

**Remarks for Bahamas Institute of Chartered Accountant's Tax Week**

**to be Delivered by the Minister of State for Finance the Hon. Michael Halkitis.**

**November 11, 2013**

***Topic: "The Need for Tax Reform: Broadening the Tax Base"***

It is an honor to be able to address you this morning during the Bahamas Institute of Chartered Accountants Week.

I must first begin by thanking the organizers of this event for the hard work and dedication they have put into ensuring that the topics discussed this week are relevant to the needs of our country's accounting professionals.

It is vital that our financial services professionals remain on the cutting edge of the industry so that The Bahamas continues to remain relevant in the context of both the Caribbean Region and the world at large. The Accounting industry is one of the few professions where continuing education is not only helpful but critical, and I must applaud

BICA for its dedication in working to ensure that Bahamian accountants are not left behind.

As we are all well aware, over the past year or so, there has been a lot of talk about the introduction of the Value-Added Tax in The Bahamas-on both the positive and potentially negative effects the implementation of this tax is likely to have on various sectors of the Bahamian economy.

The Government has been working tirelessly to ensure that all of the potential impacts of this tax are considered and that the net positive impact by far outweighs any negative impacts.

The Government has also been diligent in looking at ways it can make the transition to VAT as smooth as possible for all sectors of the economy to ensure that no group is forced to unfairly bear more of the burden of compliance. A key pillar of these efforts has been to ensure that all affected groups are equipped with all of the necessary information on exactly how the VAT will affect their industry and to

ensure that they are given the tools needed to effectively prepare themselves.

As we approach the July 1<sup>st</sup>, 2014 date for the implementation of the VAT, it is important that all affected groups are also educated on **why** this reform is needed in the first place; and what the potential effects would be of continuing down our current path. It is to that end that I would like to speak to you this morning-on understanding why the additional revenue provided by the reform of our current system is necessary at this point in our country's history. Additionally I would also like to speak to why the broadening of the tax base is so important in guaranteeing the stability of our economy going forward.

The Bahamas has always enjoyed a very liberal tax environment; characterized by the absence of key taxes upon which other major economies rely.

The most notable absences have been taxes on capital gains, corporate earnings, personal income, sales, inheritance, and dividends. This being the case, we have largely relied on a very narrow range of

revenue sources: principally customs duties, real property taxes and stamp duties. What this means is that our country continues to rely on very few revenue sources to finance a very wide range of public services. Furthermore, our current system is one where the burden of taxation falls on a relatively narrow base of goods and makes us particularly vulnerable to economic shocks.

While these revenue sources have been sufficient to sustain positive real growth in The Bahamian economy in decades past, the effects of the worldwide recession put enormous pressure on the Government to spur economic growth which put additional strain on our country's resources. This pressure necessitated increased borrowing to finance injections into our economy and resulted in a steady rise in our debt-to-GDP ratio. Stats

According to IMF predictions, if left unchecked the central government debt is projected reach 62 percent of GDP by Fiscal Year 2016/17. Adding the debt owed by non-financial public corporations the total public sector debt is projected to increase to about 76 percent of

GDP by Fiscal Year 2016/17. At those levels, and as a consequence, higher levels of public funds being directed towards debt servicing, significantly fewer resources would be available to finance critical investments needed for our country's economic growth. Such high debt levels have implications for the country's continued ability to adequately service that debt and negatively affects our ability to attract investment and to grow.

Reducing the debt ratio over the medium term is therefore an imperative for The Bahamas.

Furthermore, Revenue-to-GDP in The Bahamas is low by regional comparison and the tax base is narrow while the growth sectors of the economy—tourism and financial sectors—generate a small proportion of net revenue.

These two factors:

-rising debt-to-GDP and comparatively low revenue-to-GDP, have highlighted the critical need for a broadening of the tax base in The Bahamas. A core objective of tax policy must be to raise sufficient tax

revenues to finance public expenditure while maintaining sustainable public debt ratios.

Without attempting to reform the tax structure in The Bahamas there would be the real potential for an unchecked rise in the country's debt and a decreased flexibility to borrow in cases of emergencies—meaning increased vulnerability to shocks like hurricanes and sudden contractions in foreign economies on which we depend for tourists. Failure to raise revenues now has the potential to result in additional credit downgrades and eventual loss of access to credit markets. What this will inevitably mean for The Bahamas is a much higher tax increase, larger reductions in spending when the situation is eventually addressed.

Another important consideration when it comes to the need for tax reform is The Bahamas' upcoming accession into the World Trade Organization. Accession to the WTO will immediately compel The Bahamas to lower its average tariff rates to be consistent with other WTO members and to encourage global trade. While The Bahamas cannot afford in the long run to remain on the outside of such global

trade agreements, lowering the tariff rates without any attempt to raise revenues in other ways would significantly reduce our country's revenue. A shift in the way The Bahamas approaches taxes is therefore crucial in order to place our country in a strong economic position.

It is within this context and considering these eventualities that the Value Added Tax was introduced: with the aim of improving the country's fiscal stance and positioning The Bahamas' economy to be one of growth and opportunity going forward. Broadening the tax base will insure not only that our country has more revenue coming in, but spreading out the tax burden will allow us to tap into more sectors of the economy when demand falls in key revenue generating industries. This will improve The Bahamas' ability to weather economic shocks and to bounce back more quickly in times of recession.

The fact remains that in order to ensure economic growth and sustainability going forward, The Bahamas will need to diversify its sources of revenue collection. The most effective way this can be done is

by broadening the tax base to ensure that a wider cross section of the goods and services available within our economy are subject to taxation. At any given tax rate, a broad-based tax will raise more revenue than a narrow-based tax—simply because more is taxed. An additional, yet critical, consideration is that taxation is carried out in as uniform a way as possible for all players in the economy, with very few exemptions. What this adds up to is the need for a broad-based tax with a relatively low rate that is applied the same way to multiple sectors of the economy. All of these conditions are met with the Value Added Tax.

In summary, The Bahamas is at a very important junction in its economic history. We have come to the realization that while the current tax environment has worked to the benefit of our country in the past, if steps are not taken now to make the necessary adjustments to improve the efficiency of revenue collection, our fiscal stance will be significantly worsened in the very near future. We face debt levels cascading to unsustainable levels, credit ratings downgrades, and the need for much severe tax increases and reductions in spending if we do



not act now to reverse the trend. When considering these options, it has become clear that broadening the tax base to allow more sections of the economy to be taxed at a low and consistent rate is the most prudent course of action.

I wish you successful deliberations and thank you for the role that you are playing in education the business community and the public about these important and necessary reforms underway.

Thank You.