

The Special Economic Zones Regime

Part I – Tax concessions

- **The Special Economic Zones (SEZ) Act, 2016 came into effect on August 1, 2016**
- **Developers and occupants of SEZ to pay income tax at 12.5% or as low as approximately 7.5% if they qualify for certain tax credits**
- **No Customs duty on imported items**
- **No General Consumption Tax (GCT) on imported and local purchases of goods and services**

The SEZ Act, 2016, which repeals the Jamaica Export Free Zone Act, was enacted since February 15, 2016, but only came into effect on August 1, 2016.

On a whole the SEZ regime provides a wide range of tax concessions for entities entering that regime but the stringent investment and share capital requirements may prove to be a barrier to entry for some investors.

This publication covers the main tax concessions available to entities in the SEZ regime, while Part II will address issues relating to the transitioning of Free Zone companies to the new regime and the new stringent investment requirements.

What is a SEZ?

A SEZ is a geographical zone which is designated for economic activity.

There may be general and specialized zones. A specialized zone is one limited to specific economic activity such as maritime or aviation related zones.

A single-entity zone, is a zone whose activities are limited to one business entity. They are generally prohibited, unless the Minister directs otherwise in the public interest. *Such zones are similar to the “stand alone” Free Zones currently in existence.* Specific factors, listed in the

SEZ Act, may be considered by the Minister before allowing the approval of single-entity zones. It can be said that these factors seek to assess whether the area surrounding the proposed single-entity zone, has the infrastructural and other capacity for expansion or “building out” into a wider economic zone.

What entities can participate in the SEZ?

The following entities can participate in the SEZ:

- (i) The developer;
- (ii) The occupant; and
- (iii) The zone user.

In essence, the developer develops, constructs, operates and markets the SEZ under an agreement with the Zone Authority. The occupant carries out business in the SEZ under an agreement with the developer and the zone user, performs activities or services in a SEZ with the authorization of the Zone Authority.

A business which existed outside of the Zone, prior to the implementation of the SEZ Act, is prohibited from transferring or reestablishing inside the Zone, as a developer or occupant, for a limited period. The period of the prohibition is 10 years from August 1, 2016.

Do developers and occupants enjoy income tax relief?

Low Corporate Income Tax rate

The corporate income tax (CIT) rate for these entities will be 12.5% (i.e. half of that applicable to ordinary unregulated companies). This rate can be effectively reduced to approximately 7.5% by the following tax credits:

- a. Employment Tax Credits (“ETC”) This is capped at 30% of the entity’s CIT liability on trading income;
- b. Promotional tax credits in respect of Research & Development costs and training costs. This tax credit is capped at 10% of the taxable income from operations in the SEZ.

KPMG Comment:

Under the Fiscal Incentives (Miscellaneous Provisions) Act, entities which qualified for special incentive regimes (e.g. Hotel Incentive regime) were prohibited from claiming ETC. The availability of this credit to developers and occupants in the SEZ is a direct departure from the general tax policy and reflects the special treatment that the government has given to this sector which should underpin the logistics hub.

Tax free rental income

As a further income tax relief, the developer and occupant are exempt from tax on the income from the rental of property in the SEZ, unless the tenant is a connected party.

KPMG Comment:

ETC is ordinarily capped at 30% of the taxpayer’s tax liability on trading income. However, under the SEZ regime, rental income can be included in the total trading income of the occupant or the developer when determining the 30% limit. This is another departure from the ordinary tax policy on ETC in favour of the SEZ entities.

No withholding tax on dividends

Dividends paid by occupants to Jamaican residents or non-residents, out of profits of a trade, business or profession conducted in the SEZ, are subject to withholding tax at 0%.

Similarly, dividends paid by developers to Jamaican residents and non-residents out of the profits of the abovementioned activities in the SEZ are subject to 0% withholding tax. However, dividends paid by developers out of exempt income (e.g. rental income) do not enjoy this concession.

Under the SEZ Act, there is “a 0% rate of tax on dividend income derived from shares held by the developer and occupant”. This may be a typographical error as the result is that the developer and occupant earns tax-free dividends from their shares in other companies. The correct wording may be that the 0% rate applies to dividend income derived from shares in the developer and occupant.

KPMG comment:

Based on the above, although the developer and occupant has no obligation to withhold tax on dividends paid, the recipients may still be required to pay tax on the dividends when they file their tax returns in Jamaica. This is because such dividend income, earned by persons other than developers and occupants, are not income tax exempt based on the current wording of the amendment to the income tax law. The Jamaican resident recipient, may have to pay income tax at 15% on same upon filing his/its income tax return. As mentioned above, this result may not be the intention of the tax authorities, but further adjustments to the legislation may be necessary to achieve tax free dividend income for investors in the SEZ regime.

In the interim, investors may seek to utilize creative tax structuring measures to achieve tax efficiency on dividends.

It is further noted that dividends from the occupant or developer are the only type of distributions that qualify to be paid without withholding tax. This would mean that if a foreign company registered a branch through which to operate in the SEZ, its repatriated profits (e.g. branch remittance which are distributions) would not qualify for tax-free treatment. Such distributions would be subject to withholding tax at the standard rates (i.e. 33 $\frac{1}{3}$ % unless reduced by a Double Taxation Treaty). We do not believe, that this was the intention of Parliament as, based on past tax policy, the tax implications of a foreign owned company operating through a branch vs a subsidiary were virtually the same.

Since the developer and occupant pay dividends subject to 0% tax to shareholders, are they required to claw back the ETC?

The ETC claw back is a regime under which a company which has claimed ETC in a prior year, and which subsequently pays dividends subject to taxation at less than 10%, is required to repay to the government, a certain amount of the ETC claimed (i.e. a "claw back"). This sum to be clawed back is equivalent to the difference between 10% of the dividends paid and the amount of tax deducted from the dividend payment, if any.

Under the SEZ Act, the occupant is relieved from this regime. The developer however, is subject to ETC claw back. Consequently, where the developer claims ETC and subsequently pays dividends at 0%, it is required to pay back to the government a sum equivalent to 10% of the dividend paid.

The claw back sum must not exceed the accumulated ETC claimed by the developer in prior years and the claw back sum is payable as additional corporate income tax.

What Customs duty and GCT concessions are available?

Goods imported into the SEZ by developers or occupants are exempt from customs duty and GCT.

Local purchases of goods and services by developers or occupants, from local suppliers, located outside of the SEZ, are zero-rated. That is, no GCT is to be paid on these purchases. Free Zone companies currently pay GCT on utility services such as telecommunication and electricity services.

What other tax relief is available under the SEZ regime?

Occupants are exempt from Assets Tax, but no exemption is available to developers.

Developers are exempt from transfer tax on the sale of land for use in the SEZ.

There is a stamp duty exemption on instruments for the sale or lease of land by developers to occupants or zone users. A 50% stamp duty exemption is also available on instruments for the purchase, lease or other acquisition of land for use by the developer in the SEZ.

KPMG comment:

It is noted that developers and occupants are not exempt from Minimum Business Tax or Property Tax under the regime.

Does the zone user enjoy any tax relief?

It appears that the zone user, who performs services within the SEZ, is not entitled to any tax relief.

How long is the concession period?

The developer and occupant can enjoy the benefits of the SEZ regime for the duration of their relevant contracts. These contracts can span up to 50 years, but may be extended

Are developers and occupants barred from enjoying other concessions?

Developers and occupants cannot also qualify for tax relief under the following pieces of legislation:

- (i) Bauxite and Alumina Industries (Encouragement) Act;
- (ii) Income Tax Relief (Large Projects and Pioneer Industries) Act; and
- (iii) Urban Renewal (Tax Relief) Act.

In Part II of this issue we will address transitioning matters for existing Free Zone companies and the stringent capital and investment requirements for entry into the SEZ regime.

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