



**Government Finance Reforms in a  
Modern Bahamas**

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# Outline

- **The importance of public finance reforms**
- **VAT concepts**
- **Legal Professions / International services**
- **More on legislation**
- **Reform alternatives**
- **Some concluding comments**

**Why reforms are needed...**

**Staying in control of our destiny**

**A comprehensive approach to  
addressing the challenges**

# The comprehensive approach

- The entire public sector must control spending and become more efficient
- The system of concessions must become less generous
- Improve revenue performance (the \$500 million challenge)
  - Collect more of existing taxes
  - Identify new revenue

**Why VAT?**

# The Case for VAT

- Fits with broader program of reforms
- Broadens tax base
- Increases equity, especially in burden of fiscal adjustment
- Like a sales tax but with stronger enforcement mechanisms





**The mechanics and  
concepts.**

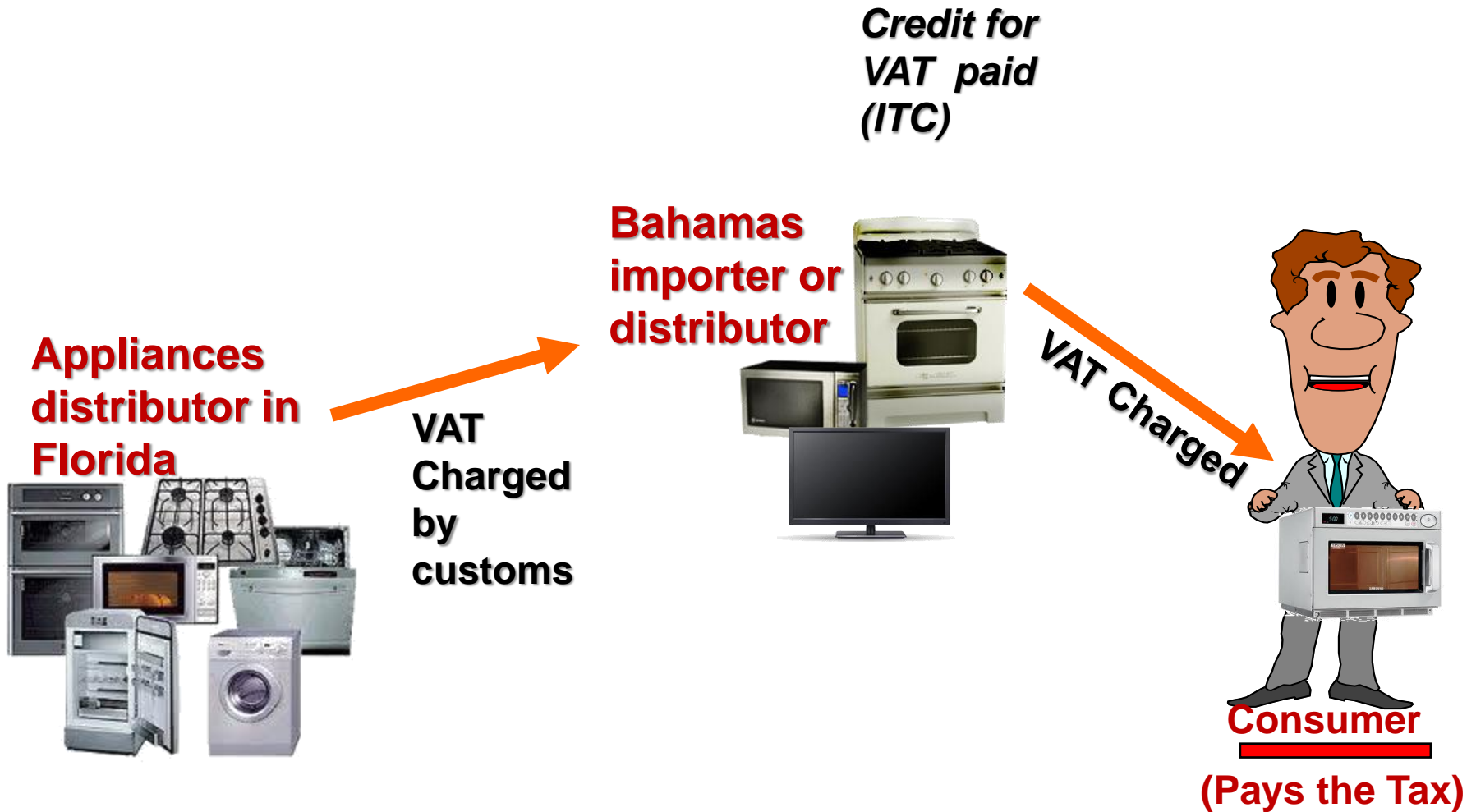
# What is VAT

*The value added tax or VAT is **the extra amount that would be added to the price of goods and services that you buy. It would be charged as a percentage, share or fraction of the price of the good or service. VAT would be collected from you by businesses and passed along to the government. Customs Department would also charge you VAT on items that you buy abroad.***

# Approach to VAT is one of rebalancing--**Plus**

- Customs duties would be substantially reduced
  - VAT would be simultaneously imposed on imports
- **PLUS....** The VAT would be charged on services
  - This would generate additional net revenue

# How would VAT work for goods?



# How would VAT work for services?

*Credit for  
VAT paid  
(ITC)*

## Business Inputs

- Data services
- Utilities
- Rent
- Contracted services
- Construction/improvements



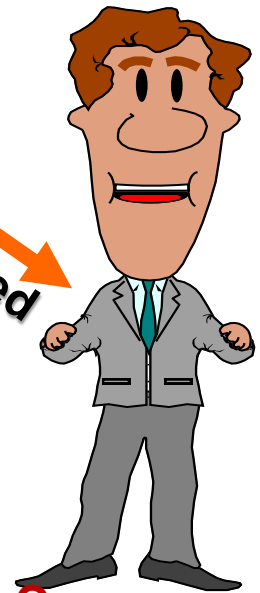
VAT  
Paid on  
goods  
and  
services

## Business Services

- Legal and accounting
- Corporate services
- Financial Advice
- Realty (sales and management)



VAT Charged



Consumer

(Pays the Tax)

# How would VAT work (example)?

- A legal practice has a monthly billings of \$250,000. About half of this is work for offshore or non-resident clients.
- The operations also incur monthly expenses on purchases of supplies, utilities and services of \$80,000.
- The practice earns a gross profit of \$170,000 that covers staff costs and, leaves some amount for profits and distribution to partners.

## How would VAT work (example)?

- VAT Calculations:

### Inputs:

- With the VAT at 15% the firm incurs total charges on inputs of \$12,000.

### Output/Supplies:

**Local billings pay VAT at standard rate (15%) offshore clients pay VAT at zero rate (0%).**

- Local billings of \$125,000 -- VAT charges of \$18,750 are collected from “Bahamian” customers.
- Foreign billings of \$125,000 -- No VAT collected from “non-resident” clients.

# How would VAT work?

## Payments and offsets

- VAT paid on operating costs: \$12,000
- VAT collected on sales: \$18,750
- VAT remitted to government
  - Collected from sales: \$18,750
  - Already paid (a credit) \$12,000
  - Remitted to CRA:  $\$18,750 - \$12,000 = \$6,750$



# VAT Concepts and terms

- VAT evolves around what is being sold or supplied, to whom it is being supplied and where it is being supplied.
  - Taxable supplies versus exempt supplies
  - Standard rate versus zero rated supplies
- Input taxes versus output taxes

# VAT Concepts and terms

- Registrant firm versus non-registrant
- VAT credits and refunds
- VAT invoices
- Apportionment or prorating of credits and refunds

# Legal Services by VAT Registrants

- Use and benefit of service can be inside or outside the Bahamas
  - Local consumption – standard VAT rate
  - Non-resident – VAT rate is 0%
- Operations would be entitled to credit on all VAT paid
  - Firms dominated by offshore business could be in a constant net refund position.

# Financial Services

- Financial Services broadly defined according to existing AML legislation
- Distinction between services supplied to domestic versus international market
- Exchange Control definition of non-resident, gives an Exchange Control definition of export.
  - Physically outside the Bahamas
  - Inside the Bahamas but not allowed to offer services to residents (offshore banks, IBCs, mutual funds and fund administrators)

# Domestic Financial Services

- Exempt
  - Lending and deposit – Interest payments
  - Foreign exchange transaction
  - All categories of insurance
- Taxable (banking/trust)
  - Legal fees on commercial and consumer loans; mortgages, etc..
  - All fees on services that do not attract stamp taxes: annual credit card fee, safety deposit box rental, credit references

# International Supply of Services

- Supplies are zero rated
  - Eligible for refunds of VAT on inputs
- Focus is on the end user (place of supply)
  - Non-resident companies (includes licensed offshore financial institutions, mutual funds and IBCs)
  - Non-resident persons
- **Note**: Legal services and commission on purchase of real estate transactions by non-Bahamians is VATable at standard rate.

# VAT Registration Criteria

- VATable supplies exceed the \$100,000 threshold
- Voluntary registration for smaller firms with good record keeping

# Other highlights in legislation

- When is VAT liability to be recognized
- Credit sales and bad debts
- Rules for payment of excess credits
- Unregistered but “taxable” persons



# Consumer protection and transparency and rights

- Only registered businesses can charge VAT
- Ability to verify registration status
- Price transparency
  - VAT paid must be shown on receipts
  - Receipts must indicate what is and is not VATable
  - Mechanism to separate VAT versus other impacts on price increases
- Publicized list of goods and services that exempt

# Suggested Alternatives....

- Reduce the size of Government
- Sales taxes
- Profit and Income taxes
- Payroll taxes

# Why Not A Sales Tax?

- The experience is same for end consumer
- Weaker self enforcement mechanism
- No ability to secure any portion of tax before final stages.
- The business is required to make an installment towards the final tax, which is paid by the consumer. This amount is returned to business later in the form of a credit.

# Why not use a lower rate of VAT?

- Fiscal reform is being driven by size of the correction.
- The Government must show a \$500 million improvement.

# **Why not other taxes: income, corporate, payroll...**

## Income tax

- Would have to apply for all persons above the poverty line (less than \$10,000 for Bahamas) or some other threshold
- Annual filing, but also ability to deduct from salary.

## **Why not other taxes: income, corporate, payroll...**

- **Payroll tax:** would be deducted from employee's paycheck similar to NIB contributions.
- With no change in customs duties could range between 9% and 12% of weekly wages or between \$110 to \$140 per month depending on revenue target and based on contributions on average wages of \$15,000 in 2012.
- With rebalancing of customs duties the rates increase to 20% to 25%. This is equal to a net take home pay that is \$2,300 to \$2,800 less per year.

# **Why not other taxes: income, corporate, payroll...**

- Reforms would have to apply fairly equitably across the economic landscape
- Large FDI projects negotiate exemption from future tax on profits
- Second home owners are attracted by freedom from income taxes
- Licensees of the Grand Bahama Port Authority are exempt from taxes

# Next Steps?

- Revised draft bill for Cabinet consideration incorporating feedback from stakeholders
- Recommendations on tariffs schedule
- Release of draft VAT Guidelines –general and specific (including):
  - Wholesale and Retail Trade
  - Financial Services
  - Professional Services
  - Transportation services
  - Hotels and Restaurants
  - Construction and Real Estate
  - Grand Bahama



**Summing up...**

# Conclusions

- VAT is one element in a broad agenda of fiscal reform
- Growth, employment and private sector interests should fare better

# Comments/Questions

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