister") budget presentation was primarily focused on the second of the three approaches through the proposed increase in revenue of $23.4 billion. There was an attempt at economic fairness through a $60,000 minimum tax on all registered companies, and an increase in the Personal Income Tax threshold.

[2] Statement by an IMF Mission to Jamaica, Press Release No. 12/100, March 22, 2012

We remain skeptical of the government's ability to raise this projected amount of revenue, given that revenues have been lower than budget for seven of the last eight years. In 2011/2012, the primary surplus was lower than the budgeted 5.2%.

The Minister presented the usual list of entities to be privatized such as Clarendon Alumina Partners, Wallenford Coffee Company, Caymanas Track Limited, Jamaica Railway Corporation and GOJ's interest in Windalco. There were a few surprises, including the proposed divestment of GOJ's shareholding in Jamaica Public Service Company Limited, and the removal of the Norman Manley International Airport from the list of proposed entities for divestment.

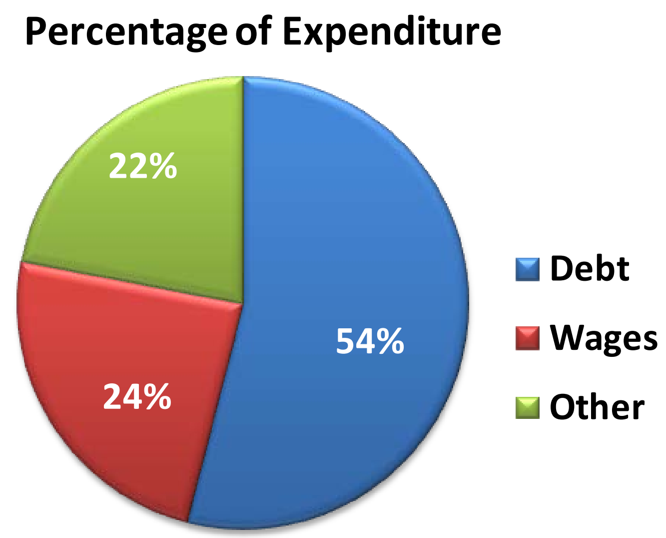
Jamaica has not yet, like much of the world, recovered from the global recession. Some economists project that real GDP is not projected to reach 2007 levels until sometime in 2013, while real per capita GDP won't fully recover until 2014. Further, full recovery in GDP is not projected to occur until 2017, almost 10 years after the recession commenced.[3] The policy response to

[3] Centre for Economic and Policy Research, Jamaica: Macroeconomic Policy, Debt and the IMF, May 2011

the reduction in real GDP has been less than innovative to date.

It is in this context that we welcome the prominence given to the use of public private partnerships ("PPPs" or "P3s"), as a vehicle to provide investment in necessary areas of infrastructure. As a firm, we have for several years suggested P3s as a means of stimulating economic activity, absent the strain of additional public debt, with more predictable recurrent expenditure. In particular, the use of PPPs in the areas of education, health care and transport is welcoming. It is our hope that these investments, along with investments in energy infrastructure, will generate much needed economic growth, and employment in the construction sector.

Given that debt and wages account for 78% of public expenditures, the government's strategy is to reduce wage expenditures through public sector pension reform and natural attrition. In closing, we recognise the limited "degrees of freedom" the MOFP had to craft this budget.



Source: Minister of Finance and Planning Presentation, May 24, 2012

Income Taxes

The anticipated White Paper on Tax Reform in Jamaica

The Minister announced that the Parliamentary Committee on Tax Reform has concluded its deliberations but its report has not been tabled in Parliament. Therefore, the anxiously anticipated White Paper on Tax Reform for Jamaica had not yet been finalised for presentation to Parliament. The Minister did indicate, however, that the tax reform measures would be tabled before Parliament closed for the summer break.

The Minister was pleased to announce that some 27 organisations, representing a wide cross-section of the Jamaican people, had responded to the invitation for formal submissions to be made to the Parliamentary Committee on tax reform, and had made presentations to the members of the Parliamentary Committee.

This is indeed heartening, in light of the recognition that the citizens of Jamaica "must be the main stakeholders in the development of a sustainable strategic taxation regime", and must be involved at the consultation stage of any tax reform programme. It should be noted that some of the short term measures proposed by the Private Sector Working Group ("the Working Group"), which included members of the Private Sector Organisation of Jamaica, the Jamaica Chamber of Commerce, the Jamaica Manufacturers Association, the Jamaica Exporters Association, the MSME Alliance, the Insurance Association of Jamaica, the Jamaica Bankers Association and the Jamaica Agro-Processors Association, have already been adopted and included in the Minister's budget presentation.

Change in the corporate income tax ("CIT") rate

Consistent with the novel recommendations of the Working Group, regulated entities such as financial institutions, securities dealers, general insurance companies, utility companies and telecommunications companies will continue to account for income tax on their tax adjusted profits and gains at the rate of 33⅓%. The Minister explained that regulated companies include all entities regulated by the Bank of Jamaica, the Financial Services Commission, the Ministry of Finance & Planning and the Office of Utilities Regulation. All unregulated companies will benefit from a rate reduction. They will account for income tax on their tax adjusted profits and gains at the rate of 25%. The new CIT rate will take effect on January 1, 2013, i.e. the commencement of year of assessment 2013.

Building societies will continue to pay income tax at the special rate of 30%, and life assurance companies will continue to pay income tax at the rate of 15% and a premium tax at the rate of 3%.

A reduction in the income tax rate was one of the proposals made in Green Paper No. 1/2011 on Tax Reform For Jamaica ("the Green Paper") tabled in May 2011. The Green Paper stated that the projected revenue impact of a reduction in the CIT rate to 25% was a revenue loss of $8.33 billion. The compromise of continuing to tax regulated entities at 33⅓%, which was recommended by the Working Group and adopted by the Minister, will result in a revenue loss of only $0.45 billion.

The submission made by the Working Group included a recommendation that the CIT rate of the regulated entities be gradually reduced over a period of 5 years. The Minister, however, did not state that this phased CIT rate reduction would be implemented.

Introduction of a minimum income tax

All registered companies (excluding charities, companies exempt from income tax under section 12 of the Income Tax Act such as approved educational institutions and companies in the first year of incorporation) will be required to pay a minimum income tax of $60,000 per annum, effective January 1, 2013. This flat tax is also applicable to self employed professionals such as lawyers, doctors and consultants.

This was one of the proposals put forward in the Green Paper for implementation in January of this year. A minimum business tax was proposed as a replacement for little trade licences and also possibly as a replacement for the assets tax. Based on the Green Paper, the minimum business tax proposed would have been payable, regardless of whether a loss was made. It is our understanding that this will apply to the minimum income tax. However, we would expect that the dividend withholding tax would be treated as a credit against the payment of the minimum income tax of $60,000.

Dividend withholding tax

The Minister announced the reimposition of a tax on dividends payable to residents at the rate of 5%. This 5% dividend withholding tax, which will take effect on June 1, 2012, is categorized in Ministry Paper No. 32/2012 as a final tax. Like all other withholding taxes, it must be deducted at source with the payer accounting to the Collector of Taxes for the amounts deducted.

The Working Group had been the only group recommending a reimposition of the tax on dividends paid by Jamaican companies to their Jamaican shareholders. The Minister adopted this recommendation, with a measure of compromise in relation to the applicable rate. A single rate, applicable to both corporate and individual shareholders, is also a change in the recent two tiered system of imposing a higher rate of tax for corporate taxpayers. This may be seen as a move towards bringing about the promised equity and simplicity in the tax system.

The Minister did not indicate whether this dividend withholding tax would be applicable to shareholders of companies listed on the Jamaica Stock Exchange. Since April 1, 2002, Jamaican shareholders of listed companies have received their dividends tax-free.

There is also some uncertainty as to whether the Personal Income Tax (PIT) threshold would apply to such dividends. We understand that the intention is that the PIT threshold should not apply to relieve such dividends from withholding tax. Therefore, a person in receipt of solely dividend income, which is below the current PIT threshold of $441,168 or as of January 1, 2013, the increased PIT threshold of $507,312 would still be subject to the 5% dividend withholding tax.

Increases in Assets Tax

It is proposed that, effective June 1, 2012, the Assets Tax regime will be modified as follows:

The filing date for the Declaration of Assets and the payment of the Assets Tax will move from September 1 to March 15.

This announcement raises the question as to whether companies will be relieved of the obligation to pay Assets Taxes for 2012 which would have been due by September 1, 2012. It is unlikely that the government will forego this tax in the current fiscal environment, therefore, we look forward to *receiving further details to clarify the implementation of this measure.*

Additionally, the convergence of the Income Tax and Assets Tax filing deadlines will put additional administrative and financial pressures on companies in the period approaching the March 15 deadline.

The proposed annual Assets Tax rate scale for non-financial institutions are:

Asset Value ($)	Proposed Annual Assets Tax ($)
Less than $50,000	$10,000
At least $50,000 but less than $500,000	$25,000
At least $500,000 but less than $5M	$50,000
At least $5M but less than $50M	$75,000
At least $50M	$100,000

This represents a significant increase over existing Asset Tax rates which range from a low of $1,000 (for asset values up to $50,000), to a high of $35,000 (for asset values exceeding $100,000,000). This move is a clear rejection of the recommendation by the Working Group for the removal of this tax which it referred to as a "nuisance tax".

The proposed annual Assets Tax rate scale for financial institutions and securities dealers governed by the Bank of Jamaica and the Financial Services Commission will be 0.2% of the asset value. The asset value for these purposes will be based on the total assets (including Guarantees/Letters of Credits). Loan loss provisions based on International Financial Reporting Standards (IFRS) and accounting prudence will be allowed as deductions in arriving at the asset value.

Effectively, the financial institutions and securities dealers will bear the brunt of this tax. Several commercial banks report assets valued in the billions of dollars in 2011. Where, for example, a bank has assets valued at $1,000,000,000 it will be liable to pay Assets Tax of $2,000,000. This far exceeds that payable by a non-financial institution whose asset tax is capped at $100,000.

The government's use of the Assets Tax regime may be an effective measure for increasing tax revenues as substantially all companies are subject to pay the tax. Further, the tax is not based on profit generation and so cannot be avoided due to the existence of tax losses as in the case of income tax, neither can the tax be mitigated by the use of credits as in the case of the GCT.

The Assets Tax is not applicable to the relatively few companies licensed by the Minister of Industry, Investment and Commerce to remove the word "Limited" from their names. These include charities and other entities established to promote commerce, science, art and religion.

The modified Assets Tax regime, along with the minimum tax imposed on registered companies, is expected to generate additional revenues of $1.95B for the government.

Consumption Taxes

General Consumption Tax

The following revenue measures are slated to take effect on June 1, 2012:

Rate

The Minister announced that there will be a 1 percentage point reduction in the GCT standard rate, which means that effective June 1, 2012 the rate will move from 17.5% to 16.5%.

This is expected to result in a reduction in revenue of $2.4 billion.

GCT on electricity

The GCT rate previously applicable on the consumption of electricity was 10% for both residential and commercial consumers with a monthly non-taxable threshold of 200 kWh for residential consumers.

It is proposed that the threshold be increased to 300 kWh for residential consumers. The GCT rate will be increased to 16.5% for all consumers. It is estimated that approximately 80,000 residential consumers will receive a tax break on their electricity bills as a result of the change.

The measure is expected to generate revenue of $0.43 billion. It is anticipated that certain government accounts will continue to enjoy exemption from the imposition of the GCT, such as schools, hospitals, clinics, government agencies and government offices. It is also expected that private institutions such as hospitals and schools will also continue to receive special waivers for the GCT on electricity.

Partially widening the GCT base

In an effort to widen the tax base and reduce the administrative issues, certain items previously listed as exempt will now be taxable at the standard rate.

The following items will now be taxable at the standard rate of 16.5%:

Tariff code	Item description
31.06	Raw foodstuff (excluding chicken)
31.07	Flavoured milk, milk based products, condensed milk and milk substitute
31.09	Corned beef (canned)
31.1	Pickled mackerel, herring, shad, dried salted fish
31.13	Buns, crackers (except water crackers), biscuits (salted and unsalted)
31.18	Eggs
31.19	All patties
31.2	Rolled oats
31.22	Live birds, fish, etc.
31.31	Syrup ex. Tariff 21.06
31.49	Animal feeds, pet food
31.51	Planting materials including cereals and seeds in their natural state, dormant flower bulbs, corns, roots and tubers, nursery stock, vegetable plants and live trees
31.58	Surgical gloves, including disposable, sterile and those made of latex rubber
31.65	Printed matter, articles and materials classified under tariff heading Nos. 49.01 and 49.05 (such as printed books, brochures, leaflets, maps and charts, etc.)

It is anticipated that this measure will generate revenues of $4.2 billion, thereby, nullifying the impact of the $2.4 billion reduction in revenues caused by the reduction in the GCT rate. It should be noted that the base has been widened to include agricultural produce, food items and educational material. However, exercise books and school bags remain exempt. It is anticipated that the GCT that will be applicable to books will significantly impact on parents' budgets for the new school year.

Special Consumption Tax ("SCT")

SCT on overproof rum

A single specific SCT will be reintroduced on overproof rum to replace the ad valorem rate currently in place. Overproof rum will attract SCT at the rate of $960 per litre of pure alcohol (L.P.A.), which brings it in line with the SCT currently payable on alcoholic beverages such as local and imported wines, cordials, liqueurs, vodka, whiskey, brandy and gin.

Similarly, the preferential ad valorem rate currently in place for the tourism sector will be replaced by a single specific SCT rate of $700 per litre of pure alcohol.

These measures will take effect on June 1, 2012.

Currently a 30% ad valorem SCT is imposed on overproof rum. The announced change runs counter to the recommendations of the rum industry, but is an attempt by the GOJ to bring about uniformity in the SCT regime on alcoholic beverages. The players in the rum industry have consistently advocated for a single rate ad valorem SCT, which they argue would give rise to a progressive SCT regime on alcoholic beverages, while the existing regime is a regressive one.

There appears to be a problem with using specific SCT amounts which are indexed in Jamaican dollars, in light of the frequent revisions that would need to be done in response to changes in the rate of inflation and rates of exchange. It is recommended that the specific SCT amounts should be set in US dollars.

Introduction of SCT on denatured ethanol

SCT at the rate of $16.32 per litre will be imposed on denatured ethanol used for the blending of petroleum products. This measure takes effect on June 1, 2012.

Denatured ethanol is an ingredient in blended petroleum products, which are blended by local suppliers of petroleum products. Ethanol imported in a denatured state, attracts no tax at the ports. The intention is to equalize the tax treatment of locally produced and imported denatured ethanol. The additional revenue of $0.54 billion, which is expected from this measure, will result from an increase in the price of petroleum products to all consumers of blended petroleum products.

Introduction of SCT on unprocessed tobacco

A specific SCT of $10.50 per 0.7 gram of unprocessed tobacco product (popularly referred to as "grabba") will be imposed with effect from June 1, 2012.

New Tourism Regime

It is proposed that effective September 1, 2012, the following two tax measures will impact the Tourism industry:

A specific GCT will be imposed on occupied rooms in hotels, villas, resort cottages/apartments and other similar tourist accommodation as follows:

No. of Rooms/ Hotel Size	Room Rate per Night (US$)
Less than 51	2.00
51 to less than 101	6.00
101 to less than 201	10.00
At least 201	12.00

Persons engaged in tourism activities will no longer be able to claim overseas travel agent and tour operator commissions and transportation expenses between hotel and airport, in computing their output tax for GCT purposes.

Tourism revenue remains subject to GCT at 10% and gratuities paid remain deductible in arriving at output tax for persons engaged in tourism activities.

In addition to tourist accommodation, other tourism activities that are likely to be affected by the removal of the deductions include the following activities carried on pursuant to a licence issued under the Tourist Board Act:

- *Camping sites and facilities;*
- *Water Sports;*
- *Tourist attractions;*
- *Tour operators.*

The present form of the GCT returns cannot accommodate the changes proposed. Presumably, the current GCT return form will be modified by September 1, 2012 to provide for reporting the special occupancy tax and to remove the deduction of the overseas commissions and transportation expenses.

Increase in the Personal Income Tax threshold

With effect from January 1, 2013, the annual personal income tax threshold will increase from the current $441,168 to $507,312.

An additional annual income tax exemption of $66,144 will be made available to individuals for 2013, which is a monthly increase in their tax-free income of $5,512.

As the Minister noted, the benefits presently afforded to employees in the hotel and tourism sector in the form of the tax-free gratuity will now be redundant. This benefit is only available to persons in receipt of a maximum annual income of $500,000, and so, currently, they benefit from an additional tax free amount of $58,832, over the existing PIT threshold of $441,168. With the proposed increase in the PIT threshold to $507,312, those employees will no longer derive a benefit from the tax-free gratuity scheme, as the increased threshold effectively affords them a greater tax-free benefit than would be available under the gratuity scheme.

Additional taxes on telecommunication services

With the reduction of the termination fee imposed by the Office of Utilities Regulation, it is proposed that, effective June 1, 2012, the following be imposed:

- J$0.30 per minute on all domestic calls for termination to a mobile network and fixed lines and
- US$0.075 per minute on all international calls for termination to a mobile network.

This appears to be a new tax type (e.g. not Income Tax or General Consumption Tax) and it is unclear how it will be administered and collected. This tax would add to the existing tax charge of 25% GCT on telephone services, including telephone cards and telephone instruments, and is likely to result in increased charges to customers.

Increase Common External Tariff (CET) on selected goods

It is proposed that, effective June 1, 2012, the CET on selected goods be increased by 10 percentage points.

The selected goods are those specified under List C of the Harmonization Tariff and may include:

- Motor vehicles;
- Motor vehicle spare parts;

- Jewellery (diamonds, wrist watches);
- Glass; and
- Alcohol (gin, vodka, liqueurs, cordial, etc).

The Minister indicated, however, that this measure will not be implemented for more than three years and would exclude the importation of buses, trucks and agricultural vehicles. He further indicated that the measure will not apply to motor vehicles with ratings of less than 2,000 cubic centimetres.

Increased motor vehicle registration and other licence fees

Effective June 1, 2012, there will be a 50% increase in fees:

- Annual motor vehicle licence fees applicable to all motor vehicles. Therefore a car with an engine capacity not exceeding 1199cc will have its annual fee moving from $5,125 to $7,700.
- Licence plate fees

Plate types	Current rates	New Rates
PP and CC plates	$1,500	$2,250
Motor cycle plates	$1,250	$1,875
Private plates	$1,500	$2,250
Trailers (private)	$1,500	$2,250
Substitute motor car plates (private)	$2,500	$3,750
Substitute motor cycle plates and trailer	$2,500	$3,750
Substitute PP/CC plates	$2,500	$3,750
Demonstration plates	$5,000	$7,500
Personalized plates	$20,000	$30,000

- Drivers' licence fees

Type of Licence	Current fee	New fee
General Driver's Licence	$4,000	$6,000
Motor Cycle Driver's Licence	$2,300	$3,450
Private Driver's Licence	$3,000	$4,500
Provisional Driver's Licence (1 year)	$1,000	$1,500
Substitute Driver's Licence	$2,300	$3,450

- Other motor vehicle related fees

Type of fee	Current fee	New fee
Application of title	$900	$1,350
Application for motor vehicle title (substitute)	$1,000	$1,500
Driver's licence examination fee	$1,800	$2,700
Motor vehicle certificate of fitness fee (Private motor vehicle/car)	$2,500	$3,750
Motor cycle fitness fee	$2,500	$3,750
Trailer and tractor fitness fee	$3,000	$4,500
Motor vehicle certificate of fitness fee PPV (L-Form)	$1,800	$2,700
Motor vehicle certificate of fitness fee – MV defects were remedied	$3,500	$5,250
Motor vehicle certificate of fitness fee – PP and CC	$3,000	$4,500
Substitute registration certificate / disc fee	$500	$750
Motor vehicle transfer fee	$500	$750

The proposed measures are expected to generate additional revenues of $0.60 billion.

It is assumed that fees referred to as "special permit" with a current rate of $3,000, as stated on the website of Tax Administration Jamaica, may have been inadvertently omitted from the list of increases above. It is believed that the new proposed fee for this category is, therefore, $4,500.

Restriction on discretionary waivers

Effective June 1, 2012, it is proposed that discretionary waivers be eliminated. This measure will include the following approaches:

- Cancellation of all blanket discretionary waivers;
- Give effect to the 2011 decision to eliminate the Modernization of Industry (MOI) waiver programme.
- All incentives which have not been in use for a number of years will be repealed in the 2012/13 financial year.

The MOI programme provided GCT exemption on the importation of capital goods for manufacturers involved in the export industry. Notwithstanding the proposed removal of this concession, manufacturers can still qualify for tax concessions under other regimes/facilities, e.g. the Export Industry Encouragement Act, Special Capital Allowances and the Jamaica Export Free Zone Act.

Other developing Revenue Measures:

The following measures are being contemplated by the government but no proposed effective date for implementation was announced:

- Removal of the stamp duty on the increase in the authorised share capital of a company. Stamp duty at 1% of the value of the increase is currently applicable.
- The Minister's announcement of the elimination of GCT on solar panels to encourage enterprises and householders to reduce their energy cost is in line with the Energy Minister's plans in encouraging investments in this area.
- The Minister introduced a proposal for a tax credit in respect of investments in the development of certain solar devices. Although he has not stated definitively how the tax credit would be applied and the effective date, he noted the government's readiness to offer tax credits to investors involved in the development of solar water heaters and photosensitive semiconductor devices.

Disclaimer

We must emphasize that the information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

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