



Focus on Barbados Budget

2009

Barbados economic proposals 2009

The Barbados Economic Proposals 2009 are based on the Economic Policy Statement delivered by the Prime Minister and Minister of Finance, the Right Hon. David Thompson, M.P., in the House of Assembly on Monday 18 May 2009.

This review and the articles have been prepared by Ernst & Young and is intended for the information of our clients and associates.

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18 May 2009



Executive summary and commentary

Focus on Barbados Budget

May 2009

The Honourable David Thompson, Prime Minister and Minister of Finance, presented his 2009 Financial Statement and Budgetary Proposals on Monday, 18 May 2009.

The Prime Minister called on Barbados to get on-board with the “Team Barbados” initiative to unite the island’s best minds and brains to tackle the social and economic issues currently facing the country. He also noted that more advanced economies have not been able to prevent and/or eliminate the symptoms of the global credit crisis.

The Prime Minister’s preamble focused on the economic upheaval of the major economies of the world and the relative performance of the Barbados economy. Emphasis was placed on the fact that global gross domestic product (GDP) has decreased on an annualised basis by 6.25% in the fourth quarter of 2008, a swing of 10.25% from the 4% growth one year earlier.

In his review of the Barbados economy, the Prime Minister reiterated the figures identified in the 2009 First Quarter Review of the Economy presented by the Central Bank. The fall in GDP by 2.8% in Q1 2009 was accounted for primarily by a decline in tourism which in turn led to reductions in overall traded sector output and to a fall-off in the activity of related non-traded sectors.

Executive summary cont'd

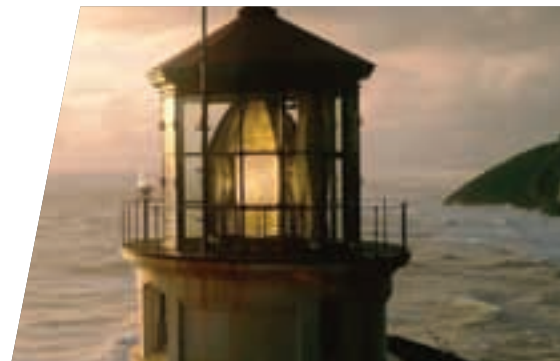


The measures in the Budget again placed a heavy emphasis on social issues. At the heart of the Budget was a call to “Team Barbados” to make sure that the social safety net is sufficiently strong and flexible to meet the demands of our people. The biggest challenges addressed were those of jobs, training, health and housing. The measures aimed at addressing these challenges included the following:

- ▶ As an incentive to provide job security, the Prime Minister has offered employers facing cash flow problems a one-year deferral of employer contributions to the National Insurance Scheme, along with waivers of penalties and interest. This initiative is focused on encouraging employers to maintain current employment levels rather than placing the financial burden of job losses on the Unemployment Fund.
- ▶ The National Insurance Board has approved a suite of courses available to unemployed individuals to facilitate re-training and a fund of \$10 million has been established for this initiative.
- ▶ The National Housing Corporation (NHC) has resumed its task of providing housing via rental, loans and sales. NHC has identified five areas where it will build 103 units over the next year at a cost of \$23.8 million. Additionally, NHC proposes to develop another 37 acres of land at an unidentified cost.
- ▶ The Prime Minister proposed that a Special Purpose Vehicle be established to deal with the designing, financing and renovating of the existing hospital, or to consider a new hospital under the project management of the Ministry of Health. No estimates of cost were provided for this venture.

Standard & Poor’s in its April 2009 Report maintained its BBB+ rating for Barbados, but has downgraded the outlook from stable to negative. Moody’s Investors Service has not completed its rating, but has placed Barbados Government Bond ratings on watch for a possible downgrade due to increased Government borrowing. Rating downgrades adversely impact the country’s ability to borrow as Barbados Government Bonds may no longer qualify for inclusion in investment portfolios.

Executive summary cont'd



The Prime Minister announced that a Memorandum of Understanding has been entered into with CLICO Holdings (Barbados) (“CLICO”). The sale of CLICO’s financial subsidiaries has now been placed in the hands of an oversight committee comprising of six persons, four appointed by Government and two by CLICO. The appointment of this committee demonstrates Government’s commitment to protecting the interest of policyholders and depositors.

The actual fiscal deficit for the financial year 2007-08 was 3.7% compared to an estimated deficit for 2008-09 of 5.1%. Government has adopted the position that foreign borrowing supported by achievement of greater efficiency and the elimination of waste in the public sector will be the strategy for stabilizing the economy. If greater reliance has to be placed on foreign borrowing, this will result in increased foreign debt which has to be serviced and repaid from foreign currency earnings. The challenge will be to grow foreign currency earnings in the present economic environment to meet these onerous obligations, failing which our net international reserves will suffer depletion.

The opinions of economists on the length of the global crisis are varied and the budget proposals seem to adopt a “wait and see” approach. The question now to be answered is, “in the absence of significant measures in this year’s budgetary proposal, are those previously presented sufficient to weather the global economic storm?”

Budget commentary



Taxes

Corporation Tax

Taxation of dividends

Barbadian resident companies, including international business companies, will be exempt from tax on dividends derived from a “substantial shareholding” in an overseas company.

Dividends paid by a Barbados resident company to non-resident shareholders out of foreign source income will be exempt from Barbados withholding tax.

Comment

The above exemptions were previously granted by way of amendments to Section 9(1) (1) (ii) and (iv) of the Income Tax Act in 2007.

Creative economy

Draft legislation will be prepared to provide for exemptions from corporation or income tax and import duties for cultural practitioners and approved corporate, governmental and other entities. These concessions will extend to projects designed for heritage development and preservation.

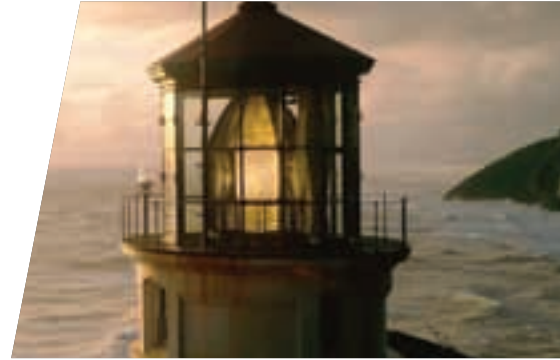
Comment

The Prime Minister must be commended for introducing measures to stimulate growth in the cultural sector.

Charitable donations

At present, in order to obtain a tax deduction for charitable donations, the donor must make the payment to an organization that is registered as a benevolent organization and the payment must be made by way of covenant for a period of at least three years. It is proposed that:

Budget commentary cont'd



- ▶ the requirement for a covenant be abolished so that receipts in respect of donations would suffice for the purposes of obtaining a tax deduction for donations made;
- ▶ donations may be made in either cash or property;
- ▶ the definition of a benevolent organization be amended to include other organizations or entities that will be listed in a Schedule to the Income Tax Act;
- ▶ the benevolent organizations may be approved as such by a letter from the appropriate Ministry and will not need to be registered with the Corporate Affairs and Intellectual Property Office (“CAIPO”) to be treated as such;
- ▶ large donations of over BDS\$1M should be carried forward for five years and there should be a restriction in the amount that may be claimed each year as a donation.

Comment

The abolition of the covenant regime and its replacement by the use of receipts, as well as the removal of the requirement for benevolent organizations to register with CAPIO certainly are welcomed changes. These changes will assist charities in raising financing as the process for being treated as a benevolent organization will be simplified. The easier access to the tax relief available to donors may also encourage more donations. We have noted that donations of both cash and property will be permitted as deductible donations. The method of valuation of properties will need to be addressed in order to avoid abuse.

Income Tax

Currently, individuals who are resident but not domiciled in Barbados are taxed on income derived from Barbados as well as any foreign source income that is remitted or deemed remitted to Barbados. It is proposed that such individuals will qualify for the foreign currency earnings credit in respect of any foreign source income that is remitted to Barbados, even where the individual becomes domiciled in Barbados. This will reduce the effective rate of tax paid by such individuals.

Comment

It is hoped that this proposal will encourage high net worth individuals that are currently resident in Barbados to become domiciled in Barbados, rather than to relocate to another jurisdiction. It may also provide an incentive to Barbados nationals living abroad to return to Barbados.

Budget commentary cont'd



Other measures

Holding company regime

The Property Transfer Tax Act and the Stamp Duty Act will be amended to exempt Barbadian and non-Barbadian vendors and purchasers from these taxes on any transfer of the shares of a “holding company”. A company will be treated as a “holding company” where its assets consist wholly of foreign shares or securities or other foreign assets and its income is derived solely from sources outside of Barbados.

It is also proposed that holding companies will be exempt from exchange controls as is the case of international business companies and regular Barbados companies engaged in international business.

Comment

The Prime Minister must be commended for introducing this proposal as it will enhance Barbados’ legislative framework to enable the development of Barbados as a suitable jurisdiction for the establishment of holding companies.

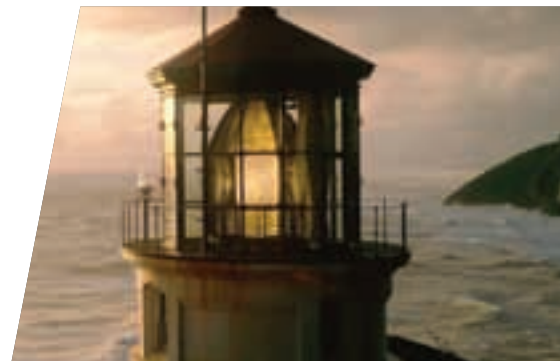
It is noted that the proposed exemption from PTT and stamp duty will not be extended to the disposition of the shares of a Barbados company that has local investments. Therefore, PTT and stamp duty at the rate of 2.5% and 1% respectively of the market value of the shares transferred will continue to apply.

The proposal to extend the exemption from exchange control regulations to holding companies will help to position Barbados as a leading holding company jurisdiction.

International Trusts Act

The International Trusts Act (“ITA”) will be amended to allow for the creation and regulation of private trust companies. The ITA will also be amended to include a definition of “trust business” to enumerate the services that may be provided by service providers

Budget commentary cont'd



who provide trust services. The ITA will also provide for the central registration of all international trusts. Guidelines will be provided in the legislation for the licensing of trust companies and the identification of the principals involved in transactions.

Comment

Currently, the trustee of an international trust is required only to file certain documents with the Ministry responsible for International Business. These documents are confidential and are not available to the public. Further, under the provisions of the ITA, international trusts are exempt from the requirement of registration under any law.

The proposal for the registration of international trusts and the regulation of persons who provide trust services represent a step in the right direction as this will ensure that Barbados is seen as a well regulated jurisdiction that adheres to international standards and has transparent laws. This was instrumental in Barbados' removal from the OECD black list in 2001. However, this proposal may deter high net worth individuals who prefer anonymity from establishing a trust in Barbados.

Barbados Financial Services Commission

While the Central Bank will retain regulatory oversight for the banking sector, a Barbados Financial Services Commission will be established in the first quarter of 2010 to regulate all domestic and international non-banking business activity.

Comment

To the extent that the centralization of regulatory oversight will improve the efficiency of the authorities in conducting their activities, this proposal is welcomed.

Business facilitation

Persons with Government contracts who have proven that they have satisfactorily performed their services will be able to speed up collection of up to 90% of amounts due to them by virtue of a proposed scheme. Under the scheme, such persons can factor their receivables with commercial banks who then discount these advances with the Central Bank. The Central Bank may enter into such arrangements for up to BDS\$15M.

Budget commentary cont'd



Comment

It is evident that the objective of the proposal is to relieve the cash flow constraints suffered by small businesses whose main source of business is Government contracts. While the objective is laudable, it is left to be seen whether access to this facility will be fraught with bureaucratic red tape that will eliminate any chance for the satisfaction of the objective of the proposal. Also, one wonders whether the costs associated with this facility will outweigh the advantages to be derived there from.

Merger of funds

Some of the Government funding agencies will be merged such as FundAccess, the Enterprise Growth Fund Ltd., the Industrial Investment Employment Fund and the Innovation Fund.

Comment

It is hoped that the above proposal to merge the various funds will permit the streamlining of the processes related to access to the funds.

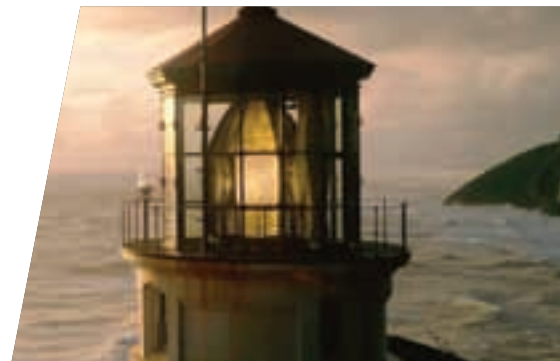
Saving jobs and national insurance

In an effort to save jobs, the Prime Minister proposed that, for employers experiencing cash flow problems associated with employing more workers than required during the business downturn, a loan from the National Insurance Scheme ("NIS") would be made available to such employers. This loan would be valued at one year's employers' NIS contributions, would bear interest at a rate of 3% per annum and would be repayable over five years. To qualify, employers would have to be compliant at 30 June 2009 and would have to commit to maintain the current level of employees for the duration of the loan. The funding for such loans would come from the Unemployment Fund.

Comment

While this source of additional loan funding is welcome and job levels would be maintained, one must question if it would be sufficient to meet employers' cash flow

Budget commentary cont'd



requirements in the long-term, as the current level of employment must be maintained and the duration of the economic recession is unknown.

Waiver of penalties and interest

Government announced that it had already introduced a programme of relief to employers and self-employed persons by way of a waiver of interest and penalties on outstanding national insurance, income tax, land tax and value added tax.

The quantum of the waiver is one-half of the total penalty and interest owed on the unpaid contributions or taxes.

There are certain criteria which must be adhered to in order to qualify.

Comment

While these programmes have been instituted for several months, no mention was made of the statistics to date on the number of persons opting for the waiver programmes and the value, in dollar terms, of such waivers to the Government.

The Shipping (Incentives) Act

The Shipping (Incentives) Act will be amended to provide for customs duty concessions to any company engaged in commercial shipping and boating in the tourist industry for a period of up to 15 years. These concessions will be available on fishing rods and reels, safety equipment, satellite navigational systems, depth sounders, VHS, SSB and AM radios.

The Shipping Corporation Act

The purposes of the Shipping Corporation Act will be extended to include the registration of incorporated and unincorporated bodies and the Act will be amended to remove the restriction that a director may not be a resident of Barbados. Further, a shipping corporation that is incorporated in a foreign jurisdiction will be allowed to be registered in Barbados as an external company.

Budget commentary cont'd



Comment

It appears that the suggested amendments will lead to greater flexibility in the legislative framework surrounding shipping companies. However, it is left to be seen whether these amendments will have the desired effect of encouraging such business.

Indirect taxes

VAT on automobiles

Effective 1 July 2009, the rebate of excise tax paid by importers of new cars will be increased from 15% to 20%.

Comment

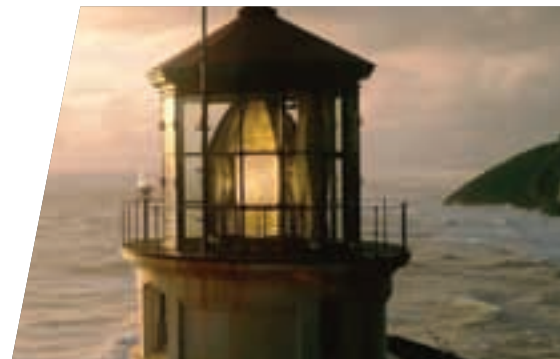
The increase in the rebate of excise tax that is available to new car dealers will result in a reduction of the overall duties and taxes on these vehicles. However, it is felt that this reduction is not significant enough to have the desired impact on new car prices and by extension, new car sales.

We understand that one of the concerns of new car dealers is the current chargeable value for the imposition of import duties and taxes. However, if consumers are to benefit from relief granted to the industry a comprehensive review of the current excise tax structure should also be undertaken.

VAT on building materials

The threshold in respect of the refund of VAT on building materials on a house costing not more than BDS\$400,000 is increased from BDS\$150,000 to BDS\$200,000. This refund is available only to first time home owners who reside in the home constructed. First time home owners wishing to benefit from the VAT refund will not be subject to a maximum family income limit.

Budget commentary cont'd



Comment

The restriction lifted on the maximum family income limit may have eased the administrative burden associated with the application of this concession by and may have increased the number of persons who would qualify for relief. This is a positive development in view of the high cost of constructing homes.

VAT on locally produced arts & crafts

It is proposed that VAT be removed from locally produced art and craft sold in customs-controlled environments such as the Grantley Adams International Airport and the Bridgetown Port.

Comment

It is unclear whether this concession will be available for vendors selling locally produced art and craft in duty-free establishments outside of the ports of entry.

In-Bond Scheme

Companies registered on the in-bond scheme will have their bond liability reduced from 30% to 5%.

Comment

With a movement to a single in-bond scheme regulating duty-free shopping as opposed to the two-tiered drawback/in-bond schemes that previously existed, persons entering this scheme will not now have to pay duties and taxes on their imported goods. The reduction of the bond liability is additional relief.

Water Rates

All water rates will be increased by 1 July 2009.

Comment

The proposed increase in water rates will not only affect Barbadian individuals but will also increase the cost of doing business in Barbados. This is really counterproductive given our objective of attracting businesses to Barbados.



Gun and drivers' licences

Effective immediately, a two-tiered licencing structure will be introduced for each gun licenced. First time registration will attract a fee of BDS\$500 and an annual renewal fee of BDS\$200 will be applicable. The annual fee represents a significant increase as the fee previously was BDS\$50.

Effective 1 January 2010, all persons 65 years and over will pay BDS\$25 annually for the renewal of their drivers' licences. This is a reduction from the BDS\$50 previously paid.

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Fair value accounting



Fair value accounting, as currently required for certain financial instruments, may be the most transparent way to reflect the economic reality of prevailing market conditions and provide investors and companies with current financial information on which they can base investment and management decisions. However, applying fair value to financial instruments in illiquid and inactive markets is highly challenging and efforts to improve its use should continue.

Fair value accounting provides a contemporaneous measure of value. It seeks to assign a value to assets based on the price they would receive if sold in the current market. This is central to the primary purpose of financial reporting because it is investor-oriented. It is intended to provide investors with the transparency necessary to make informed investment decisions.

Fair value accounting has been criticized by some as having contributed to the current financial crisis -- some say it may have exacerbated it. Certain governments and industry representatives have called for its suspension, arguing that fair value creates a downward, pro-cyclical spiral, causing particular hardship to banks because of its interaction with regulatory capital requirements. However, in its January 2009 report to Congress the US Securities and Exchange Commission found that fair value accounting did not play a 'meaningful role' in the failure of banks in the United States.

There are differing views about how fair value accounting might be improved, and the standard setters have a number of projects under way to deal with the challenges.

Fair value accounting helps to keep investors informed about the current financial condition of a company.

Fair value accounting, when supplemented by appropriate disclosures, is one of the best ways to give investors the most transparent picture of the value of a reporting company's financial instruments as they reflect current market conditions. Because it requires companies to reflect market volatility in their valuations, fair value accounting can cause pain in a downturn. And, in the extraordinary market conditions we are facing, when even very deep markets have become illiquid, some companies may be seeing surprisingly low asset valuations, particularly in light of how much they paid for the same assets even just a short time ago.

But fair value accounting enables investors, management, creditors and policymakers to recognize problems or opportunities on a timely basis so they can make informed investment or other decisions and take appropriate corrective actions. Any fundamental change to fair value reporting runs the risk of reducing confidence among investors and other market participants, which in turn would further restrict the flow of capital.

That said, applying fair value to financial instruments in illiquid and inactive markets is highly challenging and more guidance could be useful. Fair value works best when there is a market price to value assets and liabilities - a relatively straightforward task when there is an active market. In an illiquid market, where there is no market price, preparers must exercise a significant degree of judgment. In these circumstances, we as auditors, often assisted by our experienced valuation professionals, also must exercise a significant degree of judgment in auditing the company's determinations. At the same time, it is very important that financial reports make comprehensive disclosures about how the valuation has been done, including the important assumptions and rationale underlying the determination.



Fair value accounting can likely be improved and made a more effective tool in financial reporting.

There are a number of ongoing projects designed to find ways in which fair value accounting might be improved, particularly in light of the difficulty in applying fair value in illiquid markets, which the financial crisis has highlighted, as well as some of the anomalies that fair value accounting can produce. For example:

- ▶ The Financial Accounting Standards Board (FASB) has proposed two new staff positions (FSPs) that respond to recommendations made by the SEC in its December 2008 report to the US Congress. One FSP is aimed at providing additional guidance on determining fair value in illiquid or inactive markets. The second FSP would amend the determination and measurement of an 'other than temporary impairment' such that, in certain circumstances, only the portion of impairment attributable to credit losses would be recognized in earnings, with the remainder recognized as part of 'other comprehensive income'.
- ▶ The International Accounting Standards Board (IASB) is seeking views on the two FASB proposals. It has not as of yet proposed amendments to International Financial Reporting Standards (IFRS) as a result of the FASB proposals, and any changes that may be proposed following the feedback are expected to be through due process.
- ▶ The IASB has recently issued an amendment requiring additional disclosures concerning the fair value of financial instruments, in part adopting disclosures already required under US GAAP. The IASB is also in the process of providing further guidance on how to assess fair value.
- ▶ The IASB has said that it wants to propose a new simpler financial instruments standard for consultation in the next six months, rather than continue to patch up its existing one.
- ▶ The IASB and the FASB have set up the Financial Crisis Advisory Group, bringing together experienced business and government leaders, to help consider fair value and other financial reporting issues arising from the financial crisis.

In summary, fair value accounting is accused of being pro-cyclical -- both in periods of growth and in a downturn. This is because, when assets are marked to market, rising prices will reflect the upward movement of the market and declining prices reflect its downward movement in a cyclical fashion. Fair value accounting can appear harsh when prices are going down; yet no one complains when asset values are rising. ***However, fair value accounting is in fact reflecting market behaviour, not causing it.***

The use of fair value measurement in financial reporting is finely balanced between, on the one hand, the provision of information that is reliable and understandable and, on the other hand, the provision of information that is potentially misleading and confusing to the investor. After all, financial reporting is ultimately about communication and decision-usefulness – both for internal management and external investor purposes.

Floating to the top: Market downturn recovery



The Caribbean and Latin America will recover more quickly from the global crisis relative to the Advanced countries - that was the general pronouncement made by the International Monetary Fund (IMF) in its May 2009 Regional Economic Outlook. Many business executives may digest this bout of optimism for the regional economy with a sigh of relief but in fact should take it with a grain of salt and remain focused on strategies of survival and longevity for their companies.

Based on this IMF report, a turnaround seems to be looming but when exactly is it going to happen? This uncertainty presents a level of risk that makes it important for executives to assess the available information and develop likely scenarios that the company could be faced with. Reaction to economic upheaval may be as varied as there are options available. Executives may choose to do nothing and ride the wave and hope not to be consumed; whilst others may try to jump on every wave available. A downturn presents many opportunities to surpass the competition; however without your company's own sound footing it may be difficult to gain traction in the race.

How should executives tackle the effects upon their businesses of this downturn? That, of course, is no easy question - this article, based on a report produced by Ernst & Young Globally, provides an overview of a few strategies that should yield some success and also highlights key areas that may be considered in an attempt to devise and implement new and bold strategies. These strategies may not only lead to a company's survival, but ensure that it emerges from the present economic turmoil a stronger, more competitive and focused entity.

The starting point is cash

The primary short-term goal in a credit crisis must be cash. Ernst & Young utilises a stress pendulum that focuses especially on the issues of cash. Executives and their advisers have to determine where on the pendulum their businesses lie.



If you are burning cash during a credit crisis, your priorities are clear. If you are generating cash through operations, the opportunities are many.



A time for speed: securing your present

Working capital is the lifeblood of a company, and the ability to manage it becomes even more important in a downturn due to falling revenue and restricted access to new funds.

Companies should look for opportunities to manage its working capital by reviewing credit terms of both receivables and payables. This advice is age old but still is, for good measure, worth reiterating. Offering customers innovative financing packages to trigger sales and increase revenue may also be a viable consideration depending on a thorough credit risk assessment.

Divesting non-core or underperforming units or assets, including real estate, could also be beneficial. These assets may severely affect the company's performance during a downturn and now may be the time to consider parting ways. The rule of thumb for many Barbadians is that real estate only appreciates; however, many businesses may very well be better off utilising that cash from sale to increase or streamline its operations. The same can be said for non-core businesses which take up vital resources and funds and though may very well be profitable may not be to the level of core operations. These divestitures can supply a company with much needed cash and during periods of economic downturn where credit is scarce; companies with large quantities of cash are actually viewed positively by investors as they are seen as being more stable investments which are less risky due to a perceived lower level of credit risk.

While partial divestiture may be the most prudent strategy for companies trying to bolster their cash position, studies have shown that an awareness of a company's position in its market as well as the position of its competitors can produce tremendous results for companies that have access to cash.

A time for knowledge: protecting your assets

Ready access to credit for many companies have noticeably impacted the purchase and sale of assets and by extension their prices; prices that are now severely depressed because of a lack of credit in this current crisis. Many corporate leaders admit to being surprised by the economic downturn. In many instances, this surprise stemmed from inadequate risk management systems to protect assets and operations. Companies either did no risk management or, if they did, it was done on an ad hoc and incomplete basis. Risk Management should not simply be a tick on the corporate compliance checklist but rather management with trusted advisors have to be alert and nimble, prepared to define and monitor risk appetite and tolerance.

What is needed in many companies is a new approach to assessing the potential risks that now present themselves. This will ensure processes are in place to flag issues early, with the ability to identify opportunities as the dark clouds are parting, whether related to strategic growth or operational cost-reduction.

A time to perform: improving your performance

Management should always be seeking to maximise the effectiveness of its operations, but in times of broad economic growth and profitability, this goal can sometimes be downplayed against other worthy goals of achieving market and reputation share, strengthening client relationships or long term strategic positioning. In the current market conditions, however, improving performance effectiveness becomes critical to business survival.



The need for performance improvement has never been more urgent. For most, the immediate reaction is to cut-costs as those measures have always been at the top of the to-do list in a difficult market. However, the risk of reduced effectiveness is ever present and these measures are frequently only a short-term solution. Still, pressured to adjust to harsh market conditions, executives are very tempted to look toward quick-fix alternatives. Companies that emerge from crises continue to have their eye fixed on their long-term strategic objectives.

By carefully observing the operational and financial position of competitors, especially those lacking the financial security to survive the recession, willing targets for takeovers may be identified. Such strategic analysis is a necessity and it takes advantage of reduced valuations which are common during recessionary periods. This not only removes some of a company's competition and increases its market share but it can also produce operational savings.

A time for change: reshaping your business

The impact of the market changes has clearly been significant, resulting in considerable financial damage to several businesses and drastic changes to some business models. Management must take action to change its operations and assets to reflect its new world and prospects.

In response to the economic crisis, companies may be tempted to put aside long-term strategic plans and opt for what seem to be quick-fix solutions in an attempt to deal with burning issues. Businesses that emerge strengthened from the current crisis will be those that reshape intelligently, not those tempted to move quickly to extract additional value.

A time to be bold: sustaining your future

While partial divestiture may be the most prudent strategy for companies trying to bolster their cash position, studies have shown that an awareness of a company's position in its market as well as the position of its competitors can produce opportunities for growth for those businesses prepared to seize the moment, offering businesses the potential to increase market share. By the careful re-examination of business models, the most successful foundations for growth can be created. The development of sustainable business models during a downturn ensures a company's success and makes it well placed to take advantage of new growth opportunities, especially when the economy improves.

Two key themes for a sustainable future are maintain a sustainable business model and taking advantage of opportunistic deals:

- ▶ A successful model will be flexible and scalable to take advantage of opportunities that emerge, adapting rapidly to changes in volume without dependence on large-scale recruitment, training and capital investment. Businesses that are successful in a downturn have absolute clarity of their proposition, strategic direction and brand positioning combined with responsive decision-making. They efficiently combine management information to seize market opportunities, excluding those that do not fit with the strategic direction.
- ▶ Businesses continue to be bought and sold. Intense pressure is bearing down on executives to create the right divestment and acquisition strategies as many sectors consolidate further. Research shows that downturn mergers generate about 15% more value (total shareholder return) compared with boom-time mergers.



A time for action

The only constant in life is change! In times of great uncertainty and stress, there is a temptation to wait and see. Maybe tomorrow there will be more clarity regarding risks, maybe things will have improved and tough decisions can be delayed.

From our perspective, it is necessary to recognise that the crunch has happened and that its consequences will continue to emerge. Past actions can be regretted but they cannot be reversed. The future, however, can be different and that is where management must focus.

The time is now for leaders and executives to:

1. Quickly focus on cash and your exposure to the downturn. The greater your liquidity, the greater your options and your prospects of success. Understand the impact on your clients and your suppliers. Seek to understand the impact on your competitors.
2. Seek to know your situation and your options. Now is the time to be serious about risk management - not as procedural compliance but as the process for evaluating future actions and consequences.
3. Focus on the performance of your team and your assets. When markets are tough and resources are scarce, this is the time to make certain that you are achieving both efficiency and effectiveness gains. Performance is relative - for even the most distressed of companies.
4. Focus on driving the changes in the organisation. Match the changed environment that we have entered and deliver the performance that will shape the market of the future.
5. Be bold about the opportunities that do exist. Fundamentally change the competitive position of your organisation to not just survive the economic downturn but to thrive and build a position to rebound when conditions change.

International tax developments: Impact on Barbados



Recent developments in the international tax arena have once again created a level of uncertainty in relation to the future of international financial centres. This uncertainty has been triggered by the onset of the current worldwide economic crisis which has prompted the Organisation for Economic Cooperation and Development (“OECD”) and a number of Governments to adopt certain tax measures and policies which are likely to have a significant impact on international financial centres. This article will examine some of these measures and policies that have been the causes of the recent uncertainty and outline the possible impact on Barbados.

The OECD

In 2002 the international business and financial services sector in Barbados breathed a sigh of relief when it was announced that this island was not considered a “tax haven” by the OECD due to its policies with respect to exchange of information and its transparent tax and regulatory regimes. On 2 April 2009, the OECD issued an updated list of countries which either meet or do not meet the internationally agreed standard for the exchange of information. The OECD determined that Barbados has substantially implemented this standard so as to be included in its “white list”. However, many of our Caribbean neighbours such as Bermuda, the British Virgin Islands (BVI), Bahamas and the Cayman Islands were not included in the white list, although they have committed to meeting the OECD standard.

The inclusion on the OECD white list may be a feather in Barbados’ cap. This is because some multinationals with insurance or other operations in the above territories that have not been included in the white list may be encouraged to shift their operations to jurisdictions that meet the OECD standard, such as Barbados. However, it must be borne in mind that these non-compliant territories are now swiftly moving towards implementation of the OECD standard. For example, on 17 April 2009, only two weeks after the OECD announcement, Bermuda signed 8 new Tax Information Exchange Agreements (TIEAs). Bermuda now has 15 TIEAs, including an agreement with the United States (US). Therefore, Bermuda now satisfies the OECD requirement for inclusion on the “white list”.

The Cayman Islands similarly signed 7 new TIEAs and now have 8 agreements in place, including a TIEA with the US. In order to speed up the process of implementation, the Cayman Islands has also enacted legislation that allows them to exchange information unilaterally with countries that they choose. In the final analysis, therefore, any advantage enjoyed by Barbados by virtue of its inclusion on the OECD white list in contrast to its competitors, may be short-lived.

While the recent OECD listing may have provided Barbados with a competitive advantage over a number of other competing jurisdictions, this may be reduced to some extent by the legislative proposals and actions of certain Governments, such as the US and Canada.

The Obama tax proposals

Clouds were looming in 2007 when the then Senator Obama co-sponsored a bill which proposed to make changes that would affect “offshore secrecy jurisdictions” (OSJs). On 2 March 2009, Senator Carl Levin reintroduced an amended version of the Stop Tax Haven Abuse Act that will establish certain presumptions and more onerous reporting requirements for transfers of property to or from OSJs.

There are currently 34 countries that are considered OSJs, including Barbados, Bermuda, BVI, the Cayman Islands and Switzerland. Barbados’ inclusion in this list is surprising given that Barbados concluded a TIEA 25 years ago with the

US Government. Barbados also concluded a double taxation treaty with the US many years ago which also provides for exchange of information. This treaty was renegotiated as recently as 2004 and is now accepted by the US as an acceptable treaty so that dividends received by a US shareholder from a Barbadian resident corporation will generally be eligible for a maximum US tax rate of 15%.

If the proposed legislation is passed and Barbados continues to be on the US list of OSJs, US companies and individuals would be less likely to choose Barbados as a jurisdiction through which to conduct business, due to the attendant reporting obligations. This has occurred in Bermuda where some US companies have already changed their domicile to Ireland and Switzerland as a result of the pending legislation.

There are other proposed measures that may also indirectly impact on Barbados. On 4 May 2009 US President Obama announced proposals to reform the US tax deferral of overseas income and the check-the-box regulations. At present, a US company that generates active business income abroad is taxed in the US only when the income is repatriated to the US in the form of dividends. However, President Obama has proposed that US companies will be taxed on such income irrespective of whether or not the income is repatriated to the US. In addition, tax deductions will only be allowed when the income has been repatriated to the US.

The Obama proposals also seek to eliminate the US check-the-box provisions that allow a foreign corporation to be treated as a partnership for US tax purposes. Where this election is made, the income of the foreign corporation would not be subject to immediate US tax if it is reinvested abroad. In this regard, Barbados is an attractive jurisdiction for US investors as the Barbados society with restricted liability is a checkable entity for US tax purposes.

These latter proposals are likely to impact on the competitiveness of US companies as these changes are coming at a time when other developed countries, such as the United Kingdom and Japan, are amending their tax legislation in order to make their multinationals more competitive in the international arena. However, Barbados is also likely to be indirectly affected to the extent that there will no longer be the impetus for US investors to utilize entities established in Barbados in order to benefit from the US deferral rules.

Canada

Recent policy decisions by the Canadian Government may also have an impact on Barbados' international business sector. Until recently, the policy of the Canadian Government was that Canadian companies would not be subject to tax on dividends received from a subsidiary resident in a treaty jurisdiction, provided that certain other conditions were satisfied. This is commonly referred to as the exempt surplus regime. However, in its 2007 Budget, the Canadian Government announced its intention to negotiate Tax TIEAs with jurisdictions with which it does not have comprehensive double taxation agreements. It also announced that it would be prepared to extend the application of the exempt surplus regime to dividends paid by Canadian owned foreign affiliates established in such a country once a TIEA was concluded with that country.

On signing its recent TIEA with Bermuda, the Canadian Government extended the exempt surplus treatment to dividends received from companies established in Bermuda, although Bermuda does not levy income taxes and does not have a double taxation treaty with Canada. It is understood that similar TIEAs have been signed, or are about to be signed, with a number of other zero tax jurisdictions, including the Cayman Islands, that are direct competitors to Barbados.

This situation poses a challenge to Barbados' current competitive advantage in the Canadian market over zero tax jurisdictions such as Bermuda. However, with the signature of the TIEA with Bermuda, there is a concern that Canadian companies with subsidiaries in Barbados will move their operations to Bermuda to take advantage of the zero tax rate.

Conclusion

Although the developments highlighted above will pose a number of challenges for the Barbados international business and financial services sector, it should be borne in mind that there are a number of benefits of doing business in Barbados that are attractive to international investors. Firstly, Barbados' reputation has remained untarnished on the international landscape over the years. Secondly, Barbados has concluded 18 double taxation treaties, as well as a number of bilateral investment treaties, and is currently in the process of expanding its tax treaty network. These treaties offer investors reduced withholding taxes, certainty of tax treatment and investment protection. Finally, Barbados offers investors access to a pool of high quality human resources which facilitates the establishment of active businesses which require a large number of employees.

In conclusion, even though the outlook for the international business sector in Barbados is uncertain, there are many reasons to suggest that the benefits that Barbados has to offer to investors, some of which are highlighted above, will enable it to continue to be competitive despite the challenges that lie ahead.

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Country Managing Partner and International Tax Partner

Ben is the Country Managing Partner for the Barbados office of Ernst & Young Caribbean. He is also an International Tax Partner and leader of the firm's International Business industry group. With over 20 years experience in the tax advisory field, he specialises in advising clients on Barbados tax issues as well as international tax matters.

A frequent speaker on international taxation matters both in Barbados and overseas, Ben has also written articles on international tax issues for a number of international tax publications. Some of Ben's professional responsibilities and experiences include:

- ▶ Member of the CARICOM Working Group on Fiscal Policy
- ▶ Member of the Barbados Council of Economic Advisers
- ▶ Member of the Joint Policy Working Group
- ▶ Chairman of the Board of Directors of the Barbados Private Sector Association
- ▶ Member of the United Nations Committee of Experts on International Cooperation in Tax Matters

Maria Robinson, BBA, CA

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Maria is a partner in our Tax Advisory Service Division. She has spent 18 years working in the professional services field, with over thirteen years of Tax experience. She holds significant experience providing advice on tax planning for regional and international corporate clients particularly in the financial and hospitality industries for clients based in Barbados and the OECS.

Over the course of her career Maria has developed a keen appreciation for the tax implications pertaining to mergers and acquisitions and reorganizations, at the local, regional and international levels. She is a Member of the Institute of Chartered Accountants of Barbados (ICAB), a Member of the Tax Committee of the ICAB and a Member of the Institute of Chartered Accountants of Nova Scotia, Canada.

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Wade is the regional service line leader for Tax & Corporate Services. He has overall responsibility for coordinating these services to clients throughout the Caribbean. He specialises in the area of corporate international tax advisory services and his experience includes a three and a half year assignment with Ernst & Young's International Tax Services Group in New York. Wade has considerable experience in developing and implementing tax minimisation planning structures in Jamaica, Trinidad & Tobago and Barbados; including mergers and acquisitions, green-field projects, and capital markets transactions. He has been involved in tax engagements for a variety of multinational clients of the firm.

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Allison is a Canadian Chartered Accountant with over 17 years of experience preparing and reviewing tax provisions for various clients. She has also provided tax advice and implemented complex tax strategies for several European, US, Canadian and Caribbean firms and has experience in dealing with derivative products and structures for international financing and capital markets.

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Dominique joined Ernst & Young Caribbean in 2001 and holds a Masters degree in Taxation from the Universite de Sherbrooke in Canada. Before relocating to Barbados, she worked in a professional services firm as a Senior Tax Advisor in Canada. She has been trained in corporate reorganizations and has in-depth knowledge of the Canadian taxation system. Since joining Ernst & Young, Dominique has been involved in advising clients on the international tax aspects of structuring their investments in the Caribbean.

Mark Shorey, BDMS
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Mark is a seasoned tax professional with over 40 years of tax experience. He worked with the Barbados Customs and Excise Department for over 25 years, followed by 15 years in a major professional services firm, where he was responsible for the delivery of VAT compliance, indirect tax and world trade services in Barbados and the Eastern Caribbean. Mark also specializes in customs classification and valuation and other customs advisory services.

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Marilyn has spent 11 years working in the professional services field. She has experience in the provision of Barbados personal tax services and corporate tax compliance services to clients based in Barbados and the OECS. She is a member of the Institute of Chartered Accountants of Barbados and a fellow of the Association of Chartered Certified Accountants.

Toni Jackman, CGA
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Toni has worked in the Barbados office of Ernst & Young for several years. She has extensive experience primarily in the areas of corporate and personal tax compliance, providing tax services to clients operating in various industries in the local and International Financial Services Sectors.

She is a Member of the Certified General Accountants Association of Canada and a Member of the Institute of Chartered Accountants of Barbados.

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Eugene has spent 12 years working in the professional services field. He has extensive experience in the provision of personal and corporate tax compliance services in Barbados and Trinidad and Tobago; including at least four years at the Board of Inland Revenue in Trinidad.

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