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Global Tax Alert

Jamaica issues 2020/2021 Budget

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Executive summary

In his second Budget Speech before Parliament, Dr. the Honorable Nigel Clarke, Jamaica's Minister of Finance and the Public Service (the Minister) addressed the progress of the Jamaican economy and explained in detail how the country's improving debt profile has allowed his Government the fiscal ability to implement a second consecutive series of tax cuts, estimated to be in the region of J$18 billion for the 2020/2021 fiscal year.

For many years the country has confronted crippling debt, high inflation and macro-economic instability. However, through the efforts of two administrations, and cooperation from the public and private sector, the island has emerged from its 16th International Monetary Fund (IMF) program with many aspects of its macro-economic fundamentals showing marked improvement.

Minister Clarke was careful to credit the hard work and tremendous sacrifices of the Jamaican people for allowing the four pillars of macro-economic stability to evolve, namely:

Fiscal sustainability – debt is trending downward at 90.2% of gross domestic product (GDP) at the end of FY2019/20 and on pace to meet the targeted ceiling of 60% of GDP by FY2025/26.

External sustainability – Central Bank gross reserves of US$3.6 billion and non-borrowed reserves of US$2.5 billion are increasing allowing the ability to buffer uncontrollable external shocks.

Price stability – inflation remains within the Bank of Jamaica's 4% to 6% target range.

Financial stability – the banking system's loan loss reserves have been bolstered and the financial system is better capitalized.

Due to the island's improving macro-economic conditions, the Minister was able to highlight that the country's credit rating continues to be elevated in the view of international rating agencies and business confidence remains buoyant, thereby bolstering employment opportunities for the people of Jamaica.

Risks of external shocks persist and Jamaica, as a small island state, remains susceptible to natural disasters, and more imminently, the spread of the COVID-19 virus which was recently elevated by the World Health Organization (WHO) to the status of a global pandemic. These risks have been anticipated by the Government, which has responded by implementing a suite of financial-resilience instruments, including a contingent Inter-American Development Bank line of credit and a World Bank-backed catastrophe insurance bond. To combat the threat of the COVID-19 virus, the Minister has designated J$2 billion in advance investments targeted to the health sector and announcing a contingent J$7 billion arrangement to be accessed through Parliament, should the situation with the virus deteriorate.

Robust GDP growth remains elusive, falling below the Government's targeted rate of improvement. Although this was perhaps predictable in the past in view of the austerity measures placed upon the country, in the most recent fiscal year, Minister Clarke asserted that the down turn was primarily precipitated by unforeseen closures in the mining sector. Regardless of the cause, low growth, in tandem with high rates of criminal activity, remain a persistent threat to the sustainability of the Jamaican economy.

Faced with challenging circumstances, the Minister asserted that the Government chose to adopt a commercially-minded strategy of pursuing the strategic divestments of State assets. Minister Clarke described this program as a win-win. This assertion appears to be reasonable as the Government has so far implemented this strategy in a manner that has allowed it to:

- Raise much needed capital
- Reinvest the proceeds to reduce public debt by an estimated 3.3% of GDP by the end of the financial year
- Allow for wider public ownership of valuable commercial assets

It is important that the Government continues its investment program in capital items targeted at sustainably improving the physical, social, security and economic infrastructure. Capital expenditure of this nature, if properly executed, should lead to improvements in the quality of life of the Jamaican people. In a similar fashion, decisions taken to modernize the Public Service through the rationalization of public bodies and the reform of their compensation management and HR systems should, over time, assist these entities to become more efficient and ultimately improve the quality of services enjoyed by the public.

Importantly, the Minister should be recognized for taking the unprecedented step of lowering the tax burden over the past two years in a manner designed to remove impediments to business, lower the costs of transactions and public services and return money to the people of Jamaica. While any tax reduction is usually welcomed by taxpayers, it is hoped that the reduction in the standard rate of the General Consumption Tax (GCT) stimulates greater consumption, thereby creating additional stimulus for economic growth and countering the anticipated down-side economic impacts of the COVID-19 virus.

Detailed discussion

2019/20 Expenditure Budget

The FY2020/21 Budget proposes total net expenditure of J$853.5 billion, a decrease of J$5.6 billion on the planned expenditure for FY2019/20. The decreased expenditure is due to lower debt service for FY2020/21, as the non-debt expenditure is set to increase by 4.4%.

The total net expenditure of J$853.5 billion is comprised of:

Non-debt recurrent expenditure	**J$454.2 billion**
Capital expenditure	**J$74.2 billion**
Non-debt below-the-line expenditure	**J$37.3 billion**
Debt service expenditure	**J$287.8 billion**

The Minister announced the Government's intention to reduce the primary surplus to 5.4% of GDP. This is a marked shift in the higher targeted rate mandated under the IMF program. Minister Clarke pronounced that the reduction in the target rate would free up the necessary fiscal space to allow it to boost investment and consumption in a sustainable manner.

Overview of announced tax measures

The announced tax measures include:

- Decreasing the standard rate of GCT from 16.5% to 15%
- Reducing the Assets Tax payable by financial institutions to 0.125%
- Introducing a new income tax credit for companies (regulated and unregulated) with annual sales/revenue less than or equal to J$500 million
- Easing by 50% of regulatory fees payable to certain public institutions

Decrease in the standard rate of GCT from 16.5% to 15%

The Minister announced that with effect from 1 April 2020, the standard rate of GCT would be reduced from 16.5% to 15%. It is interesting to note that while the standard rate of GCT was reduced, other specific headline rates such as the 25% rate payable for telephone services, instruments and cards and the 10% rate payable for tourism services were not sequentially adjusted.

The GCT regime was introduced in October of 1991 and like other Caribbean territories, has become one of the major sources of tax revenues for the Government. The standard rate was last reduced in June of 2012, when it was adjusted downwards from 17.5% to the current rate of 16.5%. The headline rate alone (without due regard to the tax base), is not the sole determinant of the overall tax burden of indirect taxes such as GCT or value-added tax (VAT). Even so, the standard rate of GCT in Jamaica is among the highest in the region, significantly higher than the 12.5% standard VAT rates prevalent in Trinidad & Tobago and St. Lucia and is only surpassed by Barbados' standard rate of 17.5%.

In this context, the Minster prefaced the rate reduction with the factual observation that Jamaican's burden of taxation as a percentage of GDP is higher than the regional average. As such, the reduction in the headline rate, when considered in conjunction with the increase in the GCT threshold to J$10 billion per annum implemented in the prior fiscal year, does provide much needed relief to the Jamaican consumer, and is expected to incentivize all sectors through lower upfront costs and increased cash flow. As a result, it is hoped that this measure would have a counter-cyclical effect of bolstering much needed economic growth, especially in the event of a foreseeable down turn resulting from the possible spread of the COVID-19 virus.

The projected revenue loss from this measure is estimated to be J$13.968 billion.

Reduction in the Assets Tax payable by financial institutions

In the 2019/2020 Budget, the Minister abolished the Assets Tax on non-financial institutions citing its distortive effect and lack of equity in that it imposes a levy regardless of the profitability of an enterprise.

The Assets Tax continues to be payable at an ad valorem rate by specified regulated entities which are broadly defined as deposit taking entities regulated by the Bank of Jamaica and securities dealers and insurance companies regulated by the Financial Services Commission. This Assets Tax is not deductible for income tax purposes.

When the tax was introduced in 2012/13 it was levied at the rate of 0.14% but this rate was increased in 2014/15 to its current level of 0.25% of defined taxable assets. It is noteworthy that Barbados has a similar tax, based upon defined assets of certain financial institutions and set at the rate of 0.35%, but unlike the case with Jamaica, the tax is deductible for income tax purposes.

The Minister again acknowledged the inequity of the tax in that it is levied in a manner which is not aligned to the income generated by the defined taxable assets employed. He also recognized that it is a deterrent to financial institutions keeping financial assets and their related income generation within the Jamaican tax net. Moreover, the Minister incisively observed that although the tax is imposed on the specified regulated institutions, it is often passed on to consumers in the form of higher interest rates or other related financial costs.

Given these considerations, the Minister proposed a reduction in the rate of Assets Tax payable by financial institutions by 50% to 0.125% effective from year of assessment 2021 and undertook to monitor how the specified regulated institutions respond in terms of passing on resulting savings to consumers before determining whether subsequent reductions are warranted.

It is estimated that the revenue loss from this measure would be J$3.020 billion.

New Income tax credit for companies (regulated and unregulated) with annual sales/revenue less than or equal to J$500 million

The Minister proposed a tax credit amounting to J$375,000 for all companies with revenue/sales equal to or less than J$500 million with effect from the 2020 year of assessment. The credit is only available to incorporated taxpayers who file income tax returns and is stated to be targeted to continue to encourage the creation of micro, small and medium sized enterprises (MSMEs).

Minister Clarke pointed out that some of the targeted measures from the prior fiscal year such as the abolition of the Assets Tax on non-financial institutions, the removal of the minimum business tax, and the increase in the GCT threshold precipitated an increase in incorporations by 95% in the six-month period ended December 2019. Spurred on by this increase in new business activity, the Government was encouraged to go one step further to remove obstacles to starting new incorporated businesses by introducing the tax credit for MSMEs.

The measure is also designed to equalize the playing field between unincorporated businesses such as sole traders with incorporated businesses. This is due to the fact that sole traders are entitled to utilize the personal allowance of $J1,500,096 while the allowance is not available to incorporated businesses.

The Minister also specified that the tax credit could be used in conjunction with the Employment Tax Credit and that unutilized tax credits cannot be carried forward. The credit does open the possibility for abuse by taxpayers using multiple entities to take advantage of its provisions and so its implementation may increase the risk of tax avoidance.

It is estimated that the loss of revenue due to this measure is J$1.010 billion.

Easing of regulatory fees payable to certain public institutions

The Minister was prudent to recognize that along with taxation, regulatory fees also increase the cost of doing business. However, he pointed out that the genesis of such fees was credible in that they were aimed at allowing certain institutions to self-finance, thereby ensuring their independence from the central government.

Nevertheless, he concluded that the resulting increase in doing business for farmers and other impacted businesses outweighed independence considerations and determined that for institutions such as the Jamaican Agricultural and Commodities Regulatory Authority and the Trade Board Limited, it would be of benefit to impacted businesses to reduce these regulatory imposts by 50% and to supplement the resulting loss of income to these bodies with government subventions. The reduction of Trade Board Limited fees was not extended to importers of motor vehicles.

It is proposed that this measure would take effect from 1 April 2020, and it is estimated to cost J$300 million.

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